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**The Role of External Auditor to Improve the Quality of  
Auditing Process under the Risks of Measurement and  
Disclosure Based on Fair Value**

**"Experimental Study"**

**A Thesis Submitted For a Master's Degree in Accounting**

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## **Introduction:**

Accounting standards Given up on conservatism policy in measuring some balance sheet items and shifted these standards from historical cost to fair value measurement.

the historical cost is one of the most important bases of accounting for its high reliability, based on events that have already occurred and are documented, but under globalization and the growing number and size of companies, the users of financial statements need more information to help them make decisions than information based on it. Historical cost is characterized by fixed purchased power under different economic conditions, which makes it an inappropriate measure and does not provide confidence in financial information.

After increasing the criticism of user about the historical cost – as a basis for accounting – professional organizations and accounting standards boards in many countries have been moving toward issuing a set of standards to provide information that helps users of financial statements make their decisions and toward fair value.

The beginning of the International Accounting Standards Committee (IAS) issued IAS 29, entitled “the Financial Report in High-inflation economies in 1989, then The IASC issue several criteria that allowed fair value to be used in relation to assets, whether financial or non-financial, such as a standard IAS 32, "Financial instruments of Presentation and Disclosure", IAS 39, "Financial instruments of Recognition and Measurement", reissued by the International Accounting Standards Board (IAASB) of IFRS 7, "Financial instruments - Disclosure - supplementing IAS 32 and IFRS standard "Financial instruments" as an alternative to IAS 39<sup>1</sup>.

IFRS13 International Financial Report Standard (IFRS13) has been issued the IAASB fair value measurements in May 2011 as a comprehensive and guided standard for applying to any other standard that permits fair value measurement and disclosure.

By this standard, accounting measurement is based primarily on fair value but in exceptional cases which historical cost has been used .

The development of the accounting basis has been accompanied by a development in accounting disclosure in financial statements, with business and

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<sup>1</sup>-Dr. Assem Mohamed Ahmed Sorour, "Analysis Study of IFRS13 measures of Fair value and Development proposals", Scientific Journal of Economics and Commerce, Faculty of Commerce, Ain Shams University, 4th issue, 2013, pp. 571-572.

service establishments becoming required under the accounting standard for a broader and more detailed disclosure of the elements and items of financial statements measured by fair value.

Given the impact of this development on the external audit process, the external audit profession should have developed external audit procedures and methods to suit the nature of this development. Then the auditing organizations have been issued a standard for auditing fair value .

### **The research problem:**

A range of challenges faced by outside auditors on auditing the fair value measurement and disclosure, including the complexity of fair value measurement methods and models. It was not limited to measuring fair value based on market prices in active markets and the scale of measurement was extended to relying on models, methods of evaluation that were difficult to verify from substantial misrepresentations that increased risk of review associated with fair value measurement and disclosure.

The external auditor faces major problems and challenges in his role in reviewing the accounting measurement and disclosure of fair value, the most important of which are:-

1. Challenges Related to the external auditor needs evidence appropriate to nature of the fair value and accounting disclosure in which there are more substantial misrepresentations in the financial statements.
2. Challenges Related to the external auditings need skills and experience to keep pace with the development of fair value methods and applications.
3. Challenges related to the fair value accounting will be unreliable in the absence of an active market and declared prices.
4. challenges related to the levels of the fair value hierarchy, there is difficulty in verifying fair value estimates except for the first level, where it provides the best fair value assessment for its reliance on observable inputs, and the auditors can easily verify them, so depending on which level other than the first level, gives the facility an opportunity To be biased in valuing fair value, with the aim of achieving personal benefits for management.

Therefore, there are several researchers questions related to the research problem:

- What are the fair value problems and it's effects on the external auditing ?
- do external audit have the competence to overcome the risks of fair value measurement and disclosure problems?

- What is the impact of fair value measurement and disclosure risks on the quality of external auditing?

What are the requirements and procedures for external auditor to overcome the risks, problems and challenges they face?

## **Research Objectives**

Research from this study aims to achieve the following objectives:-

- to examine the risks and accounting problems resulting from measurement and disclosure on the basis of fair value.
- to study methods for assessing audit risk under fair value measurement and disclosure.
- examining the impact of the estimated review risks under the measurement and disclosure of the fair value review on the quality of the review?.

## **The Researcher's Importance**

As information users need fair value and need to measure and disclose financial statements and increase the importance of broader measurement and fair-value disclosure in financial statements, this has increased the importance of external auditor's audit and disclosure and their need for detailed guidance on how to avoid the risks associated with the measurement and disclosure audit. Based on fair value and its consequences and their impact on the quality of external audit.

## **Search hypotheses**

Research is based on testing the following hypotheses:-

1. There is a positive relationship between the problems of accounting for the fair value of measurement and disclosure and the quality of external audit.
2. The proposed framework contributes to the quality of the external review process.
3. the external auditor shall use techniques and procedures to respond to the risks of manipulation that may result from the use of fair value accounting and thereby influence the quality of external audit.

