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**THE PROFESSIONAL SCEPTICISM IN THE AUDIT
PROFESSION IN THE REPUBLIC OF MACEDONIA –
STUDENTS VERSUS EXTERNAL AUDITORS**

Abstract

In terms of global financial crises and financial scandals of big corporations worldwide, the public awareness of the responsibility of audits in detecting and preventing fraud is increasing. The interest focuses on the important role of professional scepticism and its proper application when auditing financial statements. Occurring concerns over insufficient and inadequate application of professional scepticism in audits led to development of many debates about the role of professional scepticism and suggestions on how to improve its application in the audit practice. Despite the importance of professional scepticism, in audit literature there is no consensus and empirical data for measuring the scepticism and how it affects the behavior of auditors. This paper makes an effort to define, conceptualize and measure professional scepticism. It also identifies threats to the concept and potential opportunities, i.e., measures and activities to promote the application of professional scepticism throughout the audit of financial statements, in order to improve audit quality. In order to answer the question whether the possession of a certain individual level of scepticism among auditors affects their behavior towards fraud indicators during audit engagements,

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an experimental research, in which students and external auditors in the Republic of Macedonia were taken as target groups, is conducted.

Key words: Trust, Doubt, Professional Scepticism, Fraud, Professional Judgement.

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Introduction

In terms of global financial crisis and identification of financial scandals at big international corporations (Enron, WorldCom, etc.), the awareness of the public for responsibilities of the audit for identification and prevention of frauds, has been increasing and the interest has been directed towards the significant role of the professional scepticism when auditing financial statements and its appropriate application.

In the latest public statements, the regulators, oversight bodies, developers and implementers of audit policies, as well as other stakeholders operating in the audit area for the benefit of the public interest, invite the auditors to demonstrate higher level of professional scepticism when conducting their audit engagements. At the same time, they invite them to challenge the assumptions and opinions or decisions taken by the management of the auditees when forming independent views, as well as to take actions for further improvement of the culture of the audit firms and its environment, that will encourage manifestation of higher level of professional scepticism.

Practicing the professional scepticism helps in increasing of the effectiveness of the audit engagements and in decreasing the opportunity of the auditor to choose inappropriate audit procedure, to misuse the audit procedure or the misinterpretate the audit results from the audit. Hence, the audit standards require the professional scepticism to be applied in the course of the whole audit engagement by every individual auditor from the team performing the audit engagement.

1. DEFINING AND TREATMENT OF THE PROFESSIONAL SCEPTICISM IN THE PROFESSIONAL REGULATION OF THE AUDIT PROFESSION

The term “professional scepticism” is widely used but may mean different things to different organizations and individuals. The word scepticism is formed from the root “sceptic,” which comes from the Greek word “sceptikos,” meaning “inquiring or reflective.” To inquire is “to seek information by questioning; to ask.” The characteristics commonly associated with being a sceptic include questioning and careful observation, probing reflection, looking beyond the obvious, and suspension of belief. Professional scepticism incorporates the attributes commonly associated with being a sceptic in a professional setting that requires a standard of care and due diligence in the context of professional standards, regulation, oversight, litigation, negotiation, evidence collection and evaluation, professional judgment, complex business transactions, varying incentives and motives, rationalization, and so forth. (Steven M. Glover, Douglas F. Prawitt 2013).

When considering the definition of the professional scepticism on the audit standards and the academic literature, we find related but still different definitions. According to the International Standards on Auditing (ISA), “Professional Scepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence, and requires ongoing inquiry whether or not the obtained audit information and evidences purport that there are critical observations arising from fraud.” In other terms, it means that the auditor should undertake a professional assessment, with a sceptical mind, of efficiency and suitability of the evidences obtained throughout the term of the audit task. Indeed, the concept of the “Professional Scepticism” enhances the concept of the “Professional Due Diligence” set forth in the International Standards on Auditing (ISA). The International Standards on Auditing emphasize questioning mind and a critical assessment of audit evidence. However, the terms such as “questioning mind” and “critical assessment of audit evidence” are ambiguous to a certain level and leave a room for interpretation about what represents adequate level of questioning or critical assessment, and how such behavior is demonstrated and documented in an environment characterized by different risks on assertion level.

