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KAM's initial implementation: An analysis of company complexity, financial health, and debt levels

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Abstract

This study explores factors influencing KAM disclosures by initial implementation auditors, focusing on companies across diverse sectors listed on an emerging country's stock exchange. The findings highlight that company complexity, financial health, and debt levels significantly shape KAM disclosures. Auditor size, opinions, business continuity risks, firm size, and audit rotation periods had minimal impact. This research offers valuable insights into presenting Key Audit Matters in an emerging country with diverse industries, showing that auditors prioritize firms with intricate structures and robust financial performance, often involving complex transactions that lead to more KAMs. Firms with substantial debts face stricter financial scrutiny, reducing the need for auditors to focus on specific audit areas prone to manipulation. Conversely, auditors are more meticulous with companies holding minimal debt, resulting in more KAMs. These findings underscore the importance of tailored approaches in an emerging market, balancing regulatory costs and benefits to enhance economic stability and investor confidence amidst a diverse industrial landscape. The sample stock exchange encompasses 19 industrial sectors and 662 listed companies.

Keywords: Auditor Report, Initial Implementation, Key Audit Matters, Number of KAM, Quantification of KAM.

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1. Introduction

In 2015, the International Auditing and Assurance Standards Board (IAASB) introduced a novel audit reporting standard. This was intended to produce more detailed and transparent auditor reports, fostering increased public trust [1]. The newly introduced standard, International Standards of Auditing (ISA) 701, integrates a section in the auditor's report labeled 'Key Audit Matters (KAM)'. Its goal is to underline the primary concerns of the auditor [2]. An ACCA [3] report, examining 11 countries' initial adoption of this standard, recognized three core benefits: bolstered communication between auditors and governance bodies, more concentrated auditing in key areas, and added motivation for careful financial report drafting, especially in KAM-related areas [3].

By 2020, financial regulatory authorities in an emerging economy emphasized the importance of adopting ISA 701, highlighting a disconnect between their local Audit Standards and the International Audit Standards (ISA). In 2021, the national institute of certified public accountants in this country issued an Exposure Draft representing the adoption of ISA 701, "Communicating Key Audit Matters in The Independent Auditor's Report." The issuance of ISA 701 became highly significant for its implementation due to the existing gap between the audit standards applied within the country. This concern was also highlighted in a survey conducted by the World Bank [4] related to compliance with accounting standards and the assessment of compliance with accounting and audit standards [5].

While previous research has been quite extensive, those regulations were issued earlier than in this emerging economy. Therefore, this research contributes by providing empirical results useful for regulators in countries that have only recently mandated KAM in their audit standards. The financial authorities recognized the need to align local standards with ISA to improve audit quality and prevent potential breaches stemming from audit process opaqueness [6]. This research is an empirical study that shows how factors influence auditors in determining the number of KAMs and including the monetary value of KAMs for the initial implementation.

This empirical research specifically examines how various factors influence auditors in determining the quantity of KAMs and introducing monetary values associated with KAMs for the initial implementation. The study's correlation with country's status as an emerging market underscores the prioritization of developmental approaches, balancing costs, benefits, and their impact on the national economy. Moreover, it provides a comprehensive portrayal of the initial implementation of KAM in an emerging economy characterized by diverse industrial sectors, which encompass 19 industrial sectors and 662 listed companies. These contributions not only enrich the understanding of an emerging country' capital markets but also offer valuable lessons for regulatory frameworks aiming to foster transparency and investor confidence amidst diverse industrial dynamics.

As a concrete action in response to existing regulations and phenomena, in 2022, Key Audit Matters (KAM) began to be effectively implemented in an emerging country. Consequently, financial reports in that year were required to include KAM, and this study aims to explore the factors influencing auditors in deciding the number of KAMs to include and the quantification of KAMs. The inclusion of KAM in the auditor's report is anticipated to enhance the value and relevance of the report for various stakeholders, from investors to governments. This information will provide clearer insights into audit focal points, ultimately increasing the communicative value of the report by providing better transparency in the audit process for its users. KAM facilitates improved understanding for investors. According to an ACCA report, 89% of investors read the auditor's report before the financial statements. Therefore, KAM makes it easier for investors to identify risks, take action, and address issues.

However, while the original ISA 701 by the IAASB lays out the significance of KAM, it doesn't provide sample KAMs to prevent generic reporting. Nor does it specify a KAM quantity, only suggesting that at least one KAM should be included [7]. Given this ambiguity and the reliance on professional judgment for KAM disclosures, this study zeroes in on the underlying processes and factors dictating KAM disclosures in audit reports. Leaning on Hogarth [8] disclosure theory on information assimilation, the research inspects the influences on auditors' KAM disclosure decisions. Previous studies by Pinto and Morais [7] and Genç and Erdem [9] argue that these decisions are shaped by the auditor, the environment, and the audited entity itself. Furthermore, Zhai, et al. [10] suggest that KAM disclosures reduce information acquisition costs.

