

## CHAPTER THREE

### LITERATURE REVIEW

#### 3.1 INTRODUCTION

This chapter reviews research on the Shariah audit and audit expectation gap from different perspectives. Given the paucity of studies on Shariah audit, the review includes literature in the conventional audit. The first section of the chapter examines on the definition of audit expectation gap. Followed by the different perspectives on the Audit expectation gap in the following section. Next this chapter highlights on the relevance of expectation gap in Shariah audit practices. The information from this chapter will be used to guide the formulation of the research instruments used to investigate the current state of audit expectations gap in Shariah audit in IFIs of Malaysia.

#### 3.2 AUDIT EXPECTATION GAP

Auditing from conventional perspectives is also known as a statutory audit. Statutory audit is required by a country's laws, which is sometimes called an external audit since it is carried out by external auditors. A Statement of Basic Auditing Concepts (1973) by the American Accounting Association (AAA) Committee defines audit as:

*A systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users.*

The American Institute of Certified Public Accountants (AICPA) defines audit as:

*The objective of the ordinary examination of financial statements by the independent auditor is the expression of an opinion on the fairness with which they present, in all material respects, financial position, results of operations, and cash flows in conformity with Generally Accepted Accounting Principles (GAAP).*

Statutory audit or conventional audit are performed to ascertain the validity and reliability of the information provided by organisations. It is also to provide an assessment of a system's internal control of organisations (Arens, 2009). The goal of an audit is to express an opinion on the financial statement that it is being prepared in accordance with the approved accounting standards of a country. Due to the limited resources and time constraints, an audit seeks to provide reasonable assurance that the statements are free from material misstatement. Hence, statistical sampling is often adopted in audits. In the case of financial audits, a set of financial statements is said to be true and fair when they are free of material misstatements - a concept influenced by both quantitative (numerical) and qualitative factors.

The requirement to have an annual statutory audit of certain companies audited by a qualified professional accountant, as required by Malaysian Companies Act 1965 and Islamic Banking Act 1983, is designed to protect the public interest. The assurance offered by audited accounts should enhance the confidence of all parties, which are concerned, with the affairs of institutions. The statutory audit provides assurance on the

reality and fairness of an IFI's financial information; advice on controls and processing system weaknesses and confirmation of accounting treatments on complex transactions.

Auditing is a vital part of accounting. Traditionally, audits were mainly associated with gaining information about financial systems (late 1800s-1900s) and the financial records of a company or business. However, recent auditing has begun to include non-financial subject areas, such as safety, security, information systems performance, and environmental concerns. With non-profit organisations and government agencies, there has been an increasing need for performance audits, examining their success in satisfying mission objectives. The performance audit was introduced during the 1960s-1970s. As a result, there are now audit professionals who specialise in security audits, information systems audits, and social and environmental audits which were introduced in the 1970s. The evolution of audit expanded in 2000s whereby according to Ibrahim (2009) with the rapid development of the IFIs, the public is starved for information on the IFI's activities as required by Islamic religious teaching. Thus, Shariah audit was introduced to satisfy the demands in ensuring the activities and operations of the IFIs are Shariah-compliant.

The notion of an expectations gap is not new, and one of the early applications of the concept was to the relationship between accountants and users of accounting reports by Liggio (1974). He used the concept of an expectations gap to describe the apparent failure of accounting and auditing to warn users about impending corporate collapses. He defined the expectations gap as the difference between the levels of expected performance 'as envisioned both by the independent accountant and by the user of financial statements'. However, according to Wartick and Mahon (1994), Wartick and Wood (1998), and Reichart (2003), expectation gaps are inconsistencies

between views of 'what is' and/or 'what ought to be'. Three types of gaps can emerge and each type calls for a different response:

- 1) Factual gap: This gap involves a dispute between two groups regarding inconsistencies in the fact ('what is' versus 'what if'). Factual gaps call for objective responses to specify the facts and clear up possible misconceptions.
- 2) Conformance gap: This gap involves one party's perception about inconsistencies in how another ought to behave in light of their current behaviour ('what is' versus 'what ought to be').
- 3) Ideals gap: This gap entails inconsistencies between two parties' perceptions about what one party ought to do ('what ought to be' versus 'what ought to do').