The audit literature describes different perspectives related to the concept of professional scepticism. The early audit standards suggest “neutral approach” towards the scepticism, whereas the new ones promote the approach of “presumptive doubt”. From neutral perspective, the auditor “does not assume any bias, ex ante” (Nelson 2009, p.3) and it can be considered that any evidence will be equally assessed (Hogarth & Einhorn 1992; Bamber, Ramsay & Tubbs 1997). Vice versa, the perspective of presumptive doubt assumes some certain level of dishonesty by the client management, until sufficient evidence is collected that will lead to the opposite (Nelson 2009).

The existence of different approaches and perspectives in defining the professional scepticism results in different practices.

The lack of clear direction and guidelines for practical implementation regarding which behaviors and actions represent appropriate professional scepticism in different scenarios for different assertions, leads to different views, practices and opinions. In such an environment, it is comprehensive for the observers, professionals and regulators not to agree amongst themselves. Each of the different perspectives or ways of thinking relate to the professional scepticism has implications to the audit effectiveness and potentially to the efficiency. The problem with any of the perspectives is that each of them is incomplete in the practical audit environment and none of them, under any conditions, is not necessarily optimal.

2. CONCEPTUALIZATION AND MEASUREMENT OF THE PROFESSIONAL SCEPTICISM

Within the researches related to the professional scepticism, there is a lack of clear understanding for what constitutes professional scepticism as a concept. Precisely because of that, there are difficulties in conducting various researches in the academic literature or in drawing conclusions about them. Several authors in their researches have taken a central part in the academic literatures in the context of conceptualization of the professional scepticism, especially in defining the factors that might influence it.

Shaub (1996) and Shaub & Lawrence (1996) tried to adapt a model from the arguing conflict literature into the audit context. The model to a certain extent is based on an unrealistic assumption that the professional

scepticism is equal to the doubt as a term, and the trust is simply a lack of doubt. The basis of the model is that the individual's actions regarding the trust and doubt arise from the subjective assessment of the confidentiality of the others. The subjective trust or doubt is a result of the individual's perception for the motives and/or competencies of the others. These perceptions may vary based in previous experience, situational factors or as a result of dispositional factors that characterize the individual that has confidence (Kee&Knox 1970).

Hurttt, in cooperation with Eining&Plumlee (2001), presents theoretical model of the professional scepticism that is based on the psychological and philosophy literature for methodological scepticism. Their model suggests that the professional scepticism is multidimensional creation consisted of 6 (six) individual characteristics: curiosity, self-confidence, interpersonal understanding, questioning, self-determining and deliberating. The six characteristics of the sceptic lead to four specific audit behaviors: 1) expanded information search, 2) increased contradiction detection, 3) increased alternative generation and 4) increased scrutiny of interpersonal information.

Nelson (2009) gives an overview of simple model of professional scepticism that integrates the existing literature related to the professional scepticism and that illustrates the way the audit knowledge, characteristics and stimulations combine with the audit evidence for the purpose of providing professional judgment and fulfill actions that reflect the professional scepticism. In the model, 3 (three) factors are combined with the audit evidence for the purpose of influencing the professional judgments and auditors' activities: knowledge, characteristics and stimulations.