Key Audit Matter (KAM) is a relatively new concept in Indonesia as an emerging country, and its implementation is not widely studied in the country. Unlike some nations that adopted KAM, such as Malaysia, Australia, Thailand, Singapore, Lebanon, and Jordan, Indonesia is still exploring its application. Matta and Feghali [11] said Lebanon highlight the value added by KAM in audit reports, reducing information asymmetry and building trust in accounting. Rahahleh [12] findings in Jordan there is a tendency among audit firms to report industry-specific KAM rather than entity-specific, with a focus on areas like receivables and inventory. Australia adopted KAM comprehensively since 2017, with common disclosures related to goodwill impairment, revenue recognition, and asset valuation [13]. In Thailand, there is a positive correlation between KAM reporting and audit quality, and the complexity of companies significantly influences the number of KAM reported [14]. Overall, the study emphasizes the need for further exploration of KAM's impact and application in the emerging countries contexts.

Therefore, this study is conducted urgently to examine the comparison between the year before implementing KAM and the year after implementing KAM through an analysis in an emerging country (in this case, Indonesia) concerning the implementation of KAM in audit reports, as previously regulated in ISA 701. The study will also explore why emerging countries should participate in adopting KAM and what risks may arise in its implementation. This study seeks to discern the links between the audited entity's variables and the quantity of KAMs in the audit report. These variables encompass auditor size, auditor's viewpoint, enterprise complexity, ongoing risk concerns, firm dimensions, financial metrics, corporate indebtedness, and audit turnover. Analyzing companies across sectors listed on an emerging country Stock Exchange, the research aims to elucidate how these characteristics might sway the volume of KAMs in an audit report, responding to the growing intrigue surrounding the determinants of KAM disclosure.

Despite the wide range of factors and variables being considered, this research has chosen to focus solely on one observation year. The decision to hone in on this single year is strategic, as it marks the maiden year of the initial implementation of the standard. The initial implementation, rife with learning curves and unforeseen challenges, emerges as a state-of-the-art novelty. It offers a unique vantage point to discern the immediate implications and ripple effects of early adoption. Such an approach not only underscores the immediate impacts of this transformative standard but also positions the study at the forefront of understanding the real-time intricacies of its early implementation. This is one of the urgencies of this research, as it is highly relevant to the global audit community that closely observes an emerging country's journey, aiming to gain insights that could be valuable for other emerging economies on a similar trajectory.

2. Literature Review and Hypothesis Development

2.1. The Importance of Key Audit Matters

The complexity of financial statements significantly complicates the audit process, necessitating auditors to assess the risks of material misstatement, a task made challenging by the often generic nature of auditor reports, which fail to convey the auditors' perception of significant risks. The introduction of ISA 701, aiming to communicate Key Audit Matters in the Independent Auditor's Report, particularly for audits of listed entities, seeks to address this by requiring auditors to highlight and explain in a clear, concise, and entity-specific manner the issues they find most significant, including how these issues were addressed and their relevance within the financial statements. Initiated by the International Auditing and Assurance Standards Board (IAASB) to enhance financial report transparency, KAM is seen as a way to enrich the informative value of auditor reports and improve audit quality by bolstering auditor accountability and influence over management. Reid, et al. [15] and Kitiwong and Sarapaivanich [16] state that KAM disclosure not only amplifies auditor influence and independence but also underscores their responsibility and transparency, facilitating a more accurate assessment of the audit process.

2.2. Number of Key Audit Matters

Conveying key audit matters offers supplementary insights to the intended recipients of financial statements, elucidating areas that, in the auditor's judgment, hold paramount significance in the current audit cycle [17]. This communication aims to provide a clearer understanding of both the organization in question and the primary areas management considered during the audit. Yet, some argue that the inclusion of KAM in the report might not induce the anticipated impact, or substantially alter how investors perceive and respond to the audit report. This sentiment arises because some disclosed information is either already known or isn't presented in a manner that truly benefits the user. Such challenges underscore the necessity of determining the optimal number of KAMs for inclusion in the auditor's report.

In Indonesia, a prevailing notion suggests that an excessive number of disclosed KAMs might paint a picture of a company riddled with issues. However, a high count of KAMs doesn't necessarily validate such perceptions, as KAMs primarily highlight the most pivotal aspects of the audit to users. Notably, both domestic and international audit standards do not prescribe a minimum or maximum threshold for KAM disclosures. Consequently, a large or small number of KAMs does not inherently signify positive or negative conditions for the audited entity. Fundamentally, the quantity of disclosed KAMs is determined by various factors, such as the domains commanding the most attention from management, areas vulnerable to significant misstatements, and specific events that considerably influence the audit trajectory.