According to Porter (1993), instead of naming it as audit expectation gap, it should be named 'audit expectation-performance gap' since it reflects the gap between society's expectation on auditors and society's perceptions of the auditors' performance. The figure above indicates that the gap has two major components:

1. A gap between what society expects auditors to achieve and what they can reasonably be expected to accomplish ('reasonableness gap')
2. A gap between what society can reasonably expect auditors to accomplish and what they are perceived to achieve ('performance gap')

The performance gap can be subdivided into two components, which are:

- 2.1 a gap between the duties which can reasonably be expected of auditors and auditors existing duties as defined by the law and professional promulgations ('deficient standard') and

2.2 a gap between the expected standard of performance of auditor's existing duties and auditors' perceived performance, as expected and perceived by society (deficient performance)

In Malaysia, few studies are conducted on the audit expectation-performance gap that highlights the duties and roles of the auditors. Fadzly and Ahmad (2004) addressed the issues on expectation gap of auditors and investors' perceptions on beliefs and audit function. The study involved two parts. The first part obtains evidence of the expectation gap. The second part focused on the controlled experiment on investors to study the effect of reading materials on respondents' expectations. The experiment revealed the effectiveness of the use of reading materials to educate the users and correcting some misconceptions on auditing in Malaysia.

The Cohen Commission (1978) in the United States of America extended Liggió's (1974) definition by taking into account whether a gap may exist between what the public expects or needs and what the auditors can and should reasonably expect to accomplish. Later, Porter (1993) argues that the definition of audit expectation gap provided by Liggió (1974) and the Cohen Commission (1978) is too narrow as they fail to recognise that auditors may not accomplish 'expected performance' (Liggió, 1974) or what they 'can and reasonably should' (Cohen Commission, 1978). She argues that these definitions do not allow for substandard performance. Porter proposed that the study of the audit expectation gap should be structured in a more extensive way which allows the different components of the audit expectation gap to be identified.

Previous studies in the US (AICPA, 1978; Schelluch, 1996), the UK (Humphrey, Moizer, & Turley, 1993; Porter & Gowthorpe, 2001), Australia (Gay, Schelluch, & Reid, 1997; Monroe & Woodliff, 1993), South Africa (Gloeck & de Jager, 1994), Ireland (Robinson & Lyttle, 1991), New Zealand (Porter, 1993), Malaysia

(Fadzly & Ahmed, 2004, Teck Heang et. al., 2008), China (Lin & Chen, 2004), Barbados (Alleyne & Howard, 2005), and Egypt (Dixon, Woodhead, & Sohlman, 2006), Singapore (Best, Buckby, & Tan, 2001), have indicated the existence of an audit expectations gap. Previous literature indicates that audit expectations gap exists for several reasons. Humphrey et al. (1993) and Porter and Gowthorpe (2004), for example, have argued the gap exists due to a deficiency in an auditor's performance and auditing standards. Pierce and Kilcommins (1996), Boyd et al., (2001) and McEnroe and Martens (2001), argue that the gap exists due to misinterpretations and misunderstanding of the meaning of auditing by the users. These studies suggest that the users do not understand the audit functions and the role of auditors. Consequently, they have unrealistic expectations of auditors. Earlier, research by the Canadian Institute of Chartered Accountants (CICA, 1988) and Porter (1993) established the deficient performance, deficient standards and unreasonable expectations as the components of the audit expectations gap. However, a recent empirical study conducted by Porter and Gowthorpe (2004) has shown that these components have changed over time although the perceptions of pessimism as to the audit functions have not been eliminated.

