



Ferdowsi University of Mashhad

RESEARCH ARTICLE

Auditor Management by the Client using the Omissions and Auditor's Assessment of the Misstatements Detection: Bait for the Auditor Management

Fatemeh Zholanezhad, Ehsan Kamali*, Arezoo Aghaei Chadegani

Department of Accounting, Najafabad Branch, Islamic Azad University, Najafabad, Iran

How to cite this article:

Zholanezhad, F., Kamali, E., & Aghaei Chadegani, A. (2022). Auditor Management by the Client using the Omissions and Auditor's Assessment of the Misstatements Detection: Bait for the Auditor Management. *Iranian Journal of Accounting, Auditing and Finance*, 6(4), 29-43. doi: 10.22067/ijaaf.2022.42123
https://ijaaf.um.ac.ir/article_42123.html

ARTICLE INFO

Abstract

Article History

Received: 2022-06-12

Accepted: 2022-08-31

Published online: 2022-10-07

Keywords:

Auditor Management, Clean Accounts, Fraud Detection, Misrecorded Transaction Strategy, Omission Strategy, Omissions Bias

One of the strategies of audited firms' management is to divert the auditor's attention from the managed accounts to clean accounts (without misstatement) or accounts that contain misstatements other than managed accounts to affect the auditor's ability to detect fraud. The experimental method and a sample include 106 auditors in 2022. We examine whether managers attempt to reduce the perceived intentionality of their fraudulent misstatements by perpetrating fraud via omission, as opposed to a more active form of commission, and how auditors evaluate the resulting misstatements. We find that managers choose to omit a transaction from the financial statements rather than record a transaction inappropriately. They also decide to omit critical information from supporting documents rather than provide misleading information. However, auditors generally believe that misstatements involving omissions are unintentional. Specifically, we find that auditors are less skeptical of an omitted transaction than a misrecorded transaction. They are also less skeptical of a misstatement that results from management omitting information from a supporting document than misrepresenting information. Finally, a method of fraud (omission) is identified that those managers are likely to use; on the other hand, those auditors are unlikely to judge it as intentional.

 <https://doi.org/10.22067/ijaaf.2022.42123>



NUMBER OF REFERENCES

45



NUMBER OF FIGURES

-



NUMBER OF TABLES

8

Homepage: <https://ijaaf.um.ac.ir>
 E-Issn: 2588-6142
 P-Issn: 2717-4131

*Corresponding Author: Ehsan Kamali
 Email: ehsankamali_acc@yahoo.com
 Tel: 09131054518
 ORCID:

1. Introduction

Several researchers and professional fraud examiners have emphasized the need for the early detection of fraud. Though there are many ways in which frauds can be detected, a particularly effective and inexpensive way is to identify fraudsters by scrutinizing personnel behaviour for peculiarities typical of fraudsters (Sandhu, 2022). Managers are trying to hide accounts manipulation because if the manipulations made for earnings manipulation and followingly earnings management become apparent, they will no longer benefit management (Dechow et al., 2012). Therefore, the managers try to prevent auditors from detecting managed (manipulated) accounts (Petty and Cacioppo, 1986). This aspect of management behavior is called auditor management. Auditor management covers a wide range of methods; one of the most important ones is distraction and baiting. This study tries to determine whether auditors will detect misstatements in managed accounts using the client's management's document manipulation (baiting and deflection) techniques. The important aspect from the auditors' viewpoint is that their interests are associated with fraudulent actions that cause significant misstatements in the financial statements (Moradi, Rostami and Zare 2014). Managers may divert auditors' attention to accounts that are considered free of misstatements and distortions, which are called clean accounts, or they may divert auditors' attention to distorted accounts (to be more exact, these distortions do not affect earnings, on the other hand, only have been generated from earned management accounts to mislead, or to divert auditors' attention) (Luippold et al., 2015).

There are two primary methods by which an intentional misstatement can be achieved: "misrepresentation or intentional omission from the financial statements" (PCAOB, 2002b). That is, when committing fraud, a client manager can either choose to *actively* misrepresent, alter, and/or falsify information contained within the financial statements and supporting documents (e.g., record a fictitious sale or capitalize a valid expense) or omit, through *inaction*, a necessary transaction or piece of information (e.g., fail to record an incurred expense or valid sales return). Archival evidence suggests that most frauds are perpetrated via active forms of misrepresentation, such as recording fictitious sales and recognizing revenues prematurely, while far fewer frauds are perpetrated by omitting necessary transactions (e.g., omitting expenses and liabilities) (Dechow et al., 2011; Beasley et al., 2010). However, this characterization of fraud seems inconsistent with psychology theory, which indicates that individuals prefer to bring about morally objectionable outcomes via omission (i.e., inaction) as opposed to commission (i.e., action) (Ritov and Baron 1999; Baron and Ritov 2004; DeScioli, Bruening and Kurzban 2011b).² In this paper, we examine whether financial reporting managers perpetrate fraud using an "omission strategy" (DeScioli, Bruening and Kurzban 2011b). We also examine auditors' perceptions of misstatements resulting from omission compared to a more active form of commission. Theory from psychology suggests auditors may be inclined to believe a misstatement resulting from omission is unintentional (i.e., due to error rather than fraud) (Spranca, Minsk and Baron 1991). This study is unique because human behavior as a possible fraud indicator is an under-researched area, and Implications for anti-fraud practitioners are discussed. In the following, the framework of theoretical foundations and the development of hypotheses and research method, findings and conclusions are reviewed.

