The Impact of Key Audit Matters on Audit Costs with evidence from Firms listed on the Egyptian Stock Exchange

تأثير أمور المراجعة الجوهرية على تكاليف المراجعة مع دليل من الشركات المقيدة بالبورصة المصرية

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Abstract

This research aims to investigate the relationship between key audit matters (KAMs) and audit cost (proxied by; audit report lag (ARL)). The research design is a quantitative approach. The analysis relies on secondary data through a sample

of 79 non-financial Egyptian-listed firms from 2018 to 2023. The researcher employs logistics regression analyses. The results show that there is a positive and significant relationship between KAMs and ARL.
Keywords: key audit matters, ISA701, audit report lag, Egypt.

الملخص:

يهدف هذا البحث إلى دراسة العلاقة بين أمور المراجعة الجوهرية (KAMs) وتكلفة المراجعة (المُمثلة بـ: توقيت إصدار تقرير المراجعة (ARL)). يعتمد تصميم البحث على منهج كمي. يعتمد التحليل على بيانات ثانوية من خلال عينة من ٧٩ شركة مصرية غير مالية مدرجة في البورصة خلال الفترة من ٢٠١٨ إلى ٢٠٢٣. يستخدم الباحث تحليل الانحدار اللوجستي. تُظهر النتائج وجود علاقة إيجابية ودالة إحصائياً بين أمور المراجعة الجوهرية وتوقيت إصدار تقرير المراجعة.
الكلمات المفتاحية: أمور المراجعة الجوهرية، معيار المراجعة الدولى ٧٠١، توقيت إصدار تقرير المراجعة، مصر.

1. Introduction

The International Standards on Auditing (ISA) calls for a significant change in the structure and content of audit reports. Previously, audit reports with unqualified audit opinions were formulaic and contained only a pass-or-fail statement (Li and Luo, 2023; Kitiwong et al., 2025), which is not informative enough in making decisions. Therefore, the addition of key audit matters (KAMs) to the audit report was necessary to provide highlights and key matters from the auditors' point of view.

The main reason behind the addition of KAMs is intended to provide more “entity-specific”, and “financial period-specific” information beyond the usage of standardized language of the traditional audit report, why they are recognized KAMs, and how the audit firm handled them (Bepari et al., 2024; Chang e al., 2024; Alharasis, 2025). Furthermore, the audit firm has the license to select the topics that justify their opinion and explain their findings, the number of KAMs to report, and regarding each KAM how much detail to include in its report (Hussin et al., 2023; Alharasis, 2025).

However, if the audit report becomes lengthy and has technical jargon makes KAMs tricky and challenging and can result in information overload which can overshadow other material issues in the audit report (Ong et al., 2022; Bepari, 2023), thus, audit firms must record as KAMs the topics that received substantial attention throughout the audit process.

Recently, the literature suggests that for audit firms to comply with the new audit regulations on KAMs would require the auditor to perform additional procedures, apply further compliance training, and implement further quality control checks (Elmarzouky et al. (2022). The auditor would pass this additional effort to the clients through audit costs. One of those audit risks is audit report lag (ARL).

Based on the theoretical debate in the literature on the consequences of KAMs on ARL. The positive impact is based on the need for more auditors' compliance training and excessive checks for quality control, more information about the audit process can be translated into performing additional audit procedures, and more discussion with the audit committee and board of directors (Lee et al., 2024). The negative impact is because audit firms hire high-quality audit teams in the KAM era (Baatwah et al., 2024). The no effect is based on that auditors already do those audit procedures to ensure audit quality, and no new information is needed only disclosing more detailed information (Abdullatif et al., 2023).

Therefore, this study will try to fill the gap between the prior literature through several contributions. Firstly, the past research findings of the consequences between KAMs, and ARL are mixed and are not needful applicable to emerging markets (Zhang and Shailer, 2022). Secondly, the KAMs' requirements in emerging markets are associated with a higher amount of audit effort than in developed economies. This is because auditors in those markets are characterized by relaxed regulations, ineffective enforcement, and lower litigation and reputational costs (Abdullatif and Al-Rahahleh, 2020).

Third, the coronavirus leads to an increase in restrictions faced by auditors, in addition to the high requirements from audit clients for firm-specific information in certain timelines. Finally, the research is considered an application of the agency theory to the context of the KAMs as a new section added to enhance the independent audit report.

The rest of the paper is structured as follows: in Section 2, provide the literature review and hypotheses development. Section 3, explains the research method. Section 4 demonstrates the empirical results, robustness check, and additional analyses. In Section 5, provide an overall conclusion.