Considering the various characteristics of the scepticism, it is enabled to identify many factors that influence positively and that encourage the sceptical judgments and decisions:

1) Interpersonal trust

The audit researches mainly consider the audit sceptic nature as antithesis of trust (Cushing 2000; Choo & Tan 2000; Payne & Ramsay 2005, p.324; Shaub 1996; Shaub&Lawrence 1996; Shaub& Lawrence 1999). However, certain researches treat and describe the trust as one of the many aspects of the audit sceptical nature (Hurttt 1999; Hurttt *et al.*

2003a; 2008; Rose 2007). The main idea is that when an auditor has a lower level of interpersonal trust it is assumed to be more sceptical.

2) *Delay of judgment until receiving strong evidence and a need for closing certain issue*

The delay in is noted by several authors as one of the main characteristics of the sceptics (Bunge 1991; Kurtz 1992; Hurtt *et al.*2003a). The delay in judgment is assumed to be opposite to the need for cognitive closure of certain issue. Kurtz emphasizes that “the delay in judgement... is necessary component of the sceptic research” (1992, p.41). According to Bunge (1991, p.131), “the sceptics do not accept naively the first they see or think, they are not gullible. Neither are they xenophobic. They are simply critical, they want to see evidence before they start believing”. The sceptics especially delay judgment for what had not been checked before (Bunge 1991, p.132). The sceptics proceed with collection of evidence until there is no reasonable person to doubt the given statement (Kurtz 1992, p. 132).

3) *Locus control or position control*

The external locus of the control is based on the belief that the results cannot be influenced by the efforts made by certain person, whereas the internal locus of the control presents the belief that the results depend on the individual actions (Lefcourt 1991, p.414). The persons that have greater external locus of control are call “external”, whereas those having greater internal locus of control are called “internal”. The researches show that the external persons may be easier to convince and have greater tendency to confirm and accept the information, unlike the internal persons.

4) *Comprehensive scale for measuring the professional skepticism*

The need for developing specific scale for measurement of the professional scepticism is highlighted by several authors (for example, Choo & Tan 2000; Hurtt 2001, 2003, 2007). Hurtt (2001) develops instrument separating three sets of characteristics of the scepticism from the philosophy literature, audit standards and the existing literature for the scepticism in the audit: (1) examination of evidence; (2)

understanding of the sources of evidence; and (3) undertaking actions based on the evidence. These three sets of characteristics, altogether, determine the total level of professional scepticism. There is certain empirical evidence that the results achieved according to this scale are related to the sceptical behavior (Hurt *et al.* 2008; Popova 2006; Fullerton & Durtschi 2004).

2.1. Methodology and Results from the Conducted Research

Within the frames of this paper a research was made aiming at quantifying the professional scepticism as a characteristic of two target groups, students of the subject Internal audit at Faculty of Economics, University “Ss Cyril and Methodius” in Skopje and external auditors in public and private sector, and correlating the quantified characteristic to the behavior of the certain group in situations that indicate fraud in the course of an audit engagement.

The research was conceptualized in two parts. The first part is related to the level of professional scepticism that each respondents individually has in itself. The second part is providing an answer to the question whether the respondents, that presented higher level of professional scepticism, demonstrate as well a bigger will to collect more information when coming across fraud symptoms in comparison to those respondents with lower level of professional scepticism.

In the first part of the research we used a questionnaire composed according to the professional scepticism scale of Hurtt (2003), that is consisted of 30 (thirty) questions. The answers to the questions showed the way the respondent feels in general. It could be selected from “1” – I completely disagree with the statement to “6” – I completely agree with the statement from the questionnaire.

In the second part of the research we used the fraud indicators scale developed by Fullerton & Durtschi (2004). The scale is consisted of 38 (thirty eight) questions. All the questions were broken down in 9 (nine) groups, i.e. categories of fraud indicators: corporate cultures with high level of fraud, questionable relations with external parties, financial pressure, opportunities for fraud, personal symptoms, personal rationalizations, demographic indicators, indicators for accounting practice and the indicators for financial statements. The answers to the questions should have shown the level (“1” – Not at all... “6” – Yes, too much) to which the respondent would like to broaden the extent of its

research of information, if situations indicating fraud have been noticed in the course of an audit engagement.