Research on the audit expectations gap in the Shariah audit practice has received little attention by researchers. To date, only a limited number of studies have been conducted on Shariah audit practices in Malaysia. One of the early empirical studies has been initiated by Hood and Bucheery (1999) on the audit expectation gap between financial and religious (Islamic) auditors in Bahrain. Hood and Bucheery (1999) further argued that religious audits in Bahrain seem to complement the financial audit by external auditors. Nevertheless, they questioned whether or not religious auditors have a set of religious statements to audit as compared to financial statement audited by financial auditors. They found that financial audit expectation gap does exist in Bahrain

but not for religious auditors. They also found that financial auditors and religious auditors in Bahrain seem unaware of what each other does. Hood & Bucheery (1999) presumed that this finding might be due to the respondents' lack of understanding on the subject of the religious audit.

Normative accounting judges whether a situation is desirable or undesirable. It is an expression of judgement on 'what ought to be'. The practice of Shariah audit should be seen as a normative approach or positive approach to its development. Sulaiman (2005) mentioned that "what ought to be desired (the desirable)" may not coincide with "what is actually desired (the desired)" and in consequent "what is actually desired" may not be the same as "the actual" practice. From the approach made by Sulaiman (2005), Kasim (2009) conducted a study in exploring the gap between "the desired" and "the actual" practice of Shariah auditing in IFIs in Malaysia empirically. The desirable practice is to conduct Shariah auditing externally, but the result shows that the current practice is done at the internal level only. The study conducted by Kasim (2009) is in line with Wartick and Mahon (1994), Wartick and Wood (1998), and Reichart (2003) which defined the expectation gap as inconsistencies between views of 'what is' and/or 'what ought to be. Based on the literature, expectation gap in auditing is derived from the gap that arises between normative and positive approach. Since the nature of audit posits on 'what ought to be' from the regulators perspectives and the societies defines the audit as 'what is' it should be.

A different approach in justifying and illuminating stakeholder theory is provided by the normative strand (Dusuki, 2007). Stakeholder theory proposes narrative accounts of moral behaviour and philosophical guidelines for the operation and management of the corporation in a stakeholder context. It explains what the firm 'ought to do' both regarding the ends it pursues and the means it utilises, as well as why these

'ought to's are appropriate. Similar in auditing, the society expects the auditors' 'what ought to do' to follow social expectations. Due to that, auditing departs from the normative stands. It recognises the existence of different users that rely on the auditor's report, which leads the auditors to take the interests of all the groups into account. Shariah audit also stems from the normative approach. In Islamic banking, the objectives have remained vague in the vision and mission statements of most Islamic banks and largely suggestive and normative in the writings of Muslim scholars (Mohammed & Taib, 2011). The normative approach includes morally significant values essential to effective management decisions. For example, if consumers of the Islamic banking have a right to products that are unlikely to void the Shariah compliance aspect, then the institutions are obligated to take into account this group in making decisions about product design. Thus, it provides evidence that 'what ought to do' is significant to the Shariah audit practices.

This research used the notion of audit expectations-performance gap that refers to Porter's model (1993). Compared to other definitions, Porter's (1993) definition is seen as more precise, comprehensive and practical. As described above, her definition takes into account the possibility of inadequate performance of auditors and the reasonable/unreasonable expectations by the users, which fits the present auditing environment. Although her definition is given in the context of external auditing, it is argued that this definition is applicable to the context of Shariah auditing as "the basic principle governing the issue of audit expectations gap is the same" (Chowdhury, 1996). Thus, the audit expectations gap in this study refers to the gap between the expectations of Shariah committee, internal auditors, external auditors, Shariah officers, depositors and regulators (BNM) on Shariah audit practices in the Islamic banks. The expectation also includes the performance of the Shariah auditor and the respondents' expectation

of what the Shariah auditors could and should achieve, and what Shariah auditors believe they could and should achieve.