## **Research Approaches**

In this study, the researcher used both the deductive technique when conducting a logical analysis of the proposed framework for the impact of fair value measurement and disclosure risks on the quality of external review.

The researcher also used inductive technique by presenting previous studies, studying some accounting standards for fair value measurement and disclosure, and external auditing standards that guide reviewers in reviewing fair value in financial statements, in order to achieve the quality of external review.

## **Search limits**

The search limits include:-

- The researcher will not address the role of the internal auditor towards reviewing the fair value of investments in securities except to the extent that serves the research.
- The researcher will not address the impact of the global financial crisis on reviewing the fair value of investments in securities except to the extent that serves the research.
- The researcher will not address the details of the scientific framework for measurement and accounting disclosure of the fair value of investments in securities to the extent that serves the research.
- this study deals exclusively with the external review cycle of measurement and disclosure based on fair value and knowledge of the risks and problems involved to the extent that research is relevant to the quality of the external review process.
- the proposed framework is limited to steps and actions related to the risks of fair value disclosure and its relationship to the quality of external audit.

## **Search Plan :**

In order to address the search problem and achieve its goal, the search was divided into the following chapters:

### **Chapter First: The general framework for the concept of fair value**

1/1: Introduction to the chapter

1/2: the concept of fair value

1/3: Entries and Levels of the Fair Value Hierarchy

1/3/1: Entries and methods of measuring fair value

- 1/3/2: Levels of the fair value hierarchy
- 1/3/3: Fair value measurements
  - 1/ 3/3/1: Measuring the fair value of non-financial assets
  - 1/ 3/3/2: Measuring the fair value of the entity's obligations and equity instruments
  - 1/ 3/3/3: Disclosure of fair value information
  - 1/ 3/3/4: The advantages of moving towards fair value accounting
  - 1/3/3/5: Problems and impediments to applying accounting measurement and disclosure on the basis of fair value
  - 1/ 3/3/6: The proposed mechanisms to reduce the problems and obstacles to applying measurement and accounting disclosure on the basis of fair value

## Summary of the first chapter

### Chapter second: The role of the external auditor towards reviewing the fair value of financial investments

- 2/1 The concept of reviewing the fair value of financial investments
- 2/2 The importance of reviewing the fair value of financial investments
- 2/3 The effect of the fair value of financial investments on audit evidence and means of obtaining them
- 2/4 The effect of accounting measurement and disclosure according to the fair value basis for financial investments on the assessment of the elements of the audit risk
- 2/5 The extent of the need to use expert work when reviewing the fair value of financial investments
- 2/6 The role of the Audit Committee as one of the corporate governance mechanisms in reducing the expectations gap when reviewing the fair value of financial investments
- 7/2 Professional publications related to the American Institute of Certified Public Accountants (AICPA) related to the accounting measurement review and disclosure of fair value of financial investments

- 8/2 International professional publications related to the measurement review and accounting disclosure of the fair value of financial investments and the corresponding Egyptian standards
- 2/8/1 International Auditing Standard (ISA No.540)
- 2/8/2 International Auditing Standard (ISA No.545) issued in the year 2004 and corresponding to the Egyptian Standard No. (545)
- 2/8/3 Amended International Auditing Standard 540 issued in 2009
- 2/9 The problems and challenges facing the external auditor when reviewing the fair value of financial investments
- 2/10 The proposed mechanisms to reduce the problems and challenges facing the external auditor when reviewing the fair value of financial investments
- 2/11 The concept of investments in securities
- 2/12 The concept of the quality of the professional performance of the external auditor
- 2/13 The relationship between the professional doubt of the external auditor and the professional wisdom
- 2/14 The importance of achieving the quality of the professional performance of the external auditor
- 2/15 The audit risks associated with accounting measurement and disclosure based on the fair value of financial investments and their impact on improving the quality of the audit process
- 2/16 The audit risks associated with measurement and accounting disclosure based on fair value and their impact on improving the quality of the audit process

Summary of Chapter Two

### **Chapter three: Expremental Study**

**Abstract**

**Results**

**Recommendation**

## **Reference**

### **Chapter one**

#### **The general framework of the concept of fair value**

##### **Introduction**

Historical cost has remained the concept adopted as a basis for measurement and accounting evaluation, disclosure requirements, initial recognition and subsequent measurement of all items of financial statements due to the objectivity of measurement under this system and its use of neutrality to show results in the financial statements and the inability to manipulate the values that appear in the financial statements. As a result of relying on events and facts in support of the documents that cannot be disputed, however, the authors and users of the financial statements were completely convinced that the historical cost does not reflect the true value at the time of preparing the financial statements and that they may be far from current values.

Therefore, the accounting thought tended to use the fair value as a basis for the measurement of the measurement and the accounting disclosure within the financial reporting system, and therefore increased interest in using the fair value in recognition, measurement, presentation and disclosure, and given that the fair value encountered some objections, it was initially limited to financial instruments that It can be traded in an active market or estimated in an objective way in the absence of an active market, and then the concept of fair value spread in most of the newly issued accounting standards and international financial reporting standards (IFRS) such as IFRS13 "fair value measurements" issued in May 2011.