The questions were translated from English to Macedonian and the answers were provided in Macedonian language.

Demographic questions were not used in the research.

The research approach was descriptive. One-way analysis of the variance (ANOVA) was used as a statistical model when analyzing the data, applying IBM SPSS Statistics, version 21. With ANOVA we analysed the collected data for the purpose of comparing the replies of the target group related to the level of professional scepticism with the replies regarding the red flags for fraud detection.

With Cronbach alpha we tested the internal reliability of the research.

Population of the first target group was consisted of students of the subject Internal audit at their fourth year of study on the Accounting and Auditing programme at the Faculty of Economics – Skopje, University Ss. Cyril and Methodius. The questionnaires were submitted to 147 (one hundred and seven) students, in hard copy. The total number of valid respondents whose answers were analysed, was 106 (one hundred and six).

Population of the second target group was consisted of external auditors, including state auditors from State Audit Office in Republic of Macedonia, as well as the auditors of the Instrument for Pre-Accession Assistance (IPA) from the Audit Authority for Audit of IPA in Republic of Macedonia. The questionnaires were submitted online on their e-mail addresses, using the webpage Surveyplanet (www.surveyplanet.com). The questionnaires were answered by 62 (sixty two) respondents.

Responding to the questions for the both groups was anonymous, and all the collected informations were used for this research.

Cronbach alpha for the both instruments was calculated using IBM SPSS Statistics, version 2.1. For the students as respondents, the total alpha coefficient for the Hurtt (2003) instrument amounts 0.862, whereas for the instrument Fullerton & Durtschi (2004), 0.938. With regards to the external auditors as respondents the total alpha coefficient for the Hurtt (2003) instrument is 0.795, and 0.923 for the Fullerton & Durtschi (2004) instrument.

Based on the arithmetic mean of the individual responses regarding the first part of the questionnaire, the respondents were divided as high sceptical and low sceptical.

For students, the break down was made based on the mean of 4.4047 for all responses on the scale for measurement of the level of professional scepticism of Hurtt (2003). The number of high sceptical respondents is 57 (fifty seven), whereas low sceptical are 49 (forty nine) respondents.

For the external auditors, the break down was made based on the mean of 4.8441 for all responses on the scale for measurement of the level of professional scepticism of Hurtt (2003).The number of high sceptical respondents is 35 (thirty five), whereas low sceptical are 27 (twenty seven) respondents.

Additionally, T-test was conducted on random sample for the purpose of identifying whether there is a significant difference between the means of the responses according to Hurtt's scale of the both groups of respondents. The result showed significant difference between the mean of responses for the students (M=4.40, SD=0.61) and the mean of responses for the auditors (M=4.84, SD=0.41); $t(163.42) = -5.58$, $p = 0.001$. In Table 1 and Table 2 it can be seen that the students have lower mean of the responses according to the Hurtt's scale in comparison to the external auditors.

Table 1. Group statistics of the mean of responses of the Hurtt's scale

	Group	N	Mean	Std. Deviation	Std. Error Mean
Average	Students	106	4.4047	.61347	.05959
Hurtt'sscale	Auditors	62	4.8441	.40591	.05155

Table 2. Test on independent samples

	Levene's Test for Equality of Variances		t-test for Equality of Means						
	F	Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
								Lower	Upper
Average	5.333	.022	-5.029	166	.000	-.43937	.08737	-.61186	-.26687
Hurtt'ssca			-5.576	163.417	.000	-.43937	.07879	-.59495	-.28379
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The second part of the research was supposed to confirm or reject the zero hypothesis H0: “There is no difference in the level of gathering additional information if there are noted situations that indicate fraud in the course of conducting audit engagements regarding the level of expressed professional scepticism”, i.e. to confirm or reject the alternative hypothesis H1: “There is higher level of gathering additional information if there are noted situations that indicate fraud in the course of conducting audit engagements for the external auditors that are characterized with a higher level of professional scepticism in comparison to the external auditors that are characterized with a lower level of professional scepticism”.