2.3. Quantification of Key Audit Matters

The inclusion of numerical data in KAM descriptions raises the question of whether it enhances or hinders financial statement comprehension. Yalch and Elmore-Yalch [18] found that people take longer to process information when numerical details are present. Conversely, Ang and Trotman [19] suggest that quantification in narratives adds specificity and precision, thereby reducing reader uncertainty. Based on this, we predict that when KAMs are more readable and provide clearer details, they improve investors' understanding of financial statements. However, Christensen, et al. [20] argue that quantification increases the effort required for encoding and processing information. Similarly, Ong, et al. [21] suggest that quantitative details may overload non-professional investors, potentially reducing their comprehension of financial statements. On the other hand, numerical data enable auditors to present key audit matters with greater clarity and specificity, which can help non-professional investors better interpret financial statements. Therefore, based on prior research, this study explores the impact of quantification on financial statement comprehension.

2.4. Auditor Size

Francis and Yu [22]; Krishnan [23] and Kharuddin, et al. [24] argue that public accounting firms included in the Big 4 tend to provide better audit quality. When talking about the relationship between auditors and clients, Carcello, et al. [25] revealed that the Big 4 maintain more independence in their relationships with clients and tend to report financial information more conservatively. Big 4 auditors tend to have the ability to withstand client pressure and identify non-compliance [26, 27]. Based on this, Big 4 auditors may disclose a number of key audit issues (KAMs) as a means of communicating relevant issues without being subject to the consequences that qualification disclosures can bring. Big 4 auditors are more concerned with audit failures and disclose more KAMs than non-Big 4 auditors, consequently commissioning Big 4 audit firms will likely result in a higher number of KAMs [28-30]. In addition, Big 4 auditors are expected to disclose more KAMs for several reasons, including better experience and expertise to uncover more risk issues, protect their image and reputation that can be damaged through litigation, and maintain audit quality because they have international affiliates [31]

H1.$_{1}$: Auditor size affects the number of key audit matters

H1.$_{2}$: Auditor size affects the quantification of key audit matters

2.5. Auditor Opinion

The primary purpose of ISA 701 is to improve audit reporting decisions by communicating key audit matters (KAM). The KAMs are determined by the auditor's professional judgment and represent the most significant items in the financial statement audit for the current period [2]. Matters in the KAM derived from communication with those responsible for governance include significant risks, management judgments, unusual transactions, audit difficulties, and modifications required to the audit approach. It is important to note that the communication of KAM in the audit report is not intended to express an opinion that may be detrimental to the entity in place of the opinion expressed by the auditor; instead, the inclusion of KAM is intended to assist users of financial statements in understanding the entity and significant areas of management consideration.

Empirical studies on the effectiveness of KAM reform have produced diverse perspectives and reactions. Auditors determine what to communicate in their reports, as well as the format and content of that communication. The primary goal of disclosing key audit matters is to improve the auditor's report by increasing transparency about the audit process. According to International Federation of Accountants (IFAC) [32] Key Audit Matters (KAM) refer to issues that, in the auditor's judgment, were most significant in the audit of the current period's financial statements. These matters are selected from those discussed with governance bodies. The audit opinion, along with the level of transaction or business complexity, serves as a factor influencing the number of reported KAMs. By considering both variables, it is anticipated that complexity may impact the relationship between the auditor's opinion and the number of KAMs, ensuring a clearer understanding of their interaction.

$H2._{1:}$ Auditor's opinion affects the number of key audit matters

$H2._{2:}$ Auditor's opinion affects the quantification of key audit matters

2.6. Complexity of The Company

ISA/BDS 701 states that the number of KAMs can be affected by the size and complexity of the entity. In line with this, Pinto and Morais [7] and Wuttichindanon and Issarawornrawanich [30] argue that based on the characteristics of their companies, more complex companies have many risk areas that lead to the number of KAMs disclosed. This opinion is then supported by the results of research conducted by Fera, et al. [33] which revealed that companies with good governance (not complex) and sustainability tend to disclose less KAM. But in addition to the characteristics of the company, the amount of KAM disclosed also depends on the characteristics of the auditor [34]. Based on previous studies, we assume that auditors will disclose more KAMs and include quantifications (numbers) in the AM descriptions in audit reports of companies that have many (complex) risk areas.