2. Background and Hypothesis Development

Auditor management is considered a client strategy in which the manager uses various techniques to reduce the likelihood of discovering the accounts that are regarded as managed by auditors. Auditor management can include a variety of methods; For example, managers may provide evidence to auditors in a way that manipulates the risk of audit (Jamal, Johnson and Berryman 1996), or they may provide incomplete or incorrect information to conceal auditors' questionable accounting practices;

while this research refers to baiting techniques for auditors management. Some research has been conducted on manipulating management information to manage auditors. These studies include the provision of incomplete information and the presentation of evidence. Managers may also divert auditors' attention to other areas to prevent the discovery of earnings management.

Hamilton and Smith (2021) showed that managers prefer to remove a transaction from the financial statements instead of recording a transaction improperly. Managers also remove important information from supporting documents instead of providing misleading information. However, auditors generally believe that misstatements include removing unwanted items, and auditors are less skeptical of a deleted transaction than of a recorded incorrect transaction. They are also less sure about the misrepresentation of information than of misrepresentation resulting from removing document information from backup documents. Caramanis and Lennox (2008) concluded that if client management could divert auditors to other areas through baiting techniques, it would lead to more working hours in those areas and, as a result, less time to review other sites. Consequently, this matter gives earnings management an opportunity for client management. As a result, auditor management will be a fertile ground for future research. The focus of this study will be on distracting auditors, While research on auditor management is limited.

Psychological research on distracting peoples' attention suggests that distraction reduces efficiency (Freudenburg and Alario, 2007). In their paper, Freudenburg and Alario (2007) examined several currents in the legitimacy literature. They found that the disappearance of evidence from an issue could be effective in the eyes of individuals. In this way, the magicians' trick is effective when their trick is hidden from the eyes of the people. They do this by directing people's attention or keeping their eyes away from body movements; So that their tricks remain unseen. Also, a negotiator wins when the evidence for his/her position remains unknown. Research on convincing suggests that distraction makes people more likely to agree with others; distraction has a detrimental effect on perception (Petty and Cacioppo, 1986; Baron, Baron and Miller, 1973). Researches into the details of the probability expansion model (to shape individuals' attitudes) show that distracting individuals makes the cognitive process much more difficult; Because this leads to more secondary information processing (Petty and Cacioppo, 1986; Street et al., 2001). The probability expansion model states that attitudes can be formed through two processes: central attitude or external and lateral attitude. The central approach involves careful thinking and analysis of all the details. Lateral attitude involves the superficial processing and reliance on the peripheral characteristics of a message; For example, some may agree with a message just because it was transmitted from a trusted source, regardless of the content of the message; For example, limited and stressful time budgets make auditing operations ineffective due to the impossibility of detecting significant distortions and also reduce operational efficiency in terms of time and personnel costs. Also, if it distracts people beyond the capacity of their analytical power, decision-making and judgment will be disrupted (Behzadian and Izadi Nia, 2018); it places a lot of pressure on auditors' minds regarding their self-control. This issue can influence auditors' judgment and decision-making (Daryaei and Kholousi Moshfegh, 2020).

As well as that, researches into the effects of information tracking, either in psychology or in accounting, suggest that the effect of deviance on the performance of professional auditors may both hinder and enhance the performance of auditors; As a result, searching for a predetermined part to obtain information increases people's reaction to the information they have found (Baron, Baron and Miller, 1973). This increases people's reaction to the information obtained in the predefined sections, called the information tracking effect. Several scenarios may occur when auditor attention is diverted to other accounts:

1. The auditor's mind and time are occupied with reviewing that account, and they may not, in the end, spend the proper time and carefully reviewing the other accounts.

2. If auditors deviate from clean accounts, they may feel that other accounts are necessarily free of material misstatement and reduce the scope of their review.
3. If auditors deviate from distorted accounts (distortions that are for tracking and do not include earned management accounts), they may feel satisfied after discovering that misstatements or distortion and think that they have done their job and ignore other accounts and, as a result, accounts that have been managed remain undiscovered.
4. According to information tracking theories and professional skepticism, auditors may expand their searches questioningly when they deviate to erroneous accounts and eventually discover management accounts. Those managers choose to perpetrate fraud through omission rather than commission—an important related question is whether auditors are less skeptical of misstatements resulting from omission than commission. While most of the audit literature related to fraud detection has examined auditors' fraud-related audit planning judgments (Wilks and Zimbelman 2004; Carpenter 2007; Hoffman and Zimbelman 2009; Hammersley, 2011, for a review of the fraud planning literature), it cannot be assumed that once a fraudulent misstatement is identified, it will be accurately evaluated as fraudulent. Psychology research provides evidence that third-party observers often are susceptible to an “omission bias” wherein they perceive omissions as less intentional and less blameworthy than acts of commission (Anderson 2003; Cushman, Young and Hauser 2006; DeScioli, Bruening and Kurzban 2011b). Importantly, omissions are judged less harshly, even when omission and commission result in identical outcomes (Spranca, Minsk and Baron 1991; Kordes-de Vaal, 1996).²¹ Omissions are less intentional because they do not indicate a choice, making the actor's intentions unclear (Kordes-de Vaal 1996; DeScioli, Christner and Kurzban 2011a). Therefore, it is unclear whether inaction was chosen or resulted from unawareness that action was needed. If a manager fails to record a sales return, it is unclear whether the manager intended to overstate revenues or simply forgot to record the transaction. In contrast, a manager who records revenue prematurely took an observable and inappropriate action, making it appear more intentional.

