Introduction

Listed companies in Taiwan are required to prepare their financial statements in accordance with International Financial Reporting Standard (IFRS) from 2013 on. Implementing this policy requires that the English version of IFRS be translated into Chinese as English is not the official language in Taiwan. It is a challenge to make the translation faithfully, especially when the English phrases contain vague meanings (e.g., uncertainty expressions). These phrases tend to have different interpretations in English and may be hard to find their precise counterparts in Chinese primarily due to the fact that translation involves factors associated with not only language but also culture (Doupnik and Richter 2003). Thus, the Chinese translations of the uncertainty expressions may be interpreted with even more variations, which will affect the degree to which IFRSs are implemented as originally intended. This is particularly important when convergence with IFRS has become a trend in the global financial reporting environment. This paper examines how auditors and accounting standard setters interpret (verbal) uncertainty expressions and examines the effects of some proposed factors on reducing the interpretative variations.

Prior Literature and Research Hypotheses

Extant research has indicated that when people communicate uncertain events with verbal expressions instead of numerical expressions, they interpret these verbal expressions quite differently, resulting in miscommunication of financial information (e.g., Amer, Hackenbrack, and Nelson 1994; Laswad and Mak 1997; Reimers 1992). Although there have been recommendations of providing a numerical range in conjunction with a verbal expression to enhance the effectiveness of communication (Reimers 1992; Weber and Hilton 1990), there is no research systematically examining how to reduce the variations in the interpretations of uncertainty expressions. While not directly addressing this issue, the accounting and auditing literature has provided a framework which suggests that person, interpersonal interaction, and environment are determinants of accounting and auditing judgments/decisions (Bonner 2008; Nelson and Tan 2005).

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Drawing on this framework, this paper proposes several factors that are hypothesized to mitigate the variations in interpretations.

Since financial statements are the joint product of corporate management and auditors, this paper focuses on auditors’ interpretation of the uncertainty expressions. Specifically, this paper examines auditors’ interpretation of Chinese uncertainty expressions that appear in IFRS, and examines whether factors associated with person, interpersonal interaction, and environment can reduce the variations in interpreting the uncertainty expressions. Related to the latter, we propose that person factors such as educational level and professional experience will be useful in mitigating the interpretative variations among people. This is because formal education is conductive to the acquisition of knowledge that is well accepted. Accumulation of professional experience is helpful in achieving consensus in judgments through first-hand experience and on-the-job training (Bonner and Pennington 1991; Joyce 1976). With respect to interpersonal interaction, communication is useful in enhancing the degree of consensus (Kenny 1991; Malloy et al. 1997; Schultz and Reckers 1981). As financial accounting standard-setters are more frequent than auditors in communicating the meaning of uncertainty expressions through the standard deliberation process, we expect that their interpretative variation will be lower than that among auditors. Finally, audit structure is an important feature of audit environment within which auditors perform their duties (Cushing and Loebbecke 1986; Kinney 1986). Audit structure provides auditors with smaller room for deviating from the established procedures. As such audit structure will enhance auditors’ agreement in judgment. Based on the above, we propose the following hypotheses for empirical investigation.

H1: Auditors interpret the same uncertainty expressions with variations.
H2a: The interpretative variation of uncertainty expressions is negatively related to the level of education.
H2b: The interpretative variation of uncertainty expressions is negatively related to auditors’ professional experience.
H3: The interpretative variation of uncertainty expressions among accounting standard setters is lower than that among auditors.
H4: The interpretative variation of uncertainty expressions is negatively related to the degree of audit structure.

**Research Methods**

The participants in our study include partners, senior managers, and managers from 17 audit firms whose total number of audit clients accounts for 94 percent of listed companies in Taiwan as of 2008. We sent the questionnaires to the contact partner at each audit firm and asked each of them to distribute the instrument to their colleagues. In total, we sent 292 questionnaires and obtained 158 usable responses (54 percent). The respondents' average auditing experience is 12 years (standard deviation = 4.98 years), 44 percent of the respondents have masters degree or above. To test H3, 14 out of 18 standard setters from Financial Accounting Standards Committee in Taiwan are recruited, 86 percent of them have masters degree or above.

The questionnaire contains two major parts: interpretations of uncertainty expressions, and audit structure. A pre-test with one accounting professor and two partners was conducted. The feedback from the pre-test was then used to revise and finalize the instrument. The 14 uncertainty expressions were developed based on Doupnik and Richter (2003), IFRS, and the financial accounting standards in Taiwan. The respondents were asked to write a numerical interpretation (ranging from 0 to 100, with higher numbers representing higher likelihood) corresponding to each verbal uncertainty expression to represent the likelihood of the occurrence of an event. To prevent from the possible confounding effect of context (Beyth-Marom 1982), respondents are not presented with any context against which they interpret these verbal uncertainty expressions.