$H3._{1:}$ Complexity of the company affects the number of key audit matters

$H3._{2:}$ Complexity of the company affects the quantification of key audit matters

2.7. Going Concern Risk

The company's ability to maintain its business continuity can be one of the factors considered by auditors in drafting key audit matters. In fact, in essence, auditors have the responsibility to provide judgment if there is material doubt on the entity's ability to maintain its business continuity as stated in the audit standards [35]. Going concern checks are assessed by the auditor to determine whether the assumptions used by the entity are appropriate or not [36]. When there are doubts about an entity's material future viability, such as high levels of leverage or reduced levels of liquidity [37] this is potentially a major audit issue that auditors need to disclose in auditor reports [38]. Conversely, if the client's financial position is fine so that business continuity is not compromised in the future, the auditor is less likely to disclose it as a major audit issue. When business continuity is clearly compromised, the auditor will disclose the KAM in more detail, including the quantification of KAM to clarify potential business continuity risks. Thus, the entity's business continuity risk is expected to have a positive influence on the number of KAM and quantification of KAM disclosed in the auditor's report.

$H4._{1:}$ Going concern risk affects the number of key audit matters

$H4._{2:}$ Going concern risk affects the quantification of key audit matters

2.8. Firm Size

Large-scale enterprises are synonymous with a large number of business lines. The large number of lines of business makes auditors need more time and focus to examine each area of the business due to the high level of complexity. This high business complexity has the potential to encourage auditors to disclose KAM in their audit reports. Empirical research conducted by O'Keefe, et al. [39] states that the audit process is significantly influenced by company size, complexity, and financial indebtedness. In line with this statement, in a study conducted by Pinto and Morais [7] found that the size of the company assessed from the natural log of sales as an explanatory variable had a positive relationship with the disclosure of the amount of KAM. This is supported by ISA/BDS 701, which states that the number of KAMs is influenced by the size and complexity of the entity, the nature and conditions of its business, and the "facts and circumstances of the audit engagement". Meanwhile, in Genç and Erdem [9] findings the relationship between company size and KAM problems disclosed in audit reports is actually negative. The results of the study are said to have confirmed that large companies have more power to negotiate with auditors in terms of audit costs, and they can put greater pressure on auditors to disclose less KAM [9]. Based on the two research references, the researchers predict that the relationship between company size and disclosure of the number of KAMs is positive. As a result, the KAM disclosed by the auditor will be supplemented with a quantification of KAM to clarify how complexity can be a key focus in the audit process. Thus, the relationship between the size of the company and the quantification disclosure of KAM is positive.

$H5._{1:}$ Firm size affects the number of key audit matters

$H5._{2:}$ Firm size affects the quantification of key audit matters

2.9. Financial Performance

The level of financial performance of an entity can predict future business continuity. According to research conducted by Beasley, et al. [40]; Laitinen and Laitinen [41] and Loebbecke, et al. [42] states the company's performance generates high profits, the possibility of defaulting on the entity will be smaller so that it will generally get a fair audit opinion without exception. In fact, they do not need to manipulate financial statements to make a good impression on investors [43]. Conversely, when profitability is low, entities tend to apply various accounting standards in unique ways to structure their financial statements. As a result, the auditor may issue an unqualified audit opinion characterized by an expansion of the scope of the auditor's work and a large number of KAM disclosures.

In research conducted by Pinto and Morais [7] found that entities that have low profitability have a higher potential for failure, thus creating a negative relationship with the amount of KAM. This also resulted in the KAM disclosed by the auditor in the auditor's report being equipped with a nominal value to further clarify the size of the area that the auditor focuses on. Genç and Erdem [9] states financial performance that characterizes the profitability of a company as measured through ROA turns out to have a significant positive relationship with the number of major audit issues disclosed.

$H6._{1:}$ Financial performance affects the number of key audit matters

$H6._{2:}$ Financial performance affects the quantification of key audit matters

2.10. Financial Indebtedness

In order to maintain its reputation for disclosing the findings of risky audit companies, it is predicted that auditors will disclose KAM in large quantities. In general, when the risk of a financial entity is too high, the auditor will examine the company in more detail and thoroughly so that audit efforts and costs increase [44]. Companies with more debt may be in a more precarious financial situation where auditors focus on the most significant matters related to debt repayment capabilities, liquidity risk, etc., thus concentrating on fewer but more critical KAMs.

At first glance, this may seem counterintuitive because companies with higher levels of debt often have more complex financial structures and may be expected to have more KAM. However, it could be that auditors at companies with less debt were more conscientious or conservative in their audit approach. They may choose to highlight more areas as KAMs due to lower risk tolerance thresholds. Alternatively, companies with less debt may have more resources to devote to comprehensive financial reporting, increasing the likelihood of more areas being classified as KAM.

