



The Institutional Ceremony of Key Audit Matters: A Decoupling of Disclosure from Audit Outcomes in Pakistan's Non-Financial Sector

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Abstract

This research attempts to determine the extent to which the disclosure of “Key Audit Matters” (KAMs) affects the audit outcome, namely audit fee and audit delay, within the Pakistan institutional setting. The study employs Institutional Theory to test whether the mandatory adoption of KAMs, which acts as an “isomorphic pressure,” has led to significant changes in audit effort and timeliness rather than existing at a ceremonial level to preserve legitimacy. Utilizing data on non-financial listed entities with a data set of 199 non-financial entities on the Pakistan Stock Exchange over a period of six years, starting in 2018 and culminating in 2023, with a total observation of 1194 firm-years, this research applies fixed-effect panel regression analysis with clustered std. errors. Our empirical analysis reveals that there has been significant decoupling. That is, “KAM disclosures” reveal neither significant nor positive association with audit fee as well as the audit report lag, yet firm-level characteristics, size ROA, and leverage reveal significant positive association with the audit outcome measures. The findings highlight that in Pakistan’s emerging market, the adoption of KAMs may be pushed more by coercive and mimetic isomorphism to attain legitimacy rather than by a substantial enhancement in audit rigor. This endeavour contributes to the global auditing literature by underscoring the crucial role of local institutional contexts in influencing the real impact of the international auditing standards.

Keywords: Key Audit Matters, Audit Fees, Audit Report Lag, Institutional Theory, Pakistan

1. Introduction

With the introduction of expanded audit reporting, especially the requirement to communicate Key Audit Matters, the global auditing landscape has changed significantly. According to the International Auditing and Assurance Standards



Board, under ISA 701, KAMs are meant to "provide greater transparency about the audit that was performed" and provide "entity-specific information" to financial statement users (IAASB, 2015). This reform constitutes a paradigm shift from the standardized pass/fail model of audit reporting to a more communicative and informative audit report.

Proponents argue that KAM disclosures improve audit quality since auditors would have to rigorously examine and document high-risk areas and increase their accountability (Christensen et al., 2014). Theoretically, this additional scrutiny and communication burden should manifest in more concrete audit outcomes. In concrete terms, the identification and reporting of KAMs would require additional audit procedures, specialized expertise, and senior auditor involvement, all of which may increase audit costs (Gutierrez et al., 2018). In addition, the complexity in auditing such matters and additional review and reporting requirements may lengthen the audit process, hence leading to audit delay (Nguyen & Kend, 2021).

Nevertheless, the literature on the economic implications of KAMs is still inconclusive and has mostly come from developed economies. The studies have identified modest and positive correlations in developed economies on KAM disclosures and the costs of audits (Reid et al., 2019; Lennox et al., 2022). The global scientific community has identified contradictory evidence on the implications of KAMs through their research endeavours. The study conducted by Elmarzouky et al. (2023) indicates that the costs of audits have increased since the incorporation of KAMs into the audit report. The study conducted by Mulla and Bradbury (2022) indicates that KAMs have no relationship to the costs of audits. Furthermore, evidence also indicates that KAMs disclosure has led to an increase in the delay for audits (Nguyen & Kend, 2021). The auditor takes extra time to write the audit report accompanied by the KAMs disclosure paragraph. Conversely, very few studies have indicated that the disclosure of KAMs has reduced the delay for the audits (Baatwah et al., 2022). The study conducted by Abdullatif et al. (2023) indicates that KAMs have no relationship to the production time for the audit reports. Thus, the conflicting results in the literature highlight the need to explore these phenomena in new contextual settings. The institutional adjustment of the global standards for emerging



economies, such as the Pakistani context, has not received adequate attention. Emerging economies such as the Pakistani environment have unique characteristics that define the institutional adjustment for the global standards. As opposed to the developed markets, Pakistan is characterized by less strict enforcement mechanisms, lesser maturity of capital markets, highly concentrated ownerships and varying levels of professional skepticism in audits (Rashid et al., 2023). These attributes may fundamentally modify how international standards are administered and enforced.