Accordingly, we proposed that auditors will judge identified misstatements as less likely to be intentional when they result from omission compared to a more active form of commission. Specifically, we proposed that auditors will judge a misstatement as less likely to be intentional when it relates to a transaction that was improperly omitted from the financial statements compared to a transaction recorded inappropriately. Auditors will judge an identified misstatement as less likely to be intentional when it involves an omitted transaction than a misrecorded transaction. Thus, the first hypothesis is:

H1: In the face of distorted financial statements using the omission strategy, auditors consider that the identified misstatements are unintentional.

When a misstatement is identified, auditors typically review supporting documents associated with the transaction (e.g., sales order forms, invoices, contracts). Such supporting audit evidence can provide auditors with information about the misstatement and the client's actions (or inaction) that led to the misstatement. According to auditing standards, fraud may be concealed by withholding evidence or misrepresenting information (PCAOB 2002b). The omission bias may also be relevant to how auditors perceive inaccuracies in the audit evidence underlying an identified misstatement. Specifically, we expect auditors will judge a misstatement as less likely to be intentional when a supporting document *omits* relevant information than when the document contains information that *misrepresents* the nature of the transaction. Auditors will judge an identified misstatement as less likely to be intentional when it results from an omission of relevant information from a supporting document compared to a misrepresentation of relevant information. Thus, the second hypothesis is:

H2: In the face of distorted financial statements using the manipulation strategy, auditors consider that the identified misstatements are intentional.

According to Miller, [Zweben and Johnson \(2005\)](#), values are social models that a group of people accepts. Going through details provides a basis for creating common expectations and guiding and regulating behavior, depending on people's acceptance. According to [Rokeach \(1973\)](#), value belief is relative stability on which a person prefers a particular behavior to another behavior ([Freudenburg and Alario, 2007](#)). Value is a complex concept that can be divided into individual or personal, collective and cultural values. [Schwartz \(1994\)](#) has defined value as desirable goals, each of which is of different importance and is used as guiding principles in people's lives ([Schwartz, 1992](#)). Personal values describe individual and social classifications ([Schwartz, 2006](#)), explore value-based relationships and fundamental variables, and predict individuals' attitudes and daily behaviors ([Schwartz, 1994](#)). When we talk about values, we talk about what is essential in people's lives. Each person has different values with different degrees of importance. Values vary from person to person ([Schwartz, 2006](#)), and some studies point to the effect of personal values on decision making and judgment ([Mashlah, 2015](#)).

Values influence decisions, attitudes and behaviors; Therefore, the roots of auditor judgments can be traced to values. [Mashlah \(2015\)](#) believes values influence attitudes, behaviors, decisions, motivations and ethics. Professional judgment is critical in auditing, affecting the whole audit process. Making sound professional judgments is an essential factor in performing the duties of an auditor, and increasing the skill of judging is essential for auditors ([Khoshtinat and Bostanian, 2007](#)). Therefore, in the current situation, one of the complexities of accounting and auditing that needs to be considered is the personality characteristics of judges, which are not mentioned in any standard book; Because judgment is present in the whole process of audit operations. According to paragraph 16 of Standard 200 of the Iranian Audit, the auditor must use professional judgment in the planning and execution of the audit of the financial statements. Therefore, the need to pay attention to the values of the person influencing the attitude and behavior of auditors and, ultimately, the auditors' judgment is important. Also, by influencing the behavior and attitude of auditors, personal values can have a major impact on the decision-making and judgment of auditors in the entire audit process, including detecting distortions in the financial statements. People try to behave in a way that is consistent with their values. Therefore, the third hypothesis is:

H3: Auditors with personality characters of idealism (or moral idealism) are more capable of detecting fraud than pessimistic auditors.

[Rahmawati and Indrijawati \(2020\)](#) examined the effect of auditor experience, work, and doubt personality professions on auditors' ability to detect fraud. Respondents in the study included KAP auditors in the Jakarta, Surabaya and Makassar regions with purposive sampling techniques. Distributing questionnaires to the respondents was the data collection method used in this study. Additionally, multiple linear regression analysis was used for the data analysis method. This research is very useful for auditors in order to detect fraud. To explain more, the results showed that audit experience variables, workload, and professional skepticism positively affected the auditor's ability to detect fraud. In contrast, personality variables did not influence the auditor's ability to detect fraud.

[Pratoomsuwan and Yolrabil \(2020\)](#) examined a preliminary understanding of how fraud and undetected errors affected auditor responsibility. This study provided a preliminary understanding of how undetected fraud and error misstatements affected auditor liability, given the same outcome

severity. A 2x2 between-subject experiment was conducted using undergraduate accounting students to represent evaluators who had high levels of auditing knowledge and nonaccounting students to represent evaluators with low levels of auditing knowledge. The experiment results indicated that evaluators with high auditing knowledge assessed auditors as less liable in cases of undetected misstatements due to fraud rather than an error. In contrast, less knowledgeable evaluators rated auditors as more liable in such cases. The findings of this study provided some insights that benefited the audit profession, standard setters and the Security and Exchange Commission regarding the auditor's responsibility related to fraud. This proved that other misstatements (fraud and error) helped reduce differences in auditor liability judgments, mainly when evaluators evaluated misstatements with different levels of auditing knowledge. This finding also suggests that the auditor litigation risk created by the expectation gap will remain despite any attempt to minimize it. [Widodo and Chariri \(2021\)](#) examined the relationship between auditing procedures, auditors' experience, and auditors' responsibility for detecting fraud. Auditors' responsibility for fraud detection acted as the dependent variable, whereas the independent variables were audit procedures and auditors' experience. The control variables of the study were gender and position. Empirical test results were obtained from auditors working at fourteen public accounting firms in Indonesia. The findings showed that the audit procedures and auditors' experience positively influenced the auditors' responsibility for fraud detection. This study contributed to auditing and accounting literature, precisely the fraud detection method used to increase the awareness of fraud risk. [Verwey and Asare \(2022\)](#) examined the combined effect of ethical idealism and pessimism on auditors' fraudulent judgments. The results highlighted the importance of measuring and controlling for the effects of these traits when evaluating fraud detection performance. The paper also showed that an ethics theory could generate additional understanding and insights into an important accounting phenomenon.