$H7_{.1:}$ Financial indebtedness affects the number of key audit matters

$H7_{.2:}$ Financial indebtedness affects the quantification of key audit matters

2.11. Auditor Rotation

The duration of the auditor's tenure that is too long has the potential to disrupt the auditor's objectivity and encourage the possibility of failure of the audit process, becoming an argument that encourages auditor turnover. The rotation of auditors in the form of partner changes is expected to increase auditor independence, avoid prolonged relationships between auditors and clients, and cause high professional scepticism. As a result, these actions can negatively affect the quality of the audit. The audit style of each accounting firm is different and has its own characteristics that can leave a deep "trace" on the audit report [45]. As a result, the rotation of auditors can directly affect the disclosure of audit reports, including KAM. Minister of Finance Regulation number 17/KMK.01/2008 regarding "Public Accountant Services," Article 3 concludes that rotation in Indonesia is mandatory.

The regulation requires the provision of general audit services for the financial statements of companies to be conducted by a Public Accountant (PA) for a maximum period of three (3) consecutive fiscal years and by a Public Accounting Firm (PAF) for a maximum period of six (6) consecutive fiscal years. The purpose of the mandatory audit rotation in Indonesia is primarily to enhance audit quality. The obligation for rotation, when viewed from the agency theory perspective, which provides an overview of the existence of companies, suggests that companies are better off complying with the regulations governing audit partner rotation. This is because the rotation of auditors may potentially lead to auditors disclosing Key Audit Matters (KAM) as well as their quantification. Therefore, there is a positive relationship between auditor rotation and the disclosure of KAM numbers, with a negative relationship between auditor rotation and the quantification of KAM.

$H8._{1:}$ Auditor rotation affects the number of key audit matters

$H8._{2:}$ Auditor rotation affects the quantification of key audit matters

3. Research Methodology

The population in this study consists of companies in Indonesia listed on the IDX (Indonesia Stock Exchange). The sample was selected using the simple random sampling method. This study utilized secondary data. For this study, two dependent variables were used, namely the number of KAM and the quantification of KAM. The independent variables include auditor size, auditor opinion, complexity of the company, going concern risk, firm size, financial performance, financial indebtedness, and auditor rotation.

This study employed two models or data analysis methods, namely multiple linear regression and logistic regression. The multiple linear regression analysis method is used in the first model because the number of independent variables exceeds two and aims to analyze the effect of all independent variables on the number of KAM variables. The estimated model is as follows:

$$Tot_{KAM} = \propto + \beta_1 auditor + \beta_2 opinion + \beta_3 cmplxy + \beta_4 gcrisk + \beta_5 fncprn + \beta_6 fncidbt + \beta_7 lnasset + \mathcal{U}$$

Additional information:
Totkam = Number of KAM
auditor = Auditor (Big4 and non Big4 auditors)
opinion = Audit Opinion
cmplxy = Number of business segments owned by the company
gcrisk = Going Concern Risk
fncprn = Financial Performance (ratio of net earnings to total assets)
fncidbt = Financial Indebtedness (ratio of net earnings to total liabilities)
auditrot = Audit Rotation
lnasset = Firm Size

While logistic regression analysis is used for the second model because the quantification variable KAM, as the dependent variable, is qualitative and binary—specifically, whether the quantification of KAM is expressed or not—according to Ghozali [46], "Logistic regression analysis is a regression that tests whether there is a possibility that the dependent variable can be predicted by the independent variable." The stages of logistic regression analysis include testing the feasibility of the regression model (the goodness of fit test), assessing the suitability of the model (the overall model fit), and conducting regression testing. The data analysis method used to test the hypothesis in this study is descriptive statistics, which provide an overview of the variables in this study. The logistic regression model is as follows:

$$ln(\frac{Pi}{1 - Pi}) = \propto + \beta_1 auditor + \beta_2 opinion + \beta_3 cmplxy + \beta_4 gcrisk + \beta_5 fncprn + \beta_6 fncidbt + \beta_7 lnasset + \mathcal{U}$$

Additional information:
auditor = Auditor (Big4 and non Big4 auditors)
opinion = Audit Opinion
cmplxy = Number of business segments owned by the company
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4. Result and Discussion

4.1. Descriptive Analysis

Descriptive analysis is used to provide an overview of the variables used in this study. The following are the results of the descriptive analysis shown in Table 1.

Table 1.
Descriptive analysis.