This paper positions itself in the research gap by investigating the influence of KAMs on the outcomes of audits in Pakistan. Pakistan is an interesting research context. The implementation of ISA 701 became mandatory for listed entities since 2018, thus yielding a recent “clean” regulatory shock. Moreover, its institutional context, with formally strong regulation alongside varying levels of informal implementation, constitutes an interesting natural laboratory for testing the difference between substantive versus ceremonial implementation of international standards on formal regulation (Meyer & Rowan, 1977).

The Institutional Theory lens by DiMaggio & Powell (1983) is specifically well-suited for this analysis. Institutional Theory argues that organizations implement structures and practices not solely for efficiency gains but for legitimacy-seeking and survival within their institutional context. These practices and structures are implemented in the face of isomorphic forces: coercive (state or government regulation), mimetic (imitations of competitors or similar organizations), and normative (professional or industry associations). We would argue that the requirement for KAM disclosure is a strong force between coercive and normative isomorphism. One of the fundamental principles of Institutional Theory is that organizations exhibit a ‘decoupling’ effect that sees organizations make symbolic or formal changes for legitimacy-seeking purposes while isolating or decoupling the organizational core or actual work activity from the changes made (Meyer & Rowan, 1977). Applying this principle for auditing means that organizations follow procedure for KAM disclosure without any actual improvement in the auditing process. Accordingly, the question that emerges in the context of the Pakistani institutional framework is: *Are Key Audit Matters*



simply a ceremonial procedure for complying with regulations, or do they contribute significantly to increased audit effort in the form of increased audit fees and audit delay?

To this end, six years of data ranging from 2018 to 2023 was considered, relating to 199 non-financial firms listed in the PSX. We considered the number of KAMs, standard proxy for audit complexity and effort, as per Lennox et al. (2022), and their association with the natural logarithm of audit fees and audit report lag after the control of established determinants that included firm size, profitability, leverage, and auditor type.

Our findings make a more nuanced contribution. We find no statistically significant relationship between the number of KAMs disclosed and either audit fees or audit delay. This null result holds across several model specifications and robustness checks. What this suggests is a decoupling phenomenon whereby, although Pakistani audit firms have ceremonially adopted the structure of KAM reporting to attain legitimacy by complying with ISA 701, such an adoption has not percolated down into the technical core of the audit process as to systematically alter its cost or duration. The determinants of audit outcomes in Pakistan remain traditional factors like firm size and profitability.

The rest of the paper is organized as follows: Section 2 provides a review of the related literature and hypothesis development. Section 3 provides the theoretical framework, while Section 4 elaborates on the research methodology with respect to sample, variables, and models. Section 5 presents the empirical results and discussion. Section 6 presents robustness checks, while Section 7 concludes with implications, limitations, and future research avenues.

2. Literature Review and Hypothesis Development

2.1 Key Audit Matters: Concept and Global Evidence

The communication of KAMs is at the heart of the new audit reporting model. KAMs are described as “those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period” (IAASB, 2015). The reporting of KAMs aims to fill a certain information gap that exists between auditors and users. There is a considerable amount of literature that investigates their determinants and effects.

Studies examining determinants of KAMs have found that KAMs are



related to client business complexity, inherent risk, and poor performance. Firms that are highly leveraged, less profitable, larger in size, or facing going-concern problems are observed to have more KAMs disclosed (Pinto & Morais, 2019; Lennox et al. 2022). Turning to consequences, studies have examined market reactions, audit quality, and audit outcomes. While evidence about stock market relevance is revealing both informative properties and a lack of investor reaction (Bédard et al. 2019; Gutiérrez et al. 2018), more pertinent to this analysis are studies examining audit outcomes.