[Hamilton and Smith \(2021\)](#) investigated the effect of management fraud strategies on auditors' judgments of identified distortions. The experiment results showed auditors were less skeptical of an omitted transaction than a misrecorded transaction. They were also less doubtful about a misstatement of information compared to misrepresenting information. Finally, a method of fraud was identified that managers were likely to use, but auditors were unlikely to judge it as intentional.

3. Research Methodology

This research is a descriptive-correlation study conducted to investigate the auditor management by the client using the omissions and auditor's assessment of the misstatements detection. Univariate analysis of variance (ANOVA) and one sample (T-Test) were used to test the hypotheses. The Levin test was used in the ANOVA univariate analysis of variance to evaluate the homogeneity of variance of groups. If the significance level of the Levin test is higher than 0.05, it indicates homogeneity of variance. Data were collected using a questionnaire. The standard questionnaire was designed based on the Likert scale. To test the first and second hypotheses, [Hamilton and Smith's \(2021\)](#) research scenario and to examine the third hypothesis, [Verwey and Asare's \(2021\)](#) research questionnaire has been used. Finally, in order to ensure the validity of the scenario and the questionnaire, before the final distribution among the sample members, the scenarios and questionnaires were reviewed by a number of auditors working in the audit organization and audit firms and their opinions were applied. Scenario 1 assesses the auditor's judgment in the face of distorted financial statements using an omissions strategy. Scenario 2 assesses the auditor's judgment in the face of distorted financial statements using a strategy of manipulating evidence ([Hamilton and Smith, 2021](#)). In the end, the auditor is asked questions about the auditor's personal values (idealism or moral idealism and pessimism). Managers try to hide earnings manipulation. Because if the manipulations made for fraud are revealed, it will no longer benefit the management. Therefore, the manager is trying to prevent

the auditors from discovering the tampered accounts. This aspect of earnings manipulation is called auditor management. Auditor management covers a wide range of methods; one of the most important ones is distraction and baiting. The question is whether auditors will detect misstatements in earnings management accounts when using earnings manipulation techniques (baiting and deflection) by the client's management. The important aspect from the auditor's point of view is that their interests are intertwined with fraudulent acts that cause significant misstatements in the financial statements. Managers may divert auditor attention to accounts free of misstatements and distortions, called clean accounts, or they may divert auditor attention to distorted accounts (distortions that do not affect earnings, only to mislead or to divert). Auditor attention is generated from earnings manipulation accounts. So, everyone has a set of personal values that influence their day-to-day decisions, as these values play an essential role in decision making, preferences, perceptions and even emotions. These values may vary from person to person. Therefore, personal values influencing the behavior and attitude of auditors can significantly affect the decision and judgment of auditors in the entire audit process, including detecting distortions in the financial statements. Personal values profoundly affect people's performance, sense of satisfaction, and way of thinking. Thus, each individual may react differently when placed in different situations, and using a particular technique may lead to different outcomes depending on the characteristics of the individual. Personal values and their extent differ in all individuals, and individuals make decisions and judgments according to their values. Therefore, in addition to examining the effect of the baiting technique on auditor performance, it is necessary to examine their personal values to understand the roots of this issue better. The reason is that in addition to baiting techniques, personal values also affect performance and, ultimately, the judgment and detection of fraud. In the present study, following the research of [Verwey and Asare \(2022\)](#), idealism or moral idealism and pessimism have been used as personal values for the auditor.

Finally, they were analyzed using SPSS software after collecting the required data. As a result, Cronbach's alpha was used to measure the reliability of the questionnaire. Content validity was used in this study. Experts' and experienced professors' viewpoints were used to assessing the questionnaire's validity. Cronbach's alpha was used to assess the reliability of the questionnaire, which was 0/88. As a result, since Cronbach's alpha value was greater than 0/70, the questions of the research questionnaire had good reliability.

The statistical population of this study is considered all auditors (senior auditors, supervisors and senior supervisors) working in auditing firms who are members of the Iranian Society of Certified Public Accountants and Audit Organization in 2022. Due to the infinity of the statistical community, without the placement of the infinite community, the scenarios are distributed among the members of the available statistical community. A random sampling test without placement of unlimited community is used for sampling. Since it was not possible to study the whole community, available sampling was used. The available statistical population includes 106 auditors. The results of descriptive statistics of research participants in terms of gender, age, education, experience and their position showed that 85% of male and 15% of female auditors, 78.3% of auditors, 11.7% of auditing and 10% of management (Economy = 0), the age of 20% of auditors is between 20-30 years and 35% between 40-40, 30% between 40-50 and 11.7% between 50-60 and 3.3% over 60. Audit history is 50% between 1-10 years, 26.7% between 11-20 years, 15% between 21-30 years and 8.3% above 30. 13.3% have a bachelor's degree, 70% have a master's degree, and 16.7% have a doctorate. 16.7% are partners, 20% are audit managers, 16.7% are supervisors, 25% are senior auditors, and 21.7% are auditors. 86.7% are employed in auditing firms, and 13.3% are employed in auditing organizations.