2. Literature Review and Hypothesis Development

2.1 Literature Review

In terms that the expanded audit report does not influence ARL, Abdullatif et al. (2023) investigate the impact of KAMs on ARL and whether the number of KAMs reported by 194 public Jordanian firms in the period between 2017 and 2019. The research shows that there is no statistically significant relation between the number of KAMs reported and ARL, justifying that in Jordan auditors select the reported KAMs in a way that does not affect directly their efforts. However, there is a positive association between ARL and audit fees, audit firm size, the issuance of a qualified audit opinion, and firm leverage, and a significant negative association between ARL and firm profitability.

As far as the relation between the positive relationship between the expanded audit report and ARL, Mnif and Cherif (2023) investigate the association between the auditor's industry specialization and ARL. Additionally, they examine whether the adoption of ISA701 impacts the association between the auditor's industry specialization and ARL. The authors reveal that firms audited by industry specialists have shorter ARLs, and the moderating variable ISA 701 leads to an increase in the ARL.

Regarding the negative association between expanded audit reports and ARL, Baatwah et al. (2024) examine the impact of KAMs on both audit fees and ARL. This study finds that KAMs increase the audit fees but shorten ARL during the period examined, however, there is insignificant impact for the number of KAMs on audit fees and ARL. Further, there is a different impact of KAM if it is related to entity-level risk KAM, and account-level risk. The former is associated with higher audit fees and shorter ARL. The latter does not have the same effect. The overall results show that KAM is associated with higher fees and high-quality audits even though the audit report is issued in a shorter time. This is because during the era of KAM tend to hire high-quality audit teams.

2.2 Hypothesis Development

While operating in the KAMs disclosure era, two opposite opinions were formed about the impact of KAMs on ARL.

According to the first opinion, KAMs disclosure increases auditors' accountability. Hence, an expanded audit report includes detailed information about the audit process, as a result, auditors feel a greater sense of accountability leading them to exert more time and effort in examining the financial statements, conduct more audit tests, and perform extra procedures about the disclosed areas to protect their reputation and avoid any financial costs (Elmarzouky et al., 2022; Mnif and Cherif, 2023; Baatwah et al., 2024). Thus, KAMs will be associated with higher audit fees and long ARL.

According to the second opinion, KAM is a disciplinary mechanism for managers rather than auditors (Gold et al., 2020). Hence, auditors will share their comments and observations with managers about managers' judgments and estimates, as a result, shrinking any opportunity for managers to extract personal benefits and ensure high reporting quality. Thus, KAMs will not be associated with high audit fees and longer ARL (Baatwah et al., 2024).

In tune with the second opinion, Asbahr and Ruhnke (2019), and Sierra-García et al. (2019) mention that KAMs are just disclosing how auditors build their opinion, and the whole effort goes into modifying wording, and disclosing detailed information. Nevertheless, Lee et al. (2024) claim that KAMs enhance the working dynamics between the auditor and client, they also state that a larger number of KAMs will lead to oblige auditors to consume effort and time to examine and document those matters. This is because their number involves high uncertainties and risks and more managerial opportunistic behavior (Bepari et al., 2023).

Thus, the number of KAMs indicates the severity and extent of audit risks in auditing the client. On the other side, Abdullatif et al. (2023) state that those efforts and time-consuming will shrink when auditors deal with KAMs disclosure as a formality regardless of their numbers leading to an insignificant impact on the ARL. Consequently, the research hypothesis can be formulated as follows:

Hypothesis (H1): key audit matters significantly affect audit report lag.

3. Research Method

3.1 Sample and data collection

Initially, the sample is based upon the 100 active Egyptian firms listed in the EGX, as measured by the EGX 100 index in the financial year ended in 2023, covering six years from 2018 to 2023. The final sample consists of 79 non-financial firms from 2018 to 2023; there are 474 total observations.

3.2 Models and Variables Measurement

(Table 1) shows a list of the variable measurements. Logistics analysis can estimate the relationships between the independent and dependent variables. Audit costs could be in the shape of audit report lag.

Table 1 Variables measurement

Variables	Measure	Symbol
Key Audit Matters	Dummy variables, where (1) will be assigned, if there is a KAMs section in the audit report and (0) otherwise.	KAM_{it}
Audit Report Lag	Total number of days from the firm's fiscal year-end to the external auditor's signature date.	ARL_{it}
Big 4	A dummy variable; (1) if the audit firm is big 4, (0) otherwise.	Big_{it}
Firm Size	The natural logarithm of total assets.	$Firm\_Size_{it}$
Corona	A dummy variable; (1) for the sample's period in 2019,2020, and 2021 and otherwise (0).	$Corona_{it}$
Profitability	ROA = net income/total assets.	$Profitability_{it}$
Liquidity	Current ratio = current assets/current liability.	$Liquidity_{it}$
Leverage	LEVG= total debits / total assets.	$LEVG_{it}$
Audit Opinion	A dummy variable; (1) if the auditor issues a qualified audit opinion in the current period, (0) otherwise.	$Audit\_Opinion_{it}$