And to achieve the goal of this chapter, it was divided as follows: -

- The concept of fair value.
- Entries and levels of the fair value hierarchy.
  - Fair value measurements.
  - Advantages of moving towards fair value accounting.
- Problems and obstacles in applying the accredited accounting measurement and disclosure based on fair value.



- The proposed mechanisms to reduce the problems and constraints of applying the approved accounting and disclosure based on fair value.

### **The concept of fair value:**

It was defined by (Muhammad Khalil 2007)<sup>1</sup> The fair value is defined as "the value by which the asset (or security) is exchanged or used in settlement of the obligation in the presence of an active market and expresses the desire, freedom and knowledge of the various parties involved in the exchange or the exchange value of the similar asset or The value determined using objective scientific methods in the event that the active market is not available, such as the present value of future cash flows using an appropriate discount rate in contrast to future risks, and is used as an accounting measurement tool and results in information useful to decision makers.

(Danny Pannese, Alan Deifavero 2010)<sup>2</sup> defined it as Fair Value can be defined as "the price that would be received for an asset, or paid to transfer a liability, in a current transaction between marketplace participants in the reference market for the asset or liability."

And as defined by (Ali Khalil, Mona Maghrabi 2013)<sup>3</sup> as "the value on the basis of which an asset or liability is exchanged through an organized process between participants in the active market, provided that there is independence and knowledge of the item subject to measurement, ability and desire to complete the process, and In the absence of an active market, alternative assumptions and valuation methods are used for the market value, which are proportional to the item being measured at the time of measurement.

<sup>1</sup> - د/ محمد أحمد إبراهيم خليل ، " مدخل مقترح لخصائص جودة معلومات القيمة العادلة في البنوك التجارية - دراسة نظرية تجريبية " ، مجلة الدراسات و البحوث التجارية ، كلية التجارة ، جامعة بنها ، السنة ٢٧ ، العدد الثاني ، ٢٠٠٧ ، ص ٨٦ .

<sup>2</sup> - Danny Pannese & Alan Delfavero , " Fair Value Accounting : Effect On the Auditing Profession " , The Journal of Applied Business Research, vol.26,No.3,May/June,2010,P. 45.

<sup>3</sup> - د/علي محمود مصطفى خليل /د/منى مغربي محمد إبراهيم ، "تقييم مدى ملائمة معلومات التسلسل الهرمي لقياس القيمة العادلة طبقاً لمعيار التقرير المالي الدولي رقم (١٣) في ضوء قواعد حوكمة الشركات " ، المجلة العلمية للتجارة والتمويل ، كلية التجارة ، جامعة طنطا ، المجلد الأول ، العدد الثالث ، ٢٠١٣ ، ص ٤٦٤ .

From the above, it is clear that the concept of fair value depends on a set of basic principles that must be met in order to be able to measure the fair value of financial investments, as follows:<sup>1</sup>

1. Having a topic for exchange.
2. The presence of the two parties to the exchange process (supply and demand).
3. The two parties to the exchange process have the free will to conduct the exchange.
4. The two parties to the exchange process know all the facts related to this process.
5. The existence of an active market in which the free will of the two parties to the exchange process converges.
6. The continuation of the two parties to the exchange process in the exercise of its activity without any tendency to liquidate or substantially reduce the activity.
7. The economic structure surrounding both ends of the exchange process enjoys relative stability.

If a defect occurs in any of the foregoing components, this necessarily affects the correct measurement of the fair value of the financial investments.

According to the accounting standards, the concept of fair value for financial investments has evolved with the continuous developments and amendments of these standards, including, for example, the definition contained in the Egyptian Accounting Standard No. (45) entitled "Fair value measurement."<sup>2</sup> , Which defined fair value as "the price that would be obtained to sell an asset or that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date."

Likewise, fair value has been defined in IFRS No. (13) titled "fair value measurements" as "the price that is delivered to sell an asset or is paid to transfer

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<sup>1</sup> - د/فهم صالح لوندى ، " المحاسبة عن القيمة العادلة فى البنوك التجارية و الافصاح عنها طبقا لمعايير المحاسبة الدولية دراسة تطبيقية فى المملكة الاردنية الهاشمية ، مجلة التجارة و التمويل ، كلية التجارة ، جامعة طنطا ، العدد الاول ، ٢٠٠٢ ، ص ١٢٩ .

<sup>2</sup> - وزارة الاستثمار ، معيار المحاسبة المصرى رقم (٤٥) "قياس القيمة العادلة" الوقائع المصرية العدد ١٥٨ تابع (أ) ٩، يوليو، ٢٠١٥ .

a liability in a transaction under regular conditions between market participants at the measurement date.”<sup>1</sup>

The following is clear from the definition of fair value in accordance with IFRS 13<sup>2</sup>:

1. The fair value represents the current exit price and not the entry price.
2. The exit price of the asset or liability differs from the entry price in theory (conceptual), while the entry and exit prices may be identical in many cases.
3. Fair value is a market-based measurement, not an entity-specific measurement.
4. The fair value measurement focuses on the process of selling the asset or transferring (settling) the liability, not the process of delegating the risks associated with the asset or liability.
5. The process of selling the asset or transferring the obligation is a hypothetical transaction at the date of measurement.