4. Research Findings

In this study, we examine whether auditors are less skeptical of misstatements that result from omission compared to a more active form of commission. Through a series of experiments, we examine two methods by which omissions could be used to perpetrate and conceal fraud: (1) by omitting a transaction from the financial statements and (2) by omitting information from a supporting document. Tables (1) to (8) present the average of each auditor's judgments. The auditor's judgment in the face of the client's strategies ((1) by omitting a *transaction* from the financial statements and (2) by omitting *information* from a supporting document) is presented below.

Table 1. One-Sample Statistics for Omission Strategy

	N	Mean	Std. Deviation	Std. Error Mean
Scenario 1	106	2.700	1.565	0.202

The mean of participants in scenario 1 is 2/7, and the evidence shows that 33% were completely unintentional, 22% somewhat unintentional, 22% somewhat intentional, 18% completely intentional, and 5% theoretical.

Table 2. One-Sample Test for Omission Strategy

Test Value = 0						
	T	df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference	
					Lower	Upper
Scenario 1	13.359	105	0.000	2.700	2.295	3.104

The significance for scenario 1 is equal to 0. The results showed that in the face of distorted financial statements using the strategy of omission, auditors consider that the identified misstatements are unintentional.

Table 3. One-Sample Statistics for Manipulating Evidence Strategy

	N	Mean	Std. Deviation	Std. Error Mean
Scenario 2	106	3.966	1.261	0.162

The mean of participants in scenario 1 is 3/96, and the evidence shows that 48% were completely unintentional, 23% were somewhat intentional, 13% were unintentional, 10% had no opinion, and 5% were completely unintentional.

Table 4. One-Sample Test for Manipulating Evidence Strategy

Test Value = 0						
	T	df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference	
					Lower	Upper
Scenario 2	24.351	105	0.000	3.966	3.640	4.292

The significance for scenario 1 is equal to 0. The results of Table (4) showed that auditors consider that the identified misstatements are intentional in the face of distorted financial statements using the strategy of manipulating evidence. In this study, managers choose to perpetrate fraud by omitting an expense transaction rather than misrecording a revenue transaction. Managers also commit fraud by omitting relevant information from a supporting document rather than misrepresenting the nature of the transaction. As well as that, in this study, we find that auditors judge a misstatement as less likely to be intentional when it involves omission (i.e., an omitted expense transaction or information omitted from a supporting document) compared to a more active form of manipulation. Taken together, these results suggest the methods of fraud likely to be chosen by managers are also the methods auditors are unlikely to judge as fraudulent.

The auditor's judgment in the face of the client's strategies (1) by omitting a *transaction* from the financial statements and (2) by omitting *information* from a supporting document) Among auditors with ethical values (idealism or moral idealism and pessimism) are presented below.

Table 5. ANOVA for Idealism in the Omission Strategy

Scenario 1					
	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	43.807	7	6.258	3.229	0.006
Within Groups	100.793	98	1.938		
Total	144.600	105			

Table (5) shows the results for idealist auditors whose clients have used the omission strategy. **Table**

6. ANOVA for Pessimism in the Omission Strategy

Scenario 1					
	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	24.724	6	3.090	1.315	0.258
Within Groups	119.876	99	2.351		
Total	144.600	105			

Table (6) shows the results for pessimist auditors whose clients have used the omission strategy. The significance in the ANOVA test for idealism in the omission strategy is equal to 0.006. Still, the significance of the ANOVA test for pessimism in the omission strategy is equal to 0.258. The results show that auditors with personality Characters of idealism or moral idealism are more capable of detecting fraud in the omission strategy than pessimistic auditors.

Table 7. ANOVA for Idealism in the Manipulating Evidence Strategy

Scenario 2					
	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	35.361	10	4.420	3.849	0.001
Within Groups	58.573	95	1.148		
Total	93.933	105			

Table (7) shows the results for idealist auditors whose clients have used the manipulating evidence strategy.

Table 8. ANOVA for Pessimism in the Manipulating Evidence Strategy

Scenario 2					
	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	23.402	9	3.343	1.465	0.290
Within Groups	70.531	96	1.356		
Total	93.933	105			

Table (8) shows the results for pessimist auditors whose clients have used the manipulating evidence strategy. The significance of the ANOVA test for idealism in the omission strategy is 0.001. Still, the significance of the ANOVA test for pessimism in the omission strategy is equal to 0.290. The results show that auditors with personality characteristics of idealism or moral idealism are more capable of detecting fraud in manipulating evidence than pessimistic auditors. As a result, the third hypothesis is not rejected, and Auditors with personality characteristics of idealism or moral idealism are more capable of detecting fraud than pessimistic auditors.

5. Discussion and Conclusions

To detect fraudulent financial reporting, auditors not only must identify a misstatement but also correctly conclude (initially or following additional investigation) that the misstatement resulted from an intentional act. Therefore, auditors must be able to judge the likelihood that an identified misstatement was caused intentionally effectively. Unfortunately, this ability may be compromised if managers strategically choose methods of perpetrating fraud that appear less intentional on the surface. The issue of confusing or distracting auditors reduces the effectiveness of auditors. Therefore, auditors need to be careful that management does not distract them. Many psychological types of research have been done on the effect of attention deficit, information pursuit, the mental capacity of individuals, and personal values' effect on people's judgment. But a few types of research have been done on the relationship between deviation and auditor attention as a baiting strategy to conceal earnings management accounts.