According to Porter (1993), to narrow the audit expectation gap effectively, the nature of the gap needs to be ascertained as different components of the gap require different methods. Porter's framework of the audit expectation gap consists of three main components; i) Deficient performance on the part of auditors, ii) Deficient standards that fail to live up to the reasonable expectation of the public, and iii) Unreasonable expectations on the part of the public. Teck Heang et al. (2009) adapted Porter's model on audit expectation-performance gap with the objective to examine the audit expectation gap in Malaysia. Based on the survey, 42 duties of auditors were examined including; i) the legal requirements of auditors in Malaysia (Section 174 of the Malaysian Company Act 1965); ii) the duties of auditors required by the Malaysian Approved Standards on Auditing (MASA), the Anti-Money Laundering Act (AMLA), and other relevant legislation; and iii) the often expected but not yet legislated duties of auditors. These duties described in the auditing literature, focus on the following roles:

- i. Duties of auditors to provide early warning signals of probable company failure;
- ii. Duties of auditors to guarantee the solvency of a company and the accuracy of a company's financial statements;
- iii. Duties of auditors to detect and report fraud and illegal activities; and
- iv. Duties of auditors to report matters of concern to relevant regulatory authorities.

The survey found that an audit expectation gap exists with respect to 31 of the 42 duties of auditors examined. There are different expectations exist between the auditors and non-auditors. The analysis of the nature and compositions of the expectation gap, based on Porter's (1993) framework, shows that six non-statutory duties of auditors were considered by those selected respondents to be "unreasonable"

expectations, while 17 duties were considered as "reasonable" expectations of auditors. These 17 duties were then classified as "deficient standards". This study also found that nine statutory duties were considered by the selected respondents to suffer from "deficient performance" by Malaysian auditors.

### 3.2.1 Different Perspectives on the Audit Expectation Gap

Numerous causes for the existence of the audit expectations gap have been put forward over the years. The expectations gap exists as a result of a natural time lag by the auditing profession in identifying and reacting continually to the changing auditing environments and public expectations (Tricker, 1982). According to Gaa (1991), the audit expectations gap was a direct result of the "political game between two contending parties" (p. 84), between the public and the auditors. This view is supported by Sikka et al. (1998) in which they argued that historical and political contexts can give indication "within which expectations are formed, frustrated and transformed" (p. 300). They contend that audit as a social practice is subjected to constantly shifting meanings because the social context of auditing changes continuously through interaction and negotiation. The conclusion from this perspective is that the audit expectations gap will continue to exist.

As argued by Boyd et al. (2001), user misunderstanding forms part of the elements that compromise the concepts of the audit expectations gap. This view appears to be advanced by the audit profession as a defence to the growing criticism on auditors. As stated by Sweeney (1997):

*The main conclusion of the profession was that users' perceptions of the audit were flawed rather than with any significant problem with the audit itself' (p. 20)*

This is another reason identified for the audit expectation gap due to unreasonable

expectations and a misunderstanding by the audit reports users over the audit functions. This view is consistent with the findings from Porter & Gowthorpe (2004). It found that unreasonable expectations by the public were the main factors representing 50% of the audit expectations-performance gap in the UK. Humphrey et al. (1992) argued that the audit expectations gap was "caused by the public's misunderstanding of the audit function, by over-exaggerated responses to the isolated failings of individual auditors and by misappreciation of the extent to which the profession is actively responding to public interest demands and enhancing the quality of audit services" (p. 157).

Another point of view is that the audit expectations gap is a result of corporate failure. This corporate failure, in turn, is regarded as audit failure. Corporate collapse is always accompanied by scrutiny of the roles of auditors and in some cases, litigations on the grounds that they have performed the task negligently (Power, 1994). Such focus is sharpened when the collapse of a company comes only a short time after its financial statements are given an unqualified audit opinion (Dewing and Russell, 2002). Gay et al. (1998) argued that the corporate crises "lead to new expectations and accountability requirements and periods of high standard setting activities" (p. 472). This view is supported by the finding of Porter & Gowthorpe (2004) where they suggested the "significant and unexpected company collapse both in the UK and New Zealand" (p. 1), partly contributed to an audit expectations gap in these two countries.