The independent variable in the research was the breakdown of the respondents on high and low sceptical. The dependent variables were the arithmetic means of the individual responses of the respondents for each of the nine groups, i.e. categories of fraud indicators.

Before conducting ANOVA, we tested the basic assumptions relate to the population, subject to ANOVA.

Group of students

For the students as respondents, the analysis showed significant difference for two categories of fraud indicators, i.e. ($p < 0.05$), and the alternative hypothesis was accepted. For the fifth category of fraud indicators (personal symptoms) $F(1,104) = 7.223$, $p = 0.008$ and for the sixth category (personal rationalizations) $F(1,104) = 6.428$, $p = 0.013$.

For the remaining seven categories of fraud indicators, the analysis was not significant, i.e. ($p > 0.05$). For the first category $F(1,104) = 0.054$, $p = 0.817$, for the second category $F(1, 104) = 0.347$, $p = 0.557$, for the third category $F(1,104) = 0.303$, $p = 0.583$, for the fourth category $F(1,104) = 0.039$, $p = 0.843$, for the seventh category $F(1,104) = 0.589$, $p = 0.445$, for the eighth category $F(1,104) = 0.307$, $p = 0.581$ and for the ninth category $F(1,104) = 0.414$, $p = 0.522$.

Table 3. ANOVA – Students

		Sum of Squares	df	Mean Square	F	Sig.
Category1	Between Groups	.067	1	.067	.054	.817
	Within Groups	129.492	104	1.245		
	Total	129.559	105			
Category2	Between Groups	.470	1	.470	.347	.557
	Within Groups	140.764	104	1.353		
	Total	141.234	105			
Category3	Between Groups	.228	1	.228	.303	.583
	Within Groups	78.333	104	.753		
	Total	78.562	105			
Category4	Between Groups	.064	1	.064	.039	.843
	Within Groups	167.760	104	1.613		
	Total	167.824	105			
Category5*	Between Groups	1639.509	1	1639.509	7.223	.008
	Within Groups	23606.344	104	226.984		
	Total	25245.853	105			
Category6*	Between Groups	1363.747	1	1363.747	6.428	.013
	Within Groups	22065.504	104	212.168		
	Total	23429.251	105			
Category7	Between Groups	.792	1	.792	.589	.445
	Within Groups	139.968	104	1.346		
	Total	140.760	105			
Category8*	Between Groups	75.912	1	75.912	.307	.581
	Within Groups	25689.266	104	247.012		
	Total	25765.177	105			
Category9*	Between Groups	98.223	1	98.223	.414	.522
	Within Groups	24695.232	104	237.454		
	Total	24793.455	105			

* The data for these categories of fraud indicators are calculated with non-parametric test Levene

There is no significant difference between the means of the responses for the high and low sceptical respondents. The respondents that are categorized as high sceptical gave insignificantly higher assessments to the questions related to fraud indicators for three categories of indicators, first, eighth and ninth categories, whereas regarding the remaining four categories, insignificantly higher assessments were given by the respondents categorized as low sceptical.

Group of external auditors

For the external auditors as respondents, the analysis was not significant for all of the nine categories of fraud indicators, i.e. (p>

0.05). For the first category $F(1,60) = 0.098$, $p = 0.755$, for the second category $F(1,60) = 0.062$, $p = 0.805$, for the third category $F(1,60) = 0.121$, $p = 0.729$, for the fourth category $F(1,60) = 0.060$, $p = 0.808$, for the fifth category $F(1,60) = 1.021$, $p = 0.316$, for the sixth category $F(1,60) = 0.012$, $p = 0.915$, for the seventh category $F(1,60) = 0.000$, $p = 0.999$, for the eighth category $F(1,60) = 0.262$, $p = 0.610$ and for the ninth category $F(1,60) = 0.153$, $p = 0.697$.