Since the omitted transaction is always an expense and the misrecorded transaction is always considered a revenue, we conduct a study with auditor participants that disentangles the relative effects of the (in)action that caused the misstatement (omitted versus misrecorded transaction) and

the account involved (expense versus revenue). Consistent with previous results, auditors exhibit reduced skepticism in response to omitted transactions compared to misrecorded transactions. Accordingly, the first hypothesis of the research is confirmed. In the face of distorted financial statements using the strategy of omission, auditors consider that the identified misstatements are unintentional. The result of the first hypothesis is consistent with [Hamilton and Smith's \(2021\)](#) research. While the nature of this reduced skepticism differs based on the account involved (revenue or expense), in all instances, auditors respond less sceptically to misstatements resulting from omission. Based on this, the second hypothesis of the research is confirmed. In the face of distorted financial statements using the strategy of manipulating evidence, auditors consider that the identified misstatements are intentional. The result of the second hypothesis is consistent with the research of [Hamilton and Smith \(2021\)](#). Our study contributes to the literature on fraudulent financial reporting and its detection by auditors. While prior research demonstrates that managers attempt to conceal their fraudulent misstatements ([Zimbelman and Waller 1999](#); [Bowlin 2011](#)), our study suggests managers also try to conceal their fraudulent intentions by perpetrating fraud in ways that appear less intentional the resulting misstatement becomes identified. Similarly, the audit literature on fraud detection has primarily focused on auditors' ability to identify fraudulent misstatements (e.g., via fraud risk assessments and planning procedures) ([Wilks and Zimbelman 2004](#); [Carpenter 2007](#)). However, it cannot be assumed that once a misstatement is identified, it will be accurately evaluated as fraudulent. Therefore, we extend the audit literature by examining factors that influence auditors' evaluations of identified misstatements—specifically, factors that cause a misstatement to be perceived as more or less intentional. Our research findings should also be of interest to audit practitioners and regulators. While auditing standards require auditors to consider whether identified misstatements may have been caused intentionally (PCAOB, 2010), little evidence exists regarding the effectiveness of these evaluations. Our study suggests that when managers use an omission strategy, auditors are inclined to dismiss the resulting misstatements as unintentional. As such, auditors would benefit from additional education and training that increases their awareness of this fraud strategy and encourages them to be more skeptical of misstatements characterized by omission.

Thus our findings that managers choose to perpetrate fraud by omitting expense transactions may seem inconsistent with archival fraud data that suggest most frauds involve the improper recording of revenues. However, our auditor studies' results can help explain this apparent inconsistency. Specifically, our studies suggest that in addition to misrecording revenues, managers may also be perpetrating fraud by omitting expenses. Still, fewer of these omissions are identified as fraudulent since auditors are more likely to dismiss omissions as unintentional errors. It is also worth noting that we find evidence that auditors are less skeptical of expense misstatements than revenue misstatements. This may further help to explain why most identified frauds involve revenues that were recorded inappropriately, while far fewer involve omitted expenses—namely; auditors may believe certain misstatements (e.g., those involving omissions and/or expenses) are unlikely to be fraudulent. More research is needed to understand the extent to which managers are perpetrating a fraud—and successfully concealing it (e.g., from auditors, jurors, and regulators)—via methods that appear unintentional on the surface.

The third hypothesis addresses the issue that auditors with personality characters of idealism or moral idealism are more capable of detecting fraud than pessimistic auditors. Although regulators have identified ethical lapses as a key factor contributing to auditors' failure to detect their clients' fraudulent financial reporting (fraud), research using ethical theory to examine auditors' fraud detection remains limited. We provide evidence on the joint effect of ethical idealism and trait skepticism on auditors' fraud judgments. Ethical idealism reflects an individual's concern for the welfare of others, while trait skepticism reflects an individual's disposition to validate a proposition.

Forsyth and O'Boyle (2013) theorized that there was an association between ethical idealism and tolerance for deception. Drawing on that insight, we posit that ethical idealism and trait skepticism have a complementary effect on auditor fraud planning performance. This is rooted in the former determining an auditor's tolerance for allowing a client to get away with an ethically questionable act. At the same time, the latter is essential in determining how evidence is generally sought and evaluated. Our results indicate a significant positive association between trait skepticism and the number of effective audit procedures but only for auditors with high ethical idealism. The results highlight the importance of measuring and controlling for the effects of these characters when evaluating fraud detection performance. The paper also shows that an ethics theory can generate additional understanding and insights into a vital accounting phenomenon. The result of the third hypothesis is consistent with Verwey and Asare's (2022) research.

Our study is subject to inherent limitations that should be considered when evaluating these findings. While we find that managers choose to perpetrate fraud by omitting expenses as opposed to misrecording revenues, we are unable to determine whether this choice is driven more by the account involved (expense versus revenue) or the (in)action required (omitting versus misrecording a transaction). Future research is needed to separate these effects and better understand how managers perpetrate fraud to make the resulting misstatements appear less intentional.

Additionally, assume the auditors have already detected the misstatement. Therefore, our studies cannot determine whether a misstatement characterized by omission or commission is more likely to be detected in the first place. We find evidence that managers believe omissions are less likely to be detected, but additional research is needed to test whether this is, in fact, the case. If omissions are both (1) less likely to be detected and (2) less likely to be judged intentional if detected, the implications of the omission strategy may be more pronounced than our study suggests.