Clearly, from the discussion above, the audit expectations gap exists because of various factors. It is reasonable to point out that the changes in the auditing environment have prompted the expectations questions. However, the underlying reasons for the existence of the audit expectations gap lie on its main players, the auditors and the users. On one hand, it is a direct result of the audit profession failing to respond appropriately to new issues arising from changes in the audit environment. For example, the refusal

of auditors to assume the responsibility for fraud detection and reporting exercise and their involvement with non-audit services extended the audit expectations gap. On the other hand, the gap exists due to a misunderstanding or a lack of knowledge of the users over the audit functions. This misunderstanding then leads to unreasonable expectations.

In terms of Shariah audit practices, there is a different expectation on the auditor's role and the Islamic framework within which auditors perform their duties (Briston & El-Ashker, 1986; Abdel-Karim, 1990; Khan 1985) as well as the issue of independence of the auditors (Abdel-Karim, 1990). The SSB's role is compared to that of conventional auditors (Briston & El-Ashker, 1986; Abdel-Karim, 1990). Based on Abdel-Karim (1990), the SSB function is purported to include Shariah ex-ante audit, ex-post audit, determination and payment of zakat and adoption of appropriate accounting policies. Conclusively, the role of the SSB is portrayed as wider in scope and accountability chain (Khan, 1985). Since the 1980s, the discussions on religious auditor's role and Shariah audit responsibility have been discussed thoroughly b. According to previous studies, discharging such responsibilities requires the religious auditor to be knowledgeable in accounting, finance, management, Islamic jurisprudence (at least on Islamic financial transactions) auditing and other relevant subjects (Briston & El-Ashker, 1986; Abdel-Karim, 1990; Khan, 1985). Chapra and Ahmed (2002) argued that IFIs must be Shariah cleared and audited. Also, it is necessary to provide assurance that all the transactions of the IFIs are actually in conformity with the verdicts of the SSBs. These are essential corporate mechanisms in IFIs for creating confidence in depositors and stakeholders with regards to their compliance with Shariah requirements (Grais & Pellegrini, 2006). Chapra and Ahmed (2002) assert that the SSBs could perform Shariah clearance. However, Shariah audit is difficult for the SSBs to

conduct because of time and/or staff constraints. Preferably, they suggest, existing chartered audit firms should acquire the necessary Shariah expertise to enable them to undertake the Shariah audit (Chapra & Ahmed, 2002). Thus, ideally, Shariah compliance audit would be internally and externally conducted.

According to Abdul Rahman (2008), due to the restriction of the SSBs scope of work, the SSBs rarely carry out rigorous internal Shariah review or audit (ex-ante and ex-post) on the operations of IFIs. Although efforts have been made by some jurisdictions to address some of these issues and as well as various other challenges of IFIs by introducing external institutional structures to carry out ex-post Shariah audit, inconsistent pronouncements in different operational jurisdictions of the IFIs have derailed these initiatives (Grais & Pellegrini, 2006). The authors recommend development of a framework based on both internal and external arrangements to the firm with an emphasis on market discipline, which could serve as a guide to SSBs through standardisation and harmonisation of contracts and practices by a professional self-regulatory association. Such a framework might ensure uniformity and consistency of interpretation and improve the enforceability of legal contracts. In this framework, a review of transactions would be carried by IFI's internal review units while external auditors would be responsible for expressing an opinion on the Shariah compliance of the IFIs' activities.

Notwithstanding its nature of accountability and scope, the product of SSB's role is visible as attachments to external auditors' annual financial reports or as internal reports to directors who state their opinions in annual reports as to the Shariah compliance of IFI (Briston & El-Ashker, 1986). Researchers in this period were critical of this arrangement. For instance, Abdel-Karim (1990) sees the confinement of SSBs to Shariah matters as akin to the separation between religious and external auditors and

thus incompatible with the tenets of Islam. This is confirmed by the findings that while both religious and financial auditors are unaware of what the other does, there is an audit expectation gap for nonreligious auditors (Briston & El-Ashker, 1986).