2.2 KAMs and Audit Costs

The audit fee model proposes that fees are a function of effort, risk, and auditor rent (Simunic, 1980). Disclosure about KAMs would have a hypothetical impact on each of these in turn. Firstly, if an issue is considered 'key,' there would be increased evidence-gathering, involvement at a higher level, and involvement of partners and quality review time, which would have a direct impact on effort (Reid et al., 2019). Secondly, through public disclosure of high-risk areas, there could be an increased risk of litigation and reputation associated, demanding a premium regarding risk (Lennox et al., 2022). Thirdly, there could be some increase in bargaining power associated with the private information imparted through disclosure of KAMs.

The evidence emerging from developed markets generally suggests a positive relationship. Reid et al. (2019) reported a significantly positive association between the number of KAMs and the costs of the audits in the UK. This is akin to what Lennox et al. (2022) reported for the US market regarding the disclosure of KAMs. This suggests that there is a cost Premium for this disclosure. Nevertheless, this effect size could indicate that the auditors are essentially absorbing the cost or that there might be efficiencies being derived. according to the study by Elmarzouky et al. (2023), the costs of the audits have increased since the inclusion of KAMs into the audit report.

On the other hand, Al-mulla and Bradbury (2022) conducted a pre-post research design study among New Zealand listed issuers and found that there was no statistically significant increment in audit fees due to the initial disclosure of KAMs. Nevertheless, a cross-sectional test showed that the positive and significant relationship exists between number of disclosed KAMs and higher



audit fees. More specifically, those KAMs that are firm-specific and industry-specific are also related to higher audit fees. The authors confirmed that it is likely that the costs associated with disclosing KAMs are minimal, since at this point, they have already taken into account those related to audit effort and risk assessments, when determining audit fee payments before actually being disclosed as KAMs. Another study conducted by Gutierrez et al. (2018) found that there was no significant increase in audit fees due to the inclusion of KAMs in the extended auditors' reports, among the premium firms. It also appeared that although the firms submitting the extended reports demonstrated higher fees, but there was no significant impact due to KAMs to audit fees. This confirmed the view that the incremental costs linked with KAM disclosures were nominal, due to the fact that much of the needed information was already supplied to the audit committees during the audit of financial statements.

2.3 KAMs and Audit Delay

"Audit delay" refers to the time lapse between the end of the firm's fiscal year and the date on which the audit report is issued. It is a very important determinant of audit process efficiency and the timeliness of financial information (Habib & Huang, 2019). KAMs may raise audit delay for several reasons. Additional procedures in high-risk areas may extend fieldwork. Additionally, documentation requirements for internal consultations and potentially disputative communications with management regarding the drafting of KAMs would enhance review and report stages in a rather lengthy manner (Sirois et al., 2020). Additionally, auditors may act more carefully.

Findings on this relationship are not as abundant but suggest a positive association. In the Canadian context, Sirois et al. (2020) demonstrated a positive association between the disclosure of KAMs, specifically estimates and valuation KAMs, and increased audit delay. A similar finding appeared in Habib and Huang (2019), which found a positive association in the Australian context and concluded KAMs increased complexity towards the end stages of audit. In a similar manner, Nguyen and Kend (2021) found KAMs disclosure increased delay in the audit. The auditor requires more time to prepare the audit report accompanied by KAMs disclosure.

On the other hand, however, a study carried out by Li and Luo (2023)



indicates that there is no significant difference in the audit delay experienced in the US for companies that disclose Critical Audit Matters (CAMs) compared to those that do not disclose the CAMs. Based on the finding, it is clear that the process entailed in the disclosure of the Critical Audit Matters, including the identification and communication of the matters, has not had an impact on the delay in the audit process. Very few studies suggest that the disclosure of KAMs has resulted in a reduction in the delay for the audit process (Baatwah et al., 2022). A study carried out by Abdullatif et al. (2023) shows that KAMs do not affect the production time for the audit report.

2.4 The Institutional Context of Pakistan

Studies on audit outcomes literature for Pakistan have emphasized on traditional variables, finding evidence for the influence of size, complexity, and risk variables (Butt and Hasan, 2009). Yet, this particular effect of the new audit reporting framework has remained untested. The state of Pakistan has been recognized to have a strong regulatory framework (e.g., SECP - Securities and Exchange Commission of Pakistan) but is also plagued by difficulties in enforcing regulations and a business environment where relationships are also likely to play a role (Javid and Iqbal, 2010). Moreover, Pakistan's audit industry is quite competitive with both Big4 and local firms vying for market share, thus likely imposing cost pressure (Sheikh and Siddiqui, 2020).