References

1. Anderson, C. J. (2003). The psychology of doing nothing: forms of decision avoidance result from reason and emotion. *Psychological Bulletin*, 129(1), pp. 139-167.
2. Baron, J. and Ritov, I. (2004). Omission bias, individual differences, and normality. *Organizational behavior and human decision processes*, 94(2), pp. 74-85. <https://doi.org/10.1016/j.obhdp.2004.03.003>
3. Baron, R. S., Baron, P. H. and Miller, N. (1973). The relation between distraction and persuasion. *Psychological Bulletin*, 80(4), pp. 310-323. <https://psycnet.apa.org/doi/10.1037/h0034950>
4. Beasley, M. S., J. V. Carcello, D. R. Hermanson, and T. L. Neal. (2010). Fraudulent financial reporting 1998 – 2007, an analysis of U.S. public companies. Association Sections, Divisions, Boards, Teams. Working paper. New York
5. Behzadian, F., Izadi Nia, N. (2018). Investigating the Factors Affecting the Audit Quality from the Viewpoints of Independent Auditors and Financial Managers of Companies listed on the Tehran Stock Exchange, *Journal of Accounting Advances*, 10(1), pp. 30-63. (In Persian). <https://doi.org/10.22099/JAA.2018.25885.1578>
6. Bowlin, K. (2011). Risk-based auditing, strategic prompts, and auditor sensitivity to the strategic risk of fraud. *The Accounting Review*, 86(4), 1231-1253.
7. Caramanis, C. and Lennox, C. (2008). Audit effort and earnings management. *Journal of accounting and economics*, 45(1), pp. 116-138. <https://doi.org/10.1016/j.jacceco.2007.05.002>
8. Carpenter, T. D. (2007). Audit team brainstorming, fraud risk identification, and fraud risk assessment: Implications of SAS No. 99. *The Accounting Review*, 82(5), pp. 1119-1140. <https://doi.org/10.2308/accr.2007.82.5.1119>

9. Cushman, F., Young, L. and Hauser, M. (2006). The role of conscious reasoning and intuition in moral judgment: Testing three principles of harm. *Psychological science*, 17(12), pp. 1082-1089. <https://doi.org/10.1111%2Fj.1467-9280.2006.01834.x>
10. Daryaei, A. and Kholousi Moshfegh, L. (2020). Impact of Self-Control Ego Depletion on Quality of Judgment and Decision-Making of Auditors (Test of Self-Control Ego Depletion Theory). *Journal of Health Accounting*, 8(2), pp. 20-38. (In Persian). <https://dx.doi.org/10.30476/jha.2020.68195.1227>
11. Dechow, P. M., Ge, W., Larson, C. R. and Sloan, R. G. (2011). Predicting material accounting misstatements. *Contemporary accounting research*, 28(1), pp. 17-82. <https://doi.org/10.1111/j.1911-3846.2010.01041.x>
12. Dechow, P. M., Hutton, A. P., Kim, J. H. and Sloan, R. G. (2012). Detecting earnings management: A new approach. *Journal of accounting research*, 50(2), pp. 275-334. <https://doi.org/10.1111/j.1475-679X.2012.00449.x>
13. DeScioli, P., Bruening, R. and Kurzban, R. (2011b). The omission effect in moral cognition: Toward a functional explanation. *Evolution and Human Behavior*, 32(3), pp. 204-215. <https://doi.org/10.1016/j.evolhumbehav.2011.01.003>
14. DeScioli, P., Christner, J. and Kurzban, R. (2011a). The omission strategy. *Psychological science*, 22(4), pp. 442-446. <https://doi.org/10.1177%2F0956797611400616>
15. Forsyth, D. R. and O'Boyle, E. H., Jr. (2013). *Ethics position theory and unethical work behavior*, Handbook of unethical work behavior: Implications for individual well-being, pp. 221–236. Armonk, NY
16. Freudenburg, W. R. and Alario, M. (2007). Weapons of mass distraction: Magicianship, misdirection, and the dark side of legitimation. *Sociological Forum*, 22(2), pp.146-173. <https://doi.org/10.1111/j.1573-7861.2007.00011.x>
17. Hamilton, E. L. and Smith, J. L. (2021). Error or fraud? The effect of omissions on management's fraud strategies and auditors' evaluations of identified misstatements. *The Accounting Review*, 96(1), pp. 225-249. <https://doi.org/10.2308/tar-2017-0355>
18. Hammersley, J. S. (2011). A review and model of auditor judgments in fraud-related planning tasks. *Auditing: A Journal of Practice & Theory*, 30(4), pp. 101-128. <https://doi.org/10.2308/ajpt-10145>
19. Hoffman, V. B. and Zimbelman, M. F. (2009). Do strategic reasoning and brainstorming help auditors change their standard audit procedures in response to fraud risk?. *The Accounting Review*, 84(3), pp. 811-837. <https://doi.org/10.2308/accr.2009.84.3.811>
20. Hoffman, V. B., & Zimbelman, M. F. (2012). How strategic reasoning and brainstorming can help auditors detect fraud. *Current Issues in Auditing*, 6(2), P25-P33.
21. Jamal, K., Johnson, P. E. and Berryman, R. G. (1995). Detecting framing effects in financial statements. *Contemporary Accounting Research*, 12(1), pp. 85-105. <https://doi.org/10.1111/j.1911-3846.1995.tb00482.x>
22. Khoshtinat, M., Bostanian, J. (2007). Professional Judgment in Auditing. *Empirical Studies in Financial Accounting*, 5(18), pp. 25-57. (In Persian)
23. Kordes-de Vaal, J. H. (1996). Intention and the omission bias: Omissions perceived as nondecisions. *Acta Psychologica*, 93(1-3), pp. 161-172.
24. Luippold, B. L., Kida, T., Piercey, M. D. and Smith, J. F. (2015). Managing audits to manage earnings: The impact of diversions on an auditor's detection of earnings management. *Accounting, Organizations and Society*, 41(4), pp. 39-54. <https://doi.org/10.1016/j.aos.2014.07.005>