Variable	Observes	Minimum	Maximum	Mean	Std Deviation
Number of KAM	385	0	6	1.2883	0.762
Quantification of KAM	385	0	1	0.8338	0.3728
Auditor Size	385	0	1	0.2909	0.4548
Auditor Opinion	385	1	4	3.9403	0.2682
Complexity of The Company	385	0	13	2.9013	1.8107
Going Concern Risk	385	0	1	0.0649	0.2467
Financial Performance	385	-8.9525	3612.443	9.8155	184.1684
Financial Indebtedness	385	0.0004	698.8981	3.8488	39.5850
Audit Rotation	385	0	1	0.9195	0.2724
Firm Size	385	3.6969	32.3600	15.2795	3.6969

When KAM was first required in the report of independent auditors in Indonesia, it turned out that the KAM that appeared the most was 6, but there were reports of independent auditors who chose not to mention KAM. In addition, based on the research sample, the most complex companies had 13 segments in their segment reports. Based on the results of data processing, it is known that the minimum threshold value of financial performance comes from companies engaged in the infrastructure, utilities, and transportation sectors. Meanwhile, the maximum threshold value comes from companies engaged in trade, services, and investment. Researchers also found that the minimum threshold value of the financial indebtedness variable comes from companies engaged in the agricultural sector, while the maximum value is held by companies operating in various industrial sectors.

Table 2.
Types of company sub-sectors.

Subsector	Frequency	Percent	Cumulative
Various Industries	20	5,19	5.19
Consumer Goods Industry	44	11,43	16.62
Basic Industry and Chemicals	43	11,17	27.79
Infrastructure, Utilities and Transportation	43	11,7	38.96
Finance	43	11,7	50.13
Trade, Services and Investment	99	25,71	75.84
Mining	20	5,19	81.04
Agriculture	30	7,79	88.83
Property and Real Estate	43	11,17	100.00

The objective of this study is all companies listed on the Indonesia Stock Exchange. All companies are grouped into nine business sectors, with the majority coming from the trade, services, and investment sectors.

4.2. Hypothesis Testing Result for Number of Key Audit Matters

Table 3.
Analysis Result: Multiple Linear Regression.

Variable	Coefficient	St. Error	t count	p-value
Constant	0.0422	0.6242	0.07	0.946
Auditor Size	0.0441	0.0818	0.54	0.590
Auditor Opinion	0.2086	0.1539	1.36	0.176
Complexity of The Company	0.0422	0.0218	1.94	0.054*
Going Concern Risk	0.2203	0.2475	0.89	0.374
Financial Performance	0.0003	0.00004	7.28	0.000***
Financial Indebtedness	-0.0008	0.00021	-3.63	0.000***
Audit Rotation	0.0944	0.0969	0.97	0.331
Firm Size	0.0422	0.6242	0.07	0.946
R Squared	0.0268			
F count	28.06			
Sig. F	0.000			

Note: Standard errors in parentheses
*** p<0.01; **p<0.05; *p<0.1.

Financial performance affects the number of KAMs by α=1%, which also indicates a positive relationship between financial performance and the disclosure of the number of KAMs. Companies with higher profits often have more complex business transactions for the following reasons: (1) Companies with strong financial performance may be more likely to make large investments in intangible assets. These assets are often difficult to value and may be more susceptible to manipulation. Auditors need to spend more time understanding these assets and assessing the risk of material misstatement; (2) Companies with strong financial performance may be more likely to have complex revenue recognition methods. This occurs because companies are often involved in various lines of business or have complex sales contracts. Auditors need to spend more time understanding these methods and assessing the risk of material misstatement; (3) Successful companies often expand their business operations through geographic expansion, diversification into new markets or product lines, or engagement in complex financial instruments. This expansion poses new risks and complexities that need to be assessed and addressed by auditors, potentially leading to an increase in the number of KAMs; (4) Companies with strong financial performance may be more likely to engage in aggressive accounting practices. This is because these companies are often under pressure to meet or exceed analyst expectations. Auditors should be more skeptical of a company's financial statements and spend more time looking for potential misstatements; (5) Companies with strong financial performance can attract more attention from stakeholders, including regulators, investors, and the public. This increased scrutiny may encourage auditors to place more emphasis on certain areas of the financial statements and identify additional KAMs to address potential risks and concerns; and (6) Certain industries or jurisdictions may have specific regulatory requirements that mandate reporting certain matters as a KAM. Companies with strong financial performance may operate in industries or regions with stricter regulations, making it more likely to have more KAMs.

The results of this study seem to align with research that has been conducted [9]. However, it is important to note that while financial performance can be a contributing factor, the selection of KAMs ultimately depends on the specific circumstances and risks associated with each company being audited. The auditor's professional judgment and materiality assessment also play a crucial role in determining the amount and nature of KAM.