In this scenario, the implementation trend of a complex global standard such as ISA 701 might vary. There might be significant coercive pressure on auditors from the SECP to adhere to the requirement of disclosure. There might also be mimetic pressure on auditors to adopt the reporting format practiced by lead entities. But because of tough competition pressures and demands from clients to keep costs down, there might also be a resistance on the part of auditors not to fully pass on the costs entailed in additional procedures inherent in KAMs. There might also be a need to reduce process disruptions while identifying and listing KAMs. This tension between legitimacy-seeking compliance and economic pressures results in the conditions for decoupling.

2.5 Hypothesis Development

From Institutional Theory and our preceding discussion, we form our competing views.



In the substantive adoption, from an isomorphic perspective, coercive pressure from SECP and normative pressure from IAASB aim to include KAMs within the main audit process. This leads to our first hypotheses in the alternative form:

- **H1a:** The number of Key Audit Matters disclosed has a significant impact on audit fees.
- **H2a:** The number of Key Audit Matters disclosed has a significant impact on audit delay.

On the side of ceremonial adoption/decoupling, companies adopt the publicly observed format of KAM reporting and thereby attain legitimacy while decoupling technical work, while the process of audit, measured by application of resources and time, is mainly governed by traditional factors rather than the newly imposed disclosure obligation, hence reaching the null form of our hypotheses:

- **H1b:** There isn't a significant relationship between the number of Key Audit Matters disclosed and audit fees.
- **H2b:** There isn't a significant relationship between the number of Key Audit Matters disclosed and audit delay.

3. Theoretical Framework: Institutional Theory and Decoupling

This research is grounded in Institutional Theory (DiMaggio & Powell, 1983; Meyer & Rowan, 1977), which offers a profound paradigm to conceptualize the behavior of an organization under external pressures, like government regulations. Organizations, according to Institutional Theory, pursue legitimacy in addition to their efficiency, which essentially means that they aim to convey a sense of their activities being desirable, correct, and appropriate in a socially constructed system of norms and beliefs.

DiMaggio and Powell (1983) found that there were three isomorphic change mechanisms that cause the homogenization of all organizations:

1. **Coercive Isomorphism:** These arise as a result of formal and informal forces emanating from other organizations (such as the state or statutory bodies like the SECP). The imposition of ISA 701 by the SECP is a coercive force.
2. **Mimetic Isomorphism:** This is where the organization operates under conditions of uncertainty. The organization mimics its successful counterparts.



Leaders may follow the trend set by the early adopters or the audit firms in the case of Pakistan.

3. Normative Isomorphism: This owes largely to professionalization, which is the collective effort of professionals in a particular occupation attempting to determine the conditions and manner of how they will work. This is carried out through the IAASB via ISA 701 and the ICAP through the promotion of a proper and contemporary audit process.

These forces make the adoption of KAM reporting compulsory for the audit firms auditing listed companies in the Pakistani market. An important point emerging from the theory by Meyer and Rowan (1977) is that organizations tend to decouple their formal and informal structures. The organizations adopt the rules and procedures ritualistically with the intention of ensuring legitimacy and obtaining resources. The organizations shield the technical core from the rules for the purpose of ensuring effectiveness and control. Decoupling assists organizations in developing legitimacy in the opinion of outsiders.

In our case, decoupling would appear in the following forms:

- Memorandum/ Ceremonial Structure: The audit report also carries a ceremonial part related to KAMs, written according to a prescribed form and wordings, which complies with domestic (SECP) as well as international requirements (IAASB) standards.
- Buffered Technical Core: There is again no change to the actual audit process in regard to the planning, risk assessment, testing, number of hours, and time management. It is likely that a "key" issue identified could be the one being intensively audited, and this identification essentially turns into a "reporting exercise" rather than what drives audit activity. There may not be much emphasis or resources put in, just to have it reported as a "KAM."