25. Mashlah, S. A. M. E. R. (2015). The role of people's personal values in the workplace. *International Journal of Management and Applied Science*, 1(9), pp. 158-164.
26. Miller, W. R., Zweben, J. and Johnson, W. R. (2005). Evidence-based treatment: why, what, where, when, and how?. *Journal of substance abuse treatment*, 29(4), pp. 267-276. <https://doi.org/10.1016/j.jsat.2005.08.003>
27. Moradi, J., Rostami, R., and Zare, R. (2014). Recognizing Risk Factors Affecting Fraud Probability in Financial Reporting from Auditors' Viewpoint and Its Impact on Firms' Performance. *Journal of Accounting Advances*, 6(1), pp. 141-173 (In Persian). <https://dx.doi.org/10.22099/jaa.2014.2261>
28. Petty, R. E. and Cacioppo, J. T. (1986). The elaboration likelihood model of persuasion. In *Communication and persuasion*, pp. 1-24. Springer, New York, NY.
29. Pratoomsuwan, T. and Yolrabil, O. (2020). Fraud and Error Misstatements and Auditor Liability: The Moderating Role of the Evaluator's Auditing Knowledge. *DLSU Business & Economics Review*, 30(1), pp. 42-55.
30. Public Company Accounting Oversight Board (PCAOB). (2002a). Responsibilities and Functions of the Independent Auditor. PCAOB Interim Auditing Standard 1001. Washington DC: PCAOB.
31. Public Company Accounting Oversight Board (PCAOB). (2002b). Consideration of Fraud in a Financial Statement Audit. PCAOB Interim Auditing Standard 2401. Washington DC: PCAOB.
32. Public Company Accounting Oversight Board (PCAOB). (2010). Evaluating Audit Results. Auditing Standard 2810. Washington DC: PCAOB.
33. Rahmawati, H. S. and Indrijawati, A. (2020). Auditor Experience, Work Load, Personality Type, And Professional Auditor Skeptisism Against Auditors' Ability In Detecting Fraud. *Talent Development & Excellence*, 12(2), pp. 1878-1890.
34. Ritov, I. and Baron, J. (1999). Protected values and omission bias. *Organizational behavior and human decision processes*, 79(2), pp. 79-94. <https://doi.org/10.1006/obhd.1999.2839>
35. Rokeach, M. (1973). *The nature of human values*. New York: The Free Press. N.Y
36. Sandhu, N. (2022), Red flag behaviors in financial services frauds: a mixed-methods study, *Journal of Financial Regulation and Compliance*, 30(2), pp. 167-195. <https://doi.org/10.1108/JFRC-01-2021-0005>
37. Schwartz, S. (2006). A theory of cultural value orientations: Explication and applications. *Comparative sociology*, 5(2-3), pp. 137-182. <https://doi.org/10.1163/156913306778667357>
38. Schwartz, S. H. (1992). Universals in the content and structure of values: theoretical advances and empirical tests in 20 countries. *Advances in Experimental Social Psychology*, 25(2), pp.1-65. [https://doi.org/10.1016/S0065-2601\(08\)60281-6](https://doi.org/10.1016/S0065-2601(08)60281-6)
39. Schwartz, S. H. (1994). Are there universal aspects in the structure and contents of human values?. *Journal of social issues*, 50(4), pp. 19-45. <https://doi.org/10.1111/j.1540-4560.1994.tb01196.x>
40. Spranca, M., Minsk, E. and Baron, J. (1991). Omission and commission in judgment and choice. *Journal of experimental social psychology*, 27(1), pp. 76-105. [https://doi.org/10.1016/0022-1031\(91\)90011-T](https://doi.org/10.1016/0022-1031(91)90011-T)
41. Street, M. D., Douglas, S. C., Geiger, S. W. and Martinko, M. J. (2001). The impact of cognitive expenditure on the ethical decision-making process: The cognitive elaboration model. *Organizational Behavior and Human Decision Processes*, 86(2), pp. 256-277. <https://doi.org/10.1006/obhd.2001.2957>
42. Verwey, I. G. and Asare, S. K. (2022). The joint effect of ethical idealism and trait skepticism on auditors' fraud detection. *Journal of Business Ethics*, 176(2), pp. 381-395. <https://doi.org/10.1007/s10551-020-04718-8>

43. Widodo, N. H. and Chariri, A. (2021). The Relationship Between Audit Procedures, Auditors' Experience and Auditors' Responsibility for Fraud Detection. *Diponegoro Journal of Accounting*, 10(1), pp. 1-10
44. Wilks, T. J., & Zimbelman, M. F. (2004). Decomposition of fraud-risk assessments and auditors' sensitivity to fraud cues. *Contemporary Accounting Research*, 21(3), 719-745.
45. Zimbelman, M. F., & Waller, W. S. (1999). An experimental investigation of auditor-auditee interaction under ambiguity. *Journal of Accounting Research*, 37, 135-155.