From the previous presentation of the various concepts of fair value of financial investments, the researcher concludes the following:

1. The market value differs from the fair value, as the market value is the market value, whether this market is active or inactive, and the fair value is the market value in the case of an active market.
2. Taking the fair value standard at exit prices (selling price) and neglecting entry prices (current cost).
3. The exchange process should take place in a stable economic environment with a neutral active market.
4. The fair value criterion emphasized that the price used as a basis for determining the fair value must take place in an organized market between the dealers (seller and buyer), both

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<sup>1</sup> -International Accounting Standards Board, International Financial Reporting Standard, IFRS, No.13, "Fair Value Measurement", January, 2013, p. 2. Available at: <http://www.frascandada.ca>. Retrieved at **25/4/2020**.

<sup>2</sup> - Ernst & Young, "IFRS 13, Fair Value Measurement, Important Facts about the new requirement" The global Ernst & Young Organisation, 2012, P 15 .

of whom practice the buying and selling process in normal conditions without effect.

5. The selling prices used in determining the fair value must be determined at the measurement date.

In light of the above, the fair value of financial investments from the researcher's point of view is "the price that can be received from the sale of an asset or payment for a commitment, through an exchange process between active market participants, provided that there is independence, and they have knowledge of the item subject to measurement and ability and Desire to complete the process, and in the absence of an active market, alternative evaluation methods are used that are appropriate for the item being measured at the time of measurement, and that is under normal conditions without effect.

## Fair Value Approaches And Hierarchy

The researcher will study and analyze the entries and levels of the fair value hierarchy in light of International Financial Reporting Standard No. (13) IFRS 13 (corresponding to the Egyptian Accounting Standard No. 45) as follows<sup>1</sup>

## Fair Value Approaches And Techniques

There are three methods of evaluating (measuring) fair value, as follows:

### First: Market Approach

<sup>1</sup> - لمزيد من التفاصيل يرجع في ذلك الى :

- IASB, International Accounting Standards Board, IFRS, No 13 , Op. Cit, Para, B5- B11, PP.18 -19.
- د رضا ابراهيم صالحي، "التوجه معايير المحاسبة نحو القيمة العادلة على الخصائص النوعية للمعلومات المحاسبية في ظل الأزمة المالية العالمية"، مجلة كلية التجارة والعلوم العلمية، كلية التجارة، جامعة الاسكندرية، العدد الثاني، ٢٠٠٩، ص ص ٢٠-٢١.
- د. علي محمود مصطفى خليل، د. منى مغربي محمد ابراهيم، مرجع سبق ذكره، ص ص ٢٦١ - ٢٦٣.
- د. عاصم محمد أحمد سرور، مرجع سبق ذكره، ص ص ٦١٢-٦١٤.
- ابراهيم محمد الطحان، مرجع سبق ذكره، ص ص ٤٤ - ٤٧.
- احمد فاروق السيد محمد فراج، مرجع سبق ذكره، ص ص ٩ - ١٠.
- شيرين شوقي السيد الملاح، مرجع سبق ذكره، ص ص ٣٢ - ٣٥.

This approach is based on determining the fair value of the asset based on the prices declared in an active market and other appropriate information generated by market transactions for identical assets or comparable or similar assets, and the same is true for liabilities, or a group of assets and liabilities. This entry also allows the possibility of using the Matrix Pricing to evaluate some types of financial instruments such as debt securities or bonds, as their evaluation is not only based on the use of the declared prices of these securities in the market, but also the relationship of these securities to the prices of the securities. Standard on the market in mind.

### **Secondly: Cost Approach**

This input reflects the current replacement cost, which represents the amount that is currently required to replace the service capacity or production capacity of the asset, taking into account the previous benefits obtained from the asset (aggregate depreciation). This input is preferred when measuring the fair value of the tangible assets in use. Along with other assets or with other assets and liabilities.

### **Third: Income Approach**

According to this entry, the net future cash flows are converted into a single present value, by discounting these flows according to a specific discount factor based on the declared market prices of the discount rate. This entry depends on management's expectations regarding the future cash flows that the asset is expected to generate, or That is expected to pay off the liability and interest.

### **Summary of the first chapter**

In this chapter, the researcher presented the general framework for fair value. In this regard, the researcher addressed the following points through the study and analysis:

- an introduction
- Concept of fair value
- Entries and levels of the fair value hierarchy

- Fair value measurements
- Disclosure of fair value information
- Advantages of moving towards fair value
  - Problems and obstacles to applying accounting measurement and disclosure on the basis of fair value
  - The proposed mechanisms to reduce the problems and obstacles to applying accounting measurement and disclosure on the basis of fair value

In light of what was covered in the first chapter, the researcher concludes that the orientation of accounting standards towards fair value has become unavoidable, as fair value will become the only accounting measurement model for all financial investments provided that the requirements for obtaining a reliable fair value are met, and despite the many advantages it achieves. International and Egyptian accounting standards are directed towards fair value, but it is accompanied by some problems, the most important of which are: Difficulty reaching the fair value in the absence of observable market prices, and if they are reached, their measurements will be less reliable and this will require a high cost that the establishments bear. Professional organizations work to develop mechanisms to reduce fair value problems.