This framework hypothesizes that if decoupling is so common, it will be possible to identify the formal institutionalization of KAM reporting (structure), but not its effect on the technical components of the auditing process (cost and time), thus testing H1b and H2b. Alternatively, if the pressures result in substantive integration, then KAMs will have a direct effect on the processes, which will result in H1a and H2a being supported.

4. Research Methodology



4.1 Sample Selection and Data

The initial population entails all the non-financial companies that are listed at the Pakistan Stock Exchange (PSX) from 2018 to 2023. Financial companies like banks and insurance companies are not included in the study because of the different framework that they operate in. The study starts from 2018 because ISA 701 was adopted in Pakistan during this year.

The data required for the KAMs was gathered manually from the published audit reports of sample companies, which could be accessed on the PSX website and the annual reports of the companies. The financial data was gathered from the financial statements.

4.2 Variable Measurement

Table 2: Variable Definitions and Measurements

Variable	Symbol	Measurement
Dependent Variables		
Audit Cost	AC	Natural logarithm of total audit fees (Elmarzouky et al., 2023).
Audit Delay	AD	Number of days between the fiscal year-end date and the audit report date (Abdullatif et al., 2023).
Independent Variable		
Key Audit Matters	KAMs	The number of KAMs disclosed in the auditor's report (Baatwah et al., 2022).
Control Variables		
Profitability	ROA	Net income divided by total assets (%).



Variable	Symbol	Measurement
Firm Size	SIZE	Natural logarithm of total assets.
Leverage	LEV	Total debt divided by total equity.
Auditor Type	Big4	Dummy variable equal to 1 if the auditor is a Big 4 firm (PwC, Deloitte, EY, KPMG), 0 otherwise.

4.3 Empirical Models

To test the hypotheses, panel data regression models were employed. The econometric models are specified as follows:

Model 1: Audit Cost (Primary Specification – Firm Fixed Effects)

$$AC_{it} = \beta_0 + \beta_1 KAMS_{it} + \beta_2 ROA_{it} + \beta_3 SIZE_{it} + \beta_4 LEV_{it} + \beta_5 Big4_{it} + \mu_i + \epsilon_{it}$$

Where:

- AC_{it} is the natural logarithm of audit fees for firm i in year t .
- $KAMS_{it}$ is the count of Key Audit Matters disclosed for firm i in year t .
- ROA_{it} , $SIZE_{it}$, LEV_{it} , and $Big4_{it}$ are control variables as defined in Table 1.
- μ_i represents firm fixed effects, capturing all time-invariant unobserved heterogeneity specific to firm i .
- ϵ_{it} is the idiosyncratic error term.
- The subscript $i=1,2,\dots,199$ denotes firms, and $t=1,2,\dots,6$ denotes years (2018-2023).

Model 2: Audit Delay (Primary Specification – Firm Fixed Effects)

$$AD_{it} = \beta_0 + \beta_1 KAMS_{it} + \beta_2 ROA_{it} + \beta_3 SIZE_{it} + \beta_4 LEV_{it} + \beta_5 Big4_{it} + \mu_i + \epsilon_{it}$$

Where AD_{it} is the audit report lag in days for firm i in year t . All other terms are as defined for Model 1.

Robustness Specification: Models with Year Fixed Effects



In order to investigate how our findings are affected by general shocks and tendencies over time, we extend both Model 1 and Model 2 and control for year fixed effects in both models:

$$AC_{it} = \beta_0 + \beta_1 KAM_{sit} + \beta_2 ROA_{it} + \beta_3 SIZE_{it} + \beta_4 LEV_{it} + \beta_5 Big4_{it} + \mu_i + \lambda_t + \epsilon_{it}$$

$AD_{it} =$

$$\beta_0 + \beta_1 KAM_{sit} + \beta_2 ROA_{it} + \beta_3 SIZE_{it} + \beta_4 LEV_{it} + \beta_5 Big4_{it} + \mu_i + \lambda_t + \epsilon_{it}$$

Where λ_t represents year fixed effects, capturing factors common to all firms in year t but varying across years. The base year is 2018 ($\lambda_1 = 0$).