Simultaneously, new themes such as the need for Shariah auditing, Shariah clearance by IFIs (Chapra & Ahmed, 2002; Abdul Rahman, 2008), issues and challenges of Shariah auditing (Grais & Pellegrini, 2006; Abdul Rahman, 2008; Mulyany, 2008; Kasim, 2009; Kasim et al., 2009) have been highlighted. The issues and challenges include independence, confidentiality, competence/qualification, inconsistent pronouncements, scope and timing of audits, Shariah audit evidence, audit programmes and procedures and an independent regulatory body. Based on the previous discussions on Shariah audit, these components such as framework, scope, independence, processes, reporting, competency, responsibility and Shariah auditor's performance are used as a tool in identifying expectation gaps in Shariah audit practices.

### **3.2.2 Expectation Gap in Shariah Audit Practices**

Shariah audit has currently emerged as an important mechanism in ensuring Shariah compliance in line with the rapid development of Islamic Banking. There is rise in expectation gap in Shariah audit practices due to different views and opinion by the scholars, practitioners and stakeholders on the practice of Shariah audit. Expectation gap in Shariah audit must be identified, narrow it so as to gain confidence level among scholars, practitioners and stakeholders. It is important to identify the gaps that exist in the practice of Shariah audit since its implementation requires improvement (Othman and Ameer, 2015). Currently, Shariah audit is done at the internal level of the Islamic banks. According to SGF (BNM, 2010) Shariah audit function shall be performed by

internal auditors who have acquired adequate Shariah-related knowledge and training. Also, the internal auditors may engage the expertise of the IFI's Shariah officers in performing the audit, as long as the objectivity of the audit is not compromised.

The discussions in the previous section highlights on the audit expectation gap in terms of external audit. However, audit expectation gap also exists from the internal audit point of view. There has traditionally been an air of contention between internal auditors, risk managers and the various executive they report to. Although everyone should ideally be on the same page in helping companies improve, internal auditing is often viewed as an annoyance as auditors point out flaws in processes or identify when certain policies and protocols aren't being followed properly (Patterson, 2014)

Recent research conducted by PricewaterhouseCoopers (2014) illustrated the issues many executives and business leaders have with auditors. More than half of the senior management group polled (55 percent) said they don't believe internal audit departments add any significant value to their organizations, while others felt auditors could do a better job providing timely advice that would help management handle current and future problems more effectively. However, when PwC polled board members, only approximately 30 percent said that internal audit doesn't add any significant value to the company. This suggests the problem isn't the audit department, but the relationship between upper management and specifically, chief financial officers. CFOs generally have more interaction with auditors than board members and, more often than not, they want different things. Many businesses don't know what to expect of internal audit functions. Some leaders might want advice from auditors, others may expect them to act as watchdogs, while others just want reassurance. By making the role of internal audit departments more transparent, enterprises can do away with a lot of misconceptions. Although gaps exist between internal auditors and other

executives, enterprises can work to improve the synergy between the two by considering the above steps (IPPF, 2010).

Therefore, even though Shariah audit requirement at current was performed at the internal level, the study on expectation gap in Shariah audit deem necessary since its implementation requires improvement and received various criticism in its current practice (Othman and Ameer, 2015). Among the views from the scholars and practitioners on the practice of Shariah audit in Islamic banks, there are lack of comprehensive and well-guided audit of the Shariah legal contracts, documentations and operations (Abdul Rahman, 2011). The Islamic banking industry also lack of supervision and monitoring, oversight, auditing and management of risks (Grais and Pellegrini, 2006). In addition, there is also lack of auditor competency in performing Shariah audit function according to scholars and practitioners (Uddin et. al., 2015; Yusoff, 2013; Kasim, 2009; Yaacob, 2012). The lack of both Shariah and accounting knowledge has dampened the crucial needs of the Shariah auditor competency. Those with accounting knowledge tend not to have Shariah knowledge and vice versa. Any risks resulting from auditor's incompetency during Shariah audit process will expose Islamic banks to potential losses (Othman and Ameer, 2015). The rapid and tremendous growth in Islamic finance requires the IFIs to have competent Shariah auditors. And to provide the 'check and balance' an equally competent auditor who has good knowledge of accounting, auditing and finance with the equally good Shariah and fiqh knowledge and understanding (Uddin et. al., 2015). Investments for the education in shari'ah, accounting and auditing is crucial to enhance the knowledge and expertise of the actors involve with the shari'ah audit especially and IFIs in general (Rahman, 2011; Sulaiman, 2011).