Table 4. ANOVA – External auditors

		Sum of Squares	df	Mean Square	F	Sig.
Category1*	Between Groups	8.069	1	8.069	.098	.755
	Within Groups	4926.029	60	82.100		
	Total	4934.098	61			
Category 2*	Between Groups	4.773	1	4.773	.062	.805
	Within Groups	4650.621	60	77.510		
	Total	4655.394	61			
Category 3	Between Groups	.076	1	.076	.121	.729
	Within Groups	37.821	60	.630		
	Total	37.897	61			
Category 4*	Between Groups	5.047	1	5.047	.060	.808
	Within Groups	5058.967	60	84.316		
	Total	5064.014	61			
Category5	Between Groups	1.326	1	1.326	1.021	.316
	Within Groups	77.953	60	1.299		
	Total	79.279	61			
Category6	Between Groups	.017	1	.017	.012	.915
	Within Groups	86.003	60	1.433		
	Total	86.020	61			
Category7	Between Groups	.000	1	.000	.000	.999
	Within Groups	103.242	60	1.721		
	Total	103.242	61			
Category 8*	Between Groups	22.246	1	22.246	.262	.610
	Within Groups	5088.225	60	84.804		
	Total	5110.471	61			
Category9*	Between Groups	11.935	1	11.935	.153	.697
	Within Groups	4680.550	60	78.009		
	Total	4692.485	61			

* The data for these categories of fraud indicators are calculated with non-parametric test Levene

When reviewing the mean of the answers for all nine categories of fraud indicators, it was noted that, although there is no significant difference, the respondents that are categorized as high sceptical have given higher assessments to the questions related to fraud indicators for all categories of indicators, except for the sixth group of indicators that is

related to the personal rationalizations. For this group of fraud indicators, the low sceptical respondents have given insignificantly higher assessment. For the seventh group of indicators, that is related to the demographic indicators, the assessments were approximately the same, but however, in favor of high sceptical respondents.

Conclusion

The results of the research efforts to assess more directly the professional scepticism and to link those assessments to the audit behaviours, are somewhat inconsistent. The audit research, regardless of its form, that is trying to measure the depth and width of the professional scepticism, is complicated not only due to its hybrid structure of the professional scepticism but due its multilayer structure, as well. The professional scepticism as a concept is more complex and wider concept than it is assumed to be. Hence, it can be said that the research in the field of the professional scepticism has just begun.

Although the need for practicing of the professional scepticism through mandatory obligation for applying the audit standards has been concrete and defined, in the Republic of Macedonia may be noted a lack of academic literature dealing with it in the country.

A research was conducted on two groups of respondents. Out of total 106 (one hundred and six) students on the subject Internal audit, 57 (fifty seven) respondents were assessed as highly sceptical, whereas as low sceptical are assessed 49 (forty nine) respondents. Out of total 62 (sixty two) respondents, external auditors in the country, 35 (thirty five) were qualified as high, and 27 (twenty seven) respondents as low sceptical. Students have given significantly lower assessments on the Hurtt's scale for measurement of the professional scepticism.

The received results showed significant difference between high and low sceptical respondents at students regarding the increased desire for collecting additional information in cases of fraud indicators when conducting audit engagements at two out of nine categories of fraud indicators, personal symptoms and personal rationalisations. In the remaining categories of fraud indicators, in the both groups of respondents, the analysis did not show significant difference and the zero hypothesis H_0 was accepted: "there is no difference in the level of gathering additional information if there are noted situations that indicate

fraud in the course of conducting audit engagements regarding the level of expressed professional scepticism”.

All the results from this research are, certainly, preliminary and further research is needed, as well as conduction of empirical work related to the professional scepticism and its relation to the audit behavior that will increase the fraud detection in the course of conducting audit engagements.

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