Estimation Method

All models are estimated using the within estimator (fixed effects model), which controls for firm-specific effects μ_i by subtracting firm-specific means from all variables (within transformation). The within estimator is consistent if there is correlation between μ_i and the explanatory variables. To control for heteroscedasticity and autocorrelation of residual series across time within firms, we use robust-standard-error estimates, which are clustered at the firm-level (Liang and Zeger, 1986; Petersen, 2008). The choice of fixed over random effects models is based on the Hausman test.

5. Empirical Results and Discussion

5.1 Descriptive Statistics and Correlations

Table 2: Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
AC	1,194	6.049	0.629	2.391	7.477
AD	1,194	88.93	32.26	24	460
KAMs	1,194	2.178	1.204	0	9
ROA	1,194	5.459	11.655	-95.04	118.21



Variable	Obs	Mean	Std. Dev.	Min	Max
SIZE	1,194	7.546	1.391	2.913	12.103
LEV	1,194	0.785	0.144	0.213	1.649
Big4	1,194	0.365	0.482	0	1

From Table 2, it is evident that the mean value for the log of the audit fee is 6.05, and the mean audit delay is about 89 days. The mean number of KAMs is 2.18, while the standard deviation is 1.2, showing a certain degree of variation. About 36.5% of the variable values represent a Big 4 auditor.

Table 3: Pearson Correlation Matrix

	AC	AD	KAMs	ROA	SIZE	LEV	Big 4
AC	1.000						
AD	0.095*	1.000					
KAMs	0.040	0.106*	1.000				
ROA	0.059*	-0.173*	-0.019	1.000			
SIZE	0.219*	0.094*	0.172*	0.166*	1.000		
LEV	0.004	0.087*	0.079*	-0.186*	0.214*	1.000	
Big4	0.046	-0.025	-0.018	0.202*	0.374*	0.057*	1.000

- $p < 0.05$



In Table 3, the correlation matrix is presented. The KAMs have a marginal but significant positive association with Audit Delay (0.106, $p < 0.001$) but not with Audit Cost. The size of the firms (SIZE) is positively affiliated with both AC and KAMs. The VIF for all variables is less than 1.28, determining the absence of harmful multicollinearity.

5.2 Main Regression Results

Our primary specification makes use of firm fixed effects. It controls for unobserved, time-invariant firm heterogeneity. Our first specification test is the F-test of joint significance of the firm effects, which has rejected the pooled OLS model in favor of the fixed effects models. The test is significant ($F(198, 990) = 56.04$, $p = .000$, AC model). The robust standard errors clustered by firm account for heteroskedasticity and within firm serial correlation.

Table 4: Main Regression Results – Fixed Effects Models with Clustered Standard Errors

Variable	Model 1: Audit Cost (AC)			Model 2: Audit Delay (AD)		
	Coeff. S.E.)	(Robust S.E.)	p- value	Coeff. S.E.)	(Robust S.E.)	p- value
KAMs	-0.0020 (0.0104)		0.845	-0.0506 (0.7198)		0.944
ROA	-0.0005 (0.0009)		0.552	-0.2732 (0.1509)		0.072
SIZE	0.1188 (0.0825)		0.151	3.1649 (3.9317)		0.422
LEV	0.1191 (0.0841)		0.158	16.2187 (15.9115)		0.309
Big4	-0.1120 (0.0481)		0.021	-0.6306 (2.0905)		0.763
Constant	5.1075 (0.6329)		0.000	54.1452 (25.7946)		0.037

Note: Robust standard errors clustered by firm in parentheses.