And in view of the reflection of the development in the foundations of accounting measurement and disclosure on the audit process. The auditing profession had to develop its audit procedures and methods to suit this development, as the multiplicity of accounting measurement and disclosure foundations for the fair value of financial investments placed additional burdens on the auditing profession, and required an additional effort from the external auditor.

Based on the foregoing, the researcher will address in the second chapter the evaluation of the international and Egyptian professional publications related to the fair value review and the impact of the trend towards fair value on the stages and procedures of the review process and a model for the review of accounting estimates at fair value based on professional practice, problems and challenges that the external auditor faces when reviewing the fair value and the proposed strategies to overcome On the problems and challenges that face the external auditor when reviewing fair value.

## Chapter two

# The role of the external auditor towards reviewing the fair value of financial investments

## Introduction

The mutual influence between financial accounting and external auditing is a given issue. Any development in the field of financial accounting usually requires an improvement in the audit, whether this development comes within the scope of the external auditor's work and associated work steps and procedures or within the limits of the responsibilities of the external auditor or in the requirements of qualification and training. The external auditor and assistant from the audit team to meet the practical or technical skills and capabilities required by the accounting development. He fulfilled the necessity of areas of cooperation between the external auditor and specialized experts to meet the requirements of this accounting development <sup>1</sup>.

A set of problems and challenges that face the external auditor regarding the review of measurement and disclosure on the basis of fair value have emerged, and these challenges have arisen from multiple sources, including those related to the complexity and multiple methods of evaluating (measuring) the fair value of financial investments, including what is related to increasing the audit risks associated with measurement and disclosure for this type of Financial investments, including those related to the external auditor's need for procedures, review methods and audit evidence commensurate with the nature of accounting measurement on the basis of fair value, as the external auditor is required to collect evidences of the reasonableness of important assumptions and the appropriateness of the measurement model applied by the establishment, and these challenges inevitably lead to It complicates the task of the external auditor in certifying fair value estimates that have a high degree of uncertainty.

To achieve the goal of this chapter, the researcher addresses the following points:

2/1 The concept of reviewing the fair value of financial investments

2/2 The importance of reviewing the fair value of financial investments

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<sup>1</sup> - د. مصطفى راشد العبادي، "مدى حاجة معايير المحاسبة والمراجعة السعودية لتبني القيمة العادلة كأساس للقياس والاقتراح والمراجعة بالقوائم المالية - دراسة تحليلية مقارنة"، الندوة الثانية عشر لمهنة المحاسبة في المملكة العربية السعودية وتحديات القرن الحادي والعشرين، كلية إدارة الأعمال، جامعة الملك سعود، مايو، ٢٠١٠، ص ٢٨.

- 2/3 The effect of the fair value of financial investments on audit evidence and means of obtaining them
- 2/4 The effect of accounting measurement and disclosure according to the fair value basis for financial investments on the assessment of the elements of the audit risk
- 2/5 The extent of the need to use expert work when reviewing the fair value of financial investments
- 2/6 The role of the audit committee as one of the corporate governance mechanisms in reducing the expectations gap when reviewing the fair value of financial investments
- 2/7 Professional publications related to the American Institute of Certified Public Accountants (AICPA) related to auditing measurement review and accounting disclosure of fair value of financial investments.
- 2/8 International professional publications related to the measurement review and accounting disclosure of the fair value of financial investments and the corresponding Egyptian standards.
- 2/8/1 International Auditing Standard (ISA No.540)
- 2/8/2 International Auditing Standard (ISA No.545) issued in the year 2004 and corresponding to the Egyptian Standard No. (545)
- 2/8/3 Amended International Auditing Standard 540 issued in 2009
- 2/9 The problems and challenges facing the external auditor when reviewing the fair value of financial investments
- 2/10 The proposed mechanisms to reduce the problems and challenges facing the external auditor when reviewing the fair value of financial investments
- 2/11 The concept of investments in securities
- 2/12 The concept of the quality of the professional performance of the external auditor
- 2/13 The relationship between the professional doubt of the external auditor and the professional wisdom
- 2/14 The importance of achieving the quality of the professional performance of the external auditor



2/15 The audit risks associated with accounting measurement and disclosure based on the fair value of financial investments and their impact on improving the quality of the audit process

2/16 Audit risks associated with measurement and accounting disclosure based on fair value and their impact on improving the quality of the audit process

## Summary of Chapter Two

In this chapter, the researcher discussed the concept and importance of reviewing the fair value of financial investments by identifying the concept and importance of reviewing the fair value of financial investments, as well as identifying the effect of fair value on audit evidence and means of obtaining it, in addition to the effect of measurement and accounting disclosure according to the basis of fair value of financial investments on the assessment. The elements of the audit risk, as was the need for using the expert's work when reviewing the fair value of financial investments, and the role of audit committees as one of the corporate governance mechanisms in reducing the expectations gap when reviewing the fair value of financial investments.