Financial indebtedness affects the number of KAMs with α=1%. The less debt the company has, the greater the number of KAMs disclosed in the auditor's report. Conversely, the more debt a company has, the fewer KAMs it discloses. Companies with high levels of debt are often subject to stricter financial reporting requirements. These requirements can make it harder for management to manipulate financial statements, which can reduce the need for auditors to focus on specific areas of the audit. For example, companies with high levels of debt are often required to provide more detailed disclosures about their debt obligations. This information can help auditors assess a company's ability to service its debts and identify potential risks of material misstatement. In addition, companies with high levels of debt are often required to have stronger internal controls over financial reporting. These controls can help prevent and detect errors and irregularities, which can also reduce the need for auditors to focus on specific areas of the audit. A company with a history of financial reporting problems may be subject to further scrutiny by auditors, even if it has low debt levels.

Complexity affects the number of Key Audit Matters (KAMs) with α=10%. The complexity of a company or its financial statements can influence the number of KAMs for several reasons: (1) Diverse transactions: Complex entities often engage in a wide variety of business transactions. The greater the diversity, the more areas there are that may have significant audit risks, potentially leading to more KAMs; (2) Challenging judgments: Complex companies may have more areas that require significant judgment, whether in terms of accounting treatment, estimations, or valuations. These judgments can represent significant audit risks and thus become KAMs; (3) Greater uncertainties: With complexity often comes uncertainty, especially in areas like future revenue recognition, contingent liabilities, or complicated tax situations. Such uncertainties may require more intense scrutiny during an audit and can be identified as KAMs; (4) Multiple business units or geographies: Companies that operate across multiple geographies or have various business units may face complexities in consolidating their financial statements. Discrepancies, reconciliations, or inter-company transactions in such scenarios can become KAMs; and (5) Operational complexity: Beyond financial complexity, the nature of a company's operations can introduce audit challenges. For example, a firm with a complicated supply chain might face significant risks related to inventory valuation or recognition, which could be identified as KAMs. Consistent with previous literature, more complex companies have many risk areas that lead to the number of KAMs disclosed [7].

Table 4.
Analysis results: multiple linear logistics.

Variable	Coefficient	St. error	z count	p > |z|
Constant	8.1557	2.5102	3.25	0.001
Auditor Size	0.1724	0.3397	0.51	0.612
Auditor Opinion	-1.7393	0.5984	-2.91	0.004***
Complexity of The Company	0.1316	0.0991	1.33	0.184
Going Concern Risk	-0.0374	0.6579	-0.06	0.955
Financial Performance	0.9232	0.2495	3.70	0.000***
Financial Indebtedness	0.0069	0.0049	1.39	0.164
Audit Rotation	-0.5038	0.5991	-0.84	0.400
Firm Size	0.0249	0.0451	0.55	0.580
Pseudo R Squared	0.0358			
Wald count	19.65			
Sig. Wald	0.0358			

Note: Standard errors in parentheses
*** p<0.01; **p<0.05; *p<0.1

4.3. Hypothesis Testing Result for Quantification of Key Audit Matters

Auditor opinion affects the quantification of KAMs by α=1%. An auditor's opinion can sometimes lead to a reduced quantification in Key Audit Matters (KAMs) for the following reasons: (1) Standard Unqualified Opinions: If the auditor's opinion is a standard unqualified one (i.e., without reservations), there may be less need to quantify specific concerns in KAMs, as no significant issues have been identified that would necessitate detailed numerical explanations; (2) Avoid Misinterpretation: Auditors may avoid quantification to prevent potential misinterpretations. Providing specific numbers might unintentionally emphasize certain matters over others or suggest a level of precision that is not intended; (3) Complex Estimates: Some KAMs might relate to complex estimates or judgments where precise quantification could be misleading or not feasible due to inherent uncertainties; (4) Reliance on Descriptive Explanations: In cases where a narrative or descriptive explanation is more effective in conveying the nature and implications of an issue, auditors might opt for this over quantification; (5) Professional Judgment and Sensitivity: Auditors might decide, based on professional judgment, that quantifying certain KAMs might be too sensitive or contentious, potentially leading to disputes or challenges; (6) Consistency Concerns: If quantification in KAMs varies significantly from one period to another without a clear rationale, it could create confusion. In some cases, to maintain consistency, auditors might minimize quantification; (7) Regulatory and Reporting Framework: The reporting framework or jurisdictional regulations might sometimes guide auditors towards a more qualitative approach in KAMs, depending on the nature of the auditor's opinion; (8) Mitigating Potential Liabilities: By avoiding specific quantifications, auditors might aim to mitigate potential liabilities. Providing specific numbers can sometimes expose auditors to claims if stakeholders rely on those numbers and face adverse outcomes; (9) Overloading the Audit Report: An overloaded report with excessive quantification can dilute the main messages and make the report less user-friendly. If the auditor's opinion is clear without extensive quantification, auditors might opt for a more concise approach; and (10) Focus on Primary Issues: By avoiding extensive quantification, auditors can ensure that stakeholders focus on the primary issues and concerns, rather than getting bogged down in specific numerical details.