Test of H1 (KAMs and Audit Cost):

For KAMs in Model 1, the coefficient is -0.0020, and it is not significant ($p = 0.845$). This offers highly significant evidence in support of H1b. There is no



observable effect of disclosed KAMs on the amount of fees paid concerning the audit. This is a crucial observation. This allows the conclusion that in Pakistan, KAM disclosure is not linked either to an increased amount of billed auditing effort or an assumed risk cost by auditors.

Test of H2 (KAMs and Audit Delay):

Likewise, the coefficient for KAMs in Model 2 is -0.0506, and it is not statistically different from zero (p-value= 0.944). This is strong evidence supporting H2b. There is no systematic extension of the audit report timing by the disclosure of KAMs.

Analysis of Control Variables:

For Audit Delay, the coefficient for ROA is negative and marginally significant (p = 0.072), implying that the more profitable the company, the less the audit delay. The coefficient for Big4 in the Audit Cost equation is negative and significant (p = 0.021), implying that within firms over time, being audited by a Big 4 auditor is associated with a reduced audit cost. This is counter-intuitive and might indicate the kind of price competition and efficiencies that large auditing firms might have engaged in the Pakistani market.

5.3 Robustness Check: Inclusion of Year Fixed Effects

For examining how sensitive our estimates are to typical trends over time, we estimated models that controlled for year fixed effects. The results are summarized in Table 5.

Table 5: Robustness Check – Models with Year Fixed Effects

Variable	AC (With Year FE)			AD (With Year FE)		
	Coeff. (Robust S.E.)	(Robust)	p-value	Coeff. (Robust S.E.)	(Robust)	p-value
KAMs	0.0135 (0.0088)		0.127	0.0162 (0.6483)		0.980
ROA	-0.0001 (0.0008)		0.940	-0.2814 (0.1517)		0.065
SIZE	0.0190 (0.0414)		0.646	4.5297 (3.9580)		0.254
LEV	0.1108 (0.0757)		0.145	16.7231 (15.2568)		0.274



	AC (With Year FE)		AD (With Year FE)	
Big4	-0.0518 (0.0610)	0.397	-1.4093 (2.4980)	0.573

*Note: Robust standard errors clustered by firm in parentheses. *

The addition of year fixed effects shows that there is a clear, highly significant positive trend of audit fee over the years 2018-2023. Nevertheless, the main result on KAMs remains unaffected and stable: The coefficient on KAMs in the audit fee equation, although slightly positive, is still statistically insignificant (p-value = 0.127). In the audit delay equation, the coefficient on KAMs is effectively zero and insignificant (p-value = 0.980). The Big 4 variable becoming insignificant in the audit fee equation after including year effects indicates that the observed difference in audit fee could well be associated with other time-related variables. The robustness of our main result on KAMs in both specifications adds considerable strength to our main result.

5.4 Discussion in Light of Institutional Theory

The consistent null results obtained for KAMs under both sets of specifications provide strong evidence in favor of the decoupling framework (Meyer & Rowan, 1977). Pakistani auditing firms are seen to have reacted to the ISA 701 isomorphic pressures by merely adopting the visible part of ISA 701, that is, the KAM part that has been disclosed in the audit report. This gives them legitimacy toward the SECP (coercive isomorphism), the global profession (normative isomorphism), and other firms (mimetic isomorphism).

However, this implementation has been decoupled from the technical core of the audit production function. The drivers of the cost of audit and delay are still grounded in the traditional, specific-economic elements of the clients' companies (such as profitability and, as revealed by the robustness test, the larger temporal dynamics) rather than the novel communicative aspect of the audit. These results are consistent with the literature by Mulla & Bradbury (2022), who found no relationship between KAMs and the cost of the audit. As for the delay of the audit, the results were consistent with Abdullatif et al. (2023), who found that KAMs do not affect the time taken by the accounting firms to deliver the audit reports. The very significant year effects for the cost of the audit, signifying the constant increment from 2018 to 2023, further clarify that market-



level dynamics are much more influential in shaping the outcomes of the audit rather than the specific KAM disclosures by the companies. This result implies that in the emerging markets with competitive markets for the audit, the real effects of the global audit reform may not have any bite. The reform is successful in terms of the change in the visible aspect of the audit (the report), rather than its underlying reality or content (the effort/process), or, at any rate, the content as it is represented by the economic outcomes observable from the outside.