The researcher also dealt with the professional publications related to the American Institute of Certified Public Accountants (AICPA) and the corresponding Egyptian standards related to the measurement and accounting disclosure of the fair value of financial investments.

The researcher also clarified the most important problems and challenges facing the external auditor when reviewing the fair value of financial investments. The researcher concluded that the auditing standards related to reviewing accounting estimates, including fair value estimates, provide general guidance without detailed instructions for reviewing the items of the financial statements that are measured and disclosing them at fair value. Deficiencies in these standards and requires reformulating them.

The researcher concluded that the auditing standards related to the review of accounting estimates, including the fair value estimates, provide general guidance without detailed instructions for reviewing the items of the financial statements that are measured and disclosed at fair value, which represents deficiencies in these standards and requires re-formulation.

The researcher came up with a set of proposed mechanisms to reduce the problems and challenges facing the external auditor when reviewing the fair value of financial investments, using the work of experts, activating the role of

audit committees, and the need to develop the scientific and practical interpretation of the external auditor.

The researcher also dealt with the concept of investments in securities and the concept of the quality of the professional performance of the external auditor, and the researcher clarified the relationship between the professional doubt of the external auditor and the wisdom of the professional while clarifying the importance of achieving the quality of the professional performance of the external auditor.

In light of the previous presentation, it becomes clear to the researcher that as a result of the problems and challenges facing the external auditor when reviewing the fair value measurements and disclosures of financial investments, the risks of the overall review increase, which leads to a decrease in the quality of the external auditor's professional performance. This framework works to manage the risks associated with the process of reviewing the fair value measurements and disclosures of financial investments to reduce the problems and challenges facing the external auditor with the aim of improving the quality of the professional performance of the external auditor.

## **the third Chapter**

### **Experimental study "the proposed framework"**

#### **Introduction**

As a result of the many risk areas that the external auditor may be exposed to when reviewing the items of the financial statements based on fair value (such as financial investments). And in view of the impact of these risks on the audit process, and in view of the importance of the role of the external auditor in reducing the problems and challenges of reviewing the fair value of financial investments.

This leads to a decrease in the quality of the professional performance of the external auditor. Therefore, the researcher presents a proposed framework for the role of the external auditor in improving the quality of the audit process in light of the risks of measurement and disclosure on the basis of fair value.

The researcher presents this framework in the form of a set of stages, steps and procedures that the external auditor must perform when reviewing the accounting measurement and disclosure of the fair value of financial investments and identifying areas that need additional audit procedures or an appropriate response to the assessed risks through planning and implementing additional

audit procedures to collect audit evidence. Which helps the external auditor in bringing the overall risk level to the acceptable level in preparation for expressing an opinion on the financial statements, which leads to reducing the expectation gap in reviewing the fair value measurements and disclosures of financial investments, which leads to improving the quality of the external auditor's professional performance and then the quality of the audit process In light of the risks of measurement and disclosure on the basis of fair value, as follows:

To achieve the objective of this chapter, it was divided into the following two topics:

**section 1:**

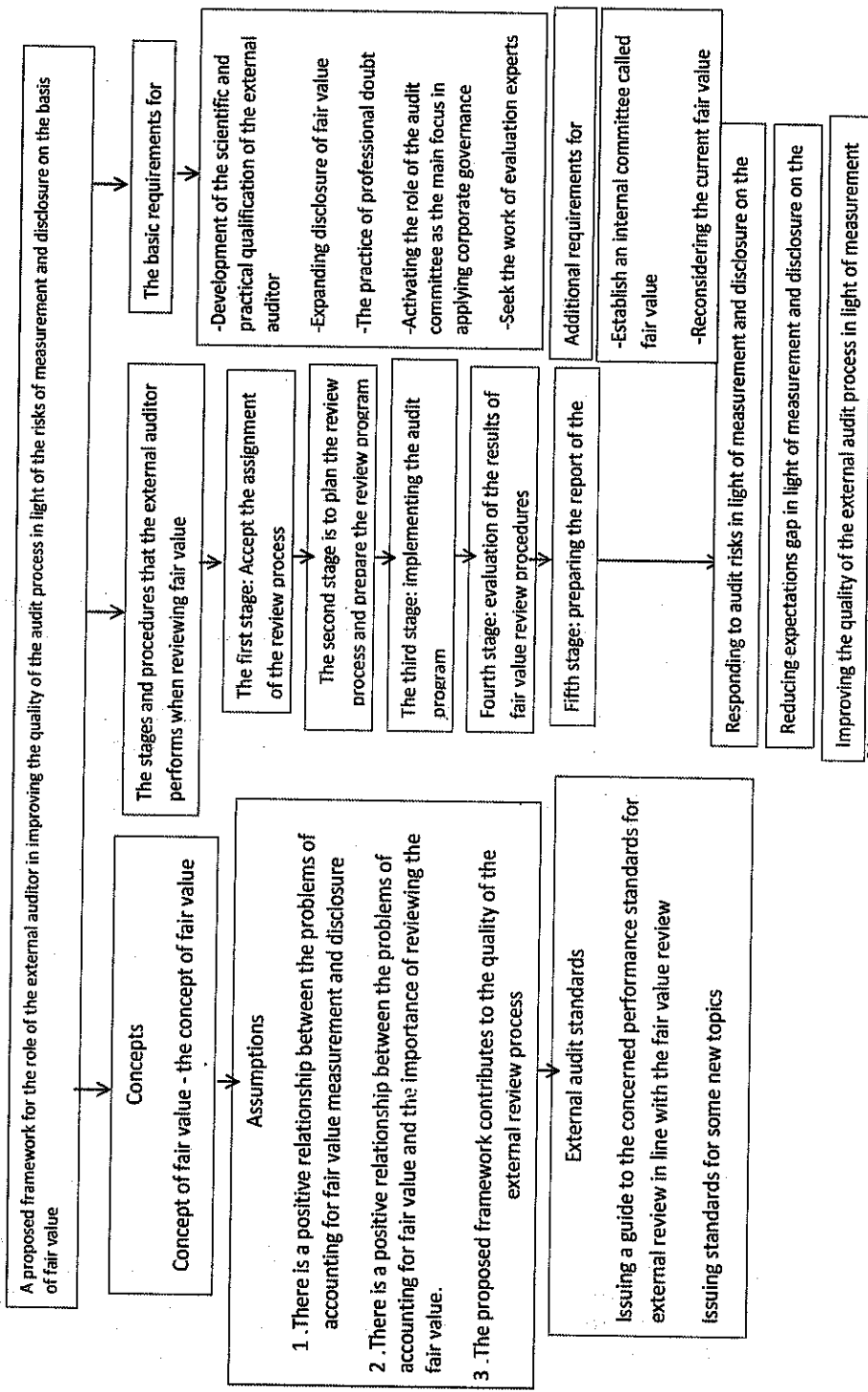
- 3/1 The objective of the proposed framework
- 3/2 The basic concepts for implementing the proposed framework
- 3/3 The assumptions upon which the proposed framework is based
  - 3/4 External Auditing Standards
  - 3/5 The basic requirements for implementing the proposed framework
- 3/6 The stages, procedures and steps that the external auditor performs when reviewing the fair value of financial investments

**section 2:**

- 3/1 The objective of the test study
- 3/2 The study assignments
- 3/3 Study sample
- 3/4 study method
- 3/5 Statistical methods used
- 3/6 Description of the study sample
- 3/7 Descriptive analysis of the study sample
- 3/8 Honesty and Stability Transactions
- 3/9 normal distribution of data

### 3/10 Examining the study hypotheses

The researcher can explain the dynamics of the proposed framework through the following figure:



## Summary of Chapter Three

In this chapter, the researcher reviewed the test study that she carried out, with the aim of determining the validity of the study hypotheses, as well as the appropriateness and validity of the proposed framework for the role of the external auditor in improving the quality of the audit process in light of the risks of measurement and disclosure on the basis of fair value.

The results of the study hypothesis tests were:

- 1-Acceptance of the first hypothesis that states "there is a positive relationship between accounting problems for fair value measurement and disclosure and the quality of the external audit."
  - 2-Acceptance of the second hypothesis, which states: "There is a positive relationship between the problems of accounting for fair value and the importance of fair value."
  - 3-Acceptance of the third hypothesis, which states "the third", the proposed framework contributes to the quality of the external review process.
- 1- The researcher also concluded that there is a positive moral correlation between the external auditor's commitment to the steps and stages of the proposed framework for the fair value review and the fair value accounting disclosure and the quality of the external audit at a significant level of 1% with a correlation coefficient of value ( $R = 0.761$ ). The correlation ratio between the two variables is 76.1. %.

## Findings, recommendations, and suggested areas of research

Findings, recommendations, and suggested areas of research

### 4/1 search results

- 1- The effects of the fair value concept is a great controversy among those interested in the academic and professional side, as the researcher reached after presenting the concept of fair value in the accounting efforts represented in the fair value of financial investments from the researcher's point of view is the "price that can be received from the sale of an asset or payment for transfer Commitment, through a reciprocal process between participants in the active market, provided that there is independence, and they have knowledge of the subject of measurement, the ability and

willingness to complete the process, and in the absence of an active market, alternative evaluation methods are used that are commensurate with the item being measured. At the time of measurement, that is under normal conditions without effect. "