In essence, while quantification can provide clarity and precision, there are scenarios where an auditor's opinion might steer towards a more qualitative or narrative-based approach in KAMs. The goal is always to provide the clearest, most relevant, and most useful information to stakeholders.

Financial performance affects the quantification of KAMs by $\alpha=1\%$. The financial performance of a company can influence the extent of quantification in Key Audit Matters (KAMs) for several reasons: (1) Highlighting Significant Changes: If a company has seen significant changes in its financial performance, auditors might quantify specific KAMs to underscore the magnitude and implications of these changes for stakeholders; (2) Complex Transactions and Adjustments: Strong or weak financial performance can stem from intricate transactions or adjustments, such as mergers, acquisitions, or major asset write-downs. By quantifying these matters, auditors offer clarity on their materiality; (3) Validation of Performance Metrics: Companies boasting excellent financial performance might have specific key performance indicators (KPIs) or metrics that drive their results. Quantifying KAMs related to these metrics can help validate them and provide insight into their derivation; (4) Increased Scrutiny: Exceptional or poor financial performance can draw increased scrutiny from stakeholders. Quantifying KAMs provides a clearer picture, potentially reducing ambiguities or concerns; (5) Mitigating Over- or Under-Representation: To ensure that stakeholders don't over- or under-interpret the significance of certain matters related to financial performance, auditors might opt to provide quantified context in the KAMs; (6) Comparative Analysis: Quantification can aid stakeholders in comparing financial performance over periods, especially if there are recurrent concerns or highlights in KAMs related to financial performance metrics; (7) Transparency in Estimations: Companies with specific financial performance results might rely on estimates, forecasts, or projections. Quantifying related KAMs ensures transparency in how these estimates impact financial results; (8) Risk and Uncertainty: Certain financial performance results may be tied to risks or uncertainties, like contingent liabilities following a particularly profitable business deal. Quantifying these KAMs can offer stakeholders insights into potential future implications; and (9) Stakeholder Expectations: Investors and other stakeholders might anticipate more detailed insights into aspects of financial performance that seem out of the norm. Quantifying KAMs meets these expectations, fostering trust.

In summary, the financial performance of a company, whether exceptionally positive or negative, can lead to increased complexities or heightened stakeholder interest. To address these complexities and meet stakeholder demands for clarity and transparency, auditors may choose to increase the quantification of Key Audit Matters (KAMs). Ang and Trotman (2015) state that quantification in narratives enhances clarity and reduces reader uncertainty. The study predicts that easily readable Key Audit Matters (KAM) with specificity and precision facilitate investor understanding of financial statements, while less readable KAM may hinder comprehension. In response to increased complexities or stakeholder interest, auditors, following this research, may choose to enhance KAM quantification for clarity and transparency.

5. Conclusion

The initial adoption of new auditing standards incorporating ISA 701's inclusion of KAMs in audit reports by an emerging economy in 2021 paved the way for our exploration into the determinants of KAM quantities and the detailed quantification in their descriptions. Our study, which encompasses companies from various sectors listed on the country's stock exchange revealing KAMs for the fiscal year 2022, confirms that the intricacies of a company, its financial standing, and indebtedness play crucial roles in the quantity and depth of KAM disclosures. Unexpectedly, factors like auditor size, their views, potential business continuity concerns, the scale of the enterprise, and audit cycles did not impact these disclosures. This investigation enriches the accounting discourse, spotlighting insights on KAM's recent integration in an emerging market.

The outcomes further underline that auditors gravitate towards intricate firms when determining the extent of KAMs and their associated quantification. Firms with robust fiscal health, signified by elevated profits, frequently engage in multifaceted transactions. Such intricacies amplify potential areas prone to significant inaccuracies, leading to augmented KAM disclosures. Furthermore, firms burdened by significant debts, suggestive of a convoluted financial framework, are anticipated to reveal more KAMs. On the flip side, auditors adopt a meticulous or cautious stance when examining less indebted companies, possibly earmarking a broader spectrum of areas as KAMs due to minimized risk appetites.

In conclusion, this study contributes to understanding the capital market in an emerging economy, emphasizing developmental approaches that balance costs, benefits, and their impact on the national economy. It provides insights into the inaugural presentation of KAMs in an emerging economy with a diverse range of industries, highlighting their role in enhancing transparency, investor confidence, and economic growth amidst varied industrial dynamics.

5.1. Declaration of Generative AI And AI-Assisted Technologies in the Writing Process

During the preparation of this work, the author used ChatGPT to paraphrase and translate. After using this tool/service, the author reviewed and edited the content as needed and takes full responsibility for the publication's content.

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