Due to that, the academics, audit practitioners and Shariah scholars in Malaysia, agreed strongly with the creation of a new Shariah audit discipline with a separate regulatory framework (Yusoff, 2013; Mulyani, 2007). There is a need to increase the understanding of Shariah auditing among internal auditors, enhance the Shariah knowledge of internal auditors, standardise the Shariah audit framework and provide general guidelines to design audit programmes for Shariah auditing (Yahya & Mahzan 2012).

In terms of independence in Shariah audit, there are three factors that significantly contribute to the degree of auditor independence, i) clarity of definition of the auditor's responsibilities ii) the position of the internal auditor within the institution's organizational structure, and iii) the reporting structure (Yusoff, 2013; Yaacob, 2012; Haniffa, 2010; Grais and Pellegrini, 2006). Haniffa (2010) raises the question of the SC independence as they are making fatwa and at the same time helping the Shariah auditors in conducting Shariah review or Shariah audit. Clearly there is no clear line on the separation of duties which is essential for any good internal control practices. The IFIs need to rethink of where they could clearly separate these roles to avoid the misperception of the stakeholders on the SC and/or Shariah auditors' independence.

Some of the scholars argued that the Shariah audit is only to be conducted by Shariah professionals instead of accountants (Kasim et.al. 2009), while some others prefer the trained internal auditor to undertake the responsibilities (Yusoff, 2013; Yaacob, 2012). The Audit Committee of the IFIs should discharge their best effort to ensure that the external auditors are capable of undertaking the ex-post Shariah compliance reviews within their term of references (IFSB, 2006). They should also work with the internal auditor and the Shariah auditor, if the internal auditors are not

Shariah capable, and more importantly with the SC (Abdul Rahman, 2011). Hence, the IFIs auditing should evolve into a professional Shariah internal and external auditors capable of doing the financial, management and also the Shariah audit. Chartered audit firms should acquire the necessary knowledge and personnel to undertake the Shariah audit.

All of the above discussions, results in different expectation in Shariah audit practices especially in the area of framework, independence, competency, reporting, scope and processes. Identifying components of the audit expectation gap is critical because problems arising from different components require different solutions. Possible tools to reduce the gap can be assigned only after the audit expectation gap and its components in a specific society have been identified (Judith, 2015).

As discussed earlier, Porter (1993) detailed the definition of reasonableness gap as a gap between what societies expects on the practices of audit and what it can reasonably be expected to accomplish. This study is looking from the perspectives of Shariah audit in terms of exploring the gap between what societies (i.e. regulators, Shariah committees, Shariah officers, Shariah managers, internal and external auditors and the depositors) expects on the practices of Shariah audit and what it can reasonably be expected to accomplish.

Kasim et al. (2009), Mulyani & Ibrahim (2008) and Sulaiman (2005) explored, empirically, the gap between “the desired” and “the actual”. The desirable practice may not be similar to the actual practice that takes place. Based on the findings done by Kasim et al. (2009) and Mulyani & Ibrahim (2008) the desired practice of Shariah auditing is to conduct externally, but the result shows that the current practice is done at the internal level only. The studies conducted by Kasim et al. (2009) and Mulyani & Ibrahim (2008) are in line with Wartick and Mahon (1994), Wartick and Wood (1998)

and Reichart (2003) that defined expectation gap as inconsistencies between views of 'what is' and/or 'what ought to be. However, Porter (1993) classified this scenario as 'reasonableness gap', which was illustrated in her model of the audit expectation-performance gap.

### 3.3 CHAPTER SUMMARY

Throughout this chapter, Shariah audit practices and nature of the audit expectation gap have been presented and discussed regarding definition and importance. The chapter concluded by highlighting the framework used in determining the expectation gap in Shariah audit practices.