Source: prepared by the researchers

4. Empirical results

The research hypothesis (H1) stated that key audit matters significantly affect audit report lag. The research model is used to test this hypothesis. The model includes KAM as an independent variable and ARL as a dependent variable. In addition to, control variables: Big4, Firm_Size, Corona, Profitability, Liquidity, LEVG, and Audit_opinion. Table (2) presents OLS regression analysis to test the fifth empirical model after treating the heteroskedasticity problem.

Table 2: OLS Regression Results of the Research Model

ARL	Coef.	St.Err.	p-value
KAM	12.96***	2.874	0
Big4	9.805***	3.15	0.002
Firm_Size	-0.657	1.727	0.704
Corona	-1.888	3.703	0.61
Profitability	-25.054	23.226	0.281
Liquidity	-1.441	1.148	0.21
LEVG	-6.732	9.642	0.485
Audit_Opinion	10.314***	3.337	0.002
Constant	71.633***	17.588	0
Industry	Included		
year	Included		
R-squared	0.149		
F- Test	3.769		
Prob > F	0.000		

Table (2) suggests the probability of an F-test is lower than 0.05 (0.000). This reveals the overall significance of the model and indicates that there is an effect of the independent variables on the dependent variable. The value of R-square is 0.149 which indicates that the independent variable (KAM) and control variables (Big4, Firm_Size, Corona, Profitability, Liquidity, LEVG, and Audit_opinion) explain about 14.9% of the changes in ARL.

Furthermore, it shows that the OLS coefficient of the main independent variable (KAM) is positively associated with ARL (12.96) and significant at 1%. This implies that there is an impact of key audit matters on audit report lag (ARL). Thus, the research hypothesis (H1) is accepted.

Regarding control variables, the results of the OLS regression analysis revealed that BIG4 and Audit_Opinion are positively related to ARL. These relations are significant at 1% for BIG4 and Audit_Opinion. Furthermore, it is found that Firm_Size, Cornoa, Profitability, Liquidity, and LEVG are related negatively to ARL, these relations are insignificant.

6. Conclusion

This paper aims to investigate the cost associated with the new audit regulation ISA 701 (KAMs) by examining the relationship between the presence and the number of risk topics disclosed by the auditor and the audit report lag. The research also examines whether this relationship is affected by the number of KAMs the auditor discloses. The research is applied to 79 non-financial Egyptian-listed firms over the period from 2018 to 2023.

The research contributes theoretically and empirically to the current literature. Theoretically, this research extends the literature that shows a growing interest in including key audit matters in the audit report and the challenges faced by auditors. Furthermore, this research extends the emerging stream of literature on audit costs, especially audit report lag that can be resulted from the KAMs disclosure. The concurrent research takes part in the debate about the consequences of KAM and the need for additional investigation to enlarge the understanding of its economic consequences. Therefore, the research comes in the favor of academic researchers, regulators, and financial standards setters to improve their understanding of key audit matters and their impact on audit costs.

Empirically, this research is particularly important after the occurrence of the financial crisis and the reform of IAASB. The complexity and difficulty of KAMs affect the audit process and require excessive communication between auditors and governance bodies. Consequently, auditors must pay more attention to KAMs and their audit costs. Therefore, this research will be useful and guide both financial statement preparers and auditors because it provides some practices auditors should do to deal with KAMs' complexity to issue audit reports on time and clarify the intended and unintended consequences of these changes to the audit report.

The result supports a positive and significant association between KAMs and ARL. The expanded audit report requires the auditor to perform additional procedures, apply further compliance training, and implement further quality control checks (Elmarzouky et al., 2022). Therefore, the auditor would pass this additional effort to the clients through audit costs. This is because KAMs disclosure exaggerates auditors' accountability, hence, it provides the stakeholder with access to identify the amount and quality of the auditor's work in detecting or preventing misstatements. Consequently, auditors dedicate more time and effort to protect their reputation and avoid financial costs leading to longer ARL. The result is consistent with Al-mulla and Bradbury (2022); Bepari et al. (2023); Li and Luo (2023); Bepari et al. (2024); Mnif and Cherif (2023).

The research has some limitations as opportunities for future research. This research is applied in the Egyptian context. Further research might consider a different country or a cross-country analysis. Also, the study just focuses on audit report lag as a representative of audit costs. Future research may consider different audit costs (audit fees) or audit benefits (audit quality).

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