- 2- The market value differs from the fair value, as the market value is the market value, whether this market is active or inactive, and the fair value is the market value in the case of an active market only.
- 3- Taking the fair value criterion (IFRS NO-13) with exit prices (selling price) and neglecting entry prices (current cost).
- 4- The use of fair value accounting results in a set of problems, the most important of which is that the fair value evaluation depends in some cases on methods that depend in large part on personal aspects of management, and thus the evaluation becomes less reliable and reliable, and it can be a fertile field for management bias, whether with intent or Unintentionally and what may result in unfair measurement and presentation of the financial position and the results of the establishment's business, and distortions in profits and property rights, in addition to that the application of fair value accounting needs some complex accounting treatments, whether in measurement or disclosure in the financial statements, which may cause fundamental distortions in the lists Financial, which indicates the importance of reviewing the fair value of financial investments.
- 5- There is an inverse relationship between the required disclosures and the levels of the fair value hierarchy, as IFRS NO.13 requires expansion of disclosure with respect to the lower levels (the third level) in order to reduce the uncertainty and subjectivity problems associated with those measurements due to reliance on personal judgment and likelihood. The bias adopted by the management, as the inputs used at this level are not visible and cannot be verified.
- 6- The professional organizations in their publications of fair value review standards did not address the problems and challenges facing the external auditor when reviewing the fair value of financial investments or providing any solutions to them. Consequently, they do not help the external auditor in reducing these problems and challenges, so the external auditor needs an independent standard. It deals with the fair value review, it contains some illustrative examples of the audit problems and challenges facing the external auditor while performing his work and trying to develop solutions to them

- 7- There are many mechanisms that help reduce the problems and difficulties of measurement and accounting disclosure of the fair value of financial investments, the most important of which is the expansion of disclosure of fair value information to include methods applied, assumptions and inputs used in measuring the fair value of financial investments. This will provide at least a partial solution to the problem of reliability. Complete levels of hierarchy in times of financial crises, the establishment of an internal committee called the fair value committee consisting of several members who have experience and scientific and practical skills.
- 8- The need to use the work of an expert is necessary when the degree of uncertainty associated with the fair value measurements is high, the invisible inputs used in the valuation models are large, the valuation technique is complex, the risks associated with the financial investments subject to fair value assessment are high, the audit evidence from various sources is insufficient and the expected impact on the auditor's report The external is high, as well as when the management relies on the work of an expert in preparing financial statements.
- 9- The need to use professional doubt when evaluating fair value estimates for financial investments, given that these estimates relate to unconfirmed information and relate to the future, which requires the external auditor to deviate from the traditional methods and for the seriousness of this stage, the availability of the characteristics of professional doubt with the external auditor will have a role in accepting or Rejecting the estimates that have been approved by the management of the audit client's facility by obtaining evidence that may collectively or individually indicate the validity of management's assumptions.
- 10- he most important problems facing the external auditor when reviewing fair value are the lack of self-measuring audit evidence, the lack and unfairness of disclosures about how to prepare these estimates, challenges related to the work of experts, the complexity and deficiency of standards associated with reviewing fair value measurements, challenges associated with the widening gap in expectations. The Expectation Gap.

#### **4/2 Results of the test study**

- 1- Acceptance of the first hypothesis, which states: "There is a positive relationship between the problems of accounting for fair value measurement and disclosure and the quality of the internal audit."



process in light of the risks of measurement and disclosure on the basis of fair value.

#### 4/4 Proposed areas of research

- 1- The researcher recommends conducting more studies and research on the tax aspects of the fair value of financial investments
- 2- The effect of accounting standards orientation towards fair value of financial investments on the fees of the audit process.
- 3- The effect of accounting standards orientation towards fair value of financial investments on the fees of the audit process.

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- 2- Accepting the second hypothesis which states "there is a positive relationship between the problems of accounting for fair value and the importance of reviewing the fair value."
- 3- Acceptance of the third hypothesis which states "the proposed framework contributes to the quality of the external review process."
- 4- Study sample individuals agree that the availability of the stages of the proposed framework within the study community will contribute to developing the role of the external auditor in improving the quality of the audit process in light of the risks of measurement and disclosure on the basis of fair value by 55% and that at a significant level of 1%, which indicates the importance of applying Framework stages within the current society and similar societies to study.

### 4/3 Research Recommendations

In light of the research's purpose, its importance, and the findings of the theoretical and experimental study, the researcher recommends the following:

- 1- The necessity for professional organizations in Egypt to issue a new auditing standard related to the review of accounting estimates, including accounting estimates for fair value, through the merging between the Egyptian Auditing Standard No. (540) entitled (Observance of Accounting Estimates) and the Egyptian Auditing Standard No. (545) Entitled (Review of fair value measurement and disclosure) so that Egyptian standards are consistent with international standards.
- 2- Paying attention to teaching fair value accounting in the accounting and auditing departments of the College of Commerce to increase awareness and knowledge of its concept, importance, stages and procedures.
- 3- Conducting continuous training courses for the external auditor to increase his skills and experience in the field of reviewing the fair value of financial investments to improve the external audit process in light of the risks of measurement and disclosure on the basis of fair value.
- 4- The researcher also recommends the external auditor to use the proposed framework for the role of the external auditor in improving the quality of the audit