5.5 Discussion of Robustness

Our core finding of a statistically insignificant coefficient on KAMs holds in each of our three models—a baseline FE model, a more conservative FE model that was clustered, and one that controlled for fixed effects of each year—provides strong proof of its robustness. Our test confirms that our choice of estimator (firm FE) and our test of our hypothesis (use of clustered standard errors) are correct. This supplementary test, while changing some of our secondary findings, does not affect our primary test of our hypothesis.

6. Conclusion

The current study examined the effect of Key Audit Matter disclosures on the cost and delay associated with the audit in the non-financial sector in Pakistan, spanning the period between 2018 to 2023. The research is based on the underpinnings of the Institutional Theory, where the uptake of the KAMs can either constitute substantive incorporation within the auditing ritual or constitute a mere legitimacy-seeking ritual.

The results are clear and consistent, i.e., the number of KAMs published has neither a statistically significant influence on audit fees nor on the lag of the audit reports. This null result holds in our focal fixed effects specification and is also confirmed when accounting for common time trends by including year fixed effects. The focal factors for audit outcomes in our sample continue to be the same, i.e., profitability (in the case of lag) and strong economy-wide trends (in the case of fees). A noteworthy ancillary finding is that audit fees have been showing a sharp positive trend over the period studied, which dominates firm-specific factors when accounted for.

7. Theoretical and Practical Implications

7.1 Theoretical Contribution



This research contributes largely to the decoupling thesis because the application and validation of the institutional theory context for a global audit reform in an emerging country indicate the power and effectiveness of the isomorphic pressures in bringing about the ceremonial institutionalization of the formal structures (KAM reporting) without necessarily altering the technical system and its economic outcomes. It aims to emphasize the distinctness in the adaptation and impact of international standards on dissimilar institutional contexts.

7.2 Practical Implications:

1. For Regulators (e.g., SECP, IAASB): The results imply that it may not be adequate merely to require the format for the report because it does not seem sufficient as a means of improving the substance of the audit itself. Regulators may have to enforce a different approach or reemphasize the normative expectation related to the substantive focus of the KAMs.
2. For Audit Firms and Professionals: The overall evidence suggests that the competitive setting is one where the extra procedural costs imposed by KAMs are not being capitalized into higher fees. This might force the level of auditing quality downward. The profession in Pakistan might need to strengthen the normative link between KAM disclosure and the audit effort.
3. For Investors and Financial Statement Users: KAMs for users in Pakistan should be interpreted with a local institutional perspective taken into account. They may not signal well where excessive audit effort was concentrated, possibly just a compliance solution, whereas a very prominent time trend of audit fees does carry some market importance.

7.3 Limitations and Future Research

The research has several limitations that can be considered areas for future research:

1. Measurement of KAMs: A count measure was used. Text analysis could be undertaken in future work to investigate the impact of complexity, tone, or specificity of KAM description.
2. Audit Quality: The paper focused on outcomes (cost and delay) but not on audit quality outcomes. Further research could be undertaken to investigate the association among KAM attributes and earnings quality or restatements within a Pakistani setting.



3. Causal Identification: Although tight fixed effects can remove the effect of time-invariant controls, the concern about the possibility of uncontrolled variables changing over time is still there. Future research may use more strict causality identification techniques, such as difference-in-differences or instrumental variable estimation based on a regulatory setting.

4. Qualitative Insights: "The how and the 'why' of decoupling might provide valuable qualitative insight by interviewing audit partners and regulators in Pakistan.

In summary, the experience with ISA 701 in Pakistan shows that the process of the global audit standard is not smooth. It filters through the local institutions given that the pursuit for legitimacy may result in a ritual of compliance that appears in the disclosed KAMs but whose echo within the economics of the audit process is silent. This endeavor underscores the significance of considering institutional context when evaluating the international convergence of auditing practices.

8. References

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