We referred to Cushing and Loebbecke (1986) in developing the scale for measuring audit structure. In total, we included 22 statement-items related to audit structure in the instrument. The respondents were asked to rate the degree to which they agree with each statement on a 1-7 scale with “1” representing “completely disagree” and “7” “completely agree.” We performed a principal component analysis on the collected responses, and extracted three factors with each having an eigenvalue greater than one. These factors were then rotated using varimax rotation. The items loading on their corresponding factor have a loading greater than 0.60, suggesting clear separation of the factors. The factors are named as audit plan, fieldwork guidance, and audit tools; and their Cronbach alphas are 0.9186, 0.8528, and 0.8885, respectively. Since audit plan pertains most to the judgment of likelihood, we chose the factor “audit plan” to measure audit structure in the subsequent analysis. For a respondent, we calculated the average of his/her responses to the items loading on “audit plan” as the measure. Thus, the theoretical range of the responses is from 1 to 7. The average of these averages obtained from all respondents coming from an audit firm serves as the audit structure measure for that audit firm.

**Analysis and Results**

We first report the descriptive statistics on the auditors’ interpretations of the 14 uncertainty expressions. The responses range from “remote” (15.67) to “highly probable” (83.50). Eight out of the 14 expressions are interpreted to have occurrence likelihood higher than 50 and six expressions have occurrence likelihood lower than 50. Consistent with prior research, the interpretations for the complementary expressions are lack of symmetry (“expected” vs. “not expected,” “probable” vs. “improbable,” and “uncertain” vs. “reasonable assurance”). For example, the response to “expected” and the response to “not expected” are summed to 89.71 instead of 100. Similarly, the response to “probable” and the response to “improbable” are summed to 113.25 rather than 100. Moreover, the 14 expressions can be formed into nine groups, where the expressions within each group represent similar mean interpretations. This result suggests that the uncertainty expressions are vague and auditors cannot distinguish these expressions from each other clearly. A comparison with prior research in the English context shows that the interpretations of our auditor respondents are similar to those in prior research only for three uncertainty expressions: “highly probable,” “probable,” and “reasonable assurance.” The responses of the auditors in our study are higher than those in prior research when the uncertainty expressions (for example, “improbable,” “not expected”) are in the range of lower likelihood, whereas the responses of the auditors in our study are lower than those in prior research when the uncertainty expressions (for example, “highly probable,” “expected”) are in the range of higher likelihood. Whether this finding is due to the difference in language (English expressions vs. Chinese translations of the English expressions) or the difference in the respondents remains to be explored.

We use the standard deviations of the interpretations as a measure of interpretative variations. The standard deviation of the interpretations for the 14 expressions ranges from 11.95 (“probable”) to 18.79 (“reasonable expectation”). A comparison with prior research indicates that the auditors in our study interpret the uncertainty expressions more diversely than those in prior research. This applies to the individual auditor level as well as the audit firm level. With respect to audit structure, the average audit structure of the 17 audit firms is 5.28 (on a 1-7 scale). The maximum is 6.50 whereas the minimum is 4.03, suggesting that overall, the audit firms in our study are fairly structured in providing audit guidance and procedures.

H1 expects the interpretative variation as represented by the variance of the interpretations to be greater than zero. A Chi-square test is applied to examine this hypothesis, and the results show that all the variances of the interpretations for the 14 uncertainty expressions are larger than zero ($p<0.001$).
Also, a Levene’s test shows that the 17 audit firms are different in their interpretations of seven uncertainty expressions: “expected,” “not expected,” “possible,” “potentially,” “reasonable assurance,” “remote,” and “uncertain” \( (p<0.10) \). There is no difference in the variations of the interpretations for the uncertainty expressions among the Big 4 firms. But, the variances of the interpretations are different among the non-Big 4 firms for eight uncertainty expressions: “highly probable,” “not expected,” “possible,” “potentially,” “reasonable assurance,” “reasonable expectation,” “remote,” and “uncertain.” Taken as whole, the above results suggest that auditors in our study interpret the uncertainty expressions with statistically significant variations. H2a and H2b predict that both educational level and professional experience are negatively related with the variations of interpretations for the uncertainty expressions. Levene’s tests indicate that auditors with a bachelor degree are higher than those with a master degree (or above) in their variations of interpretations for three uncertainty expressions: “highly probable,” “possible,” and “remote.” Thus, H2a is partially supported. To test H2b, we use the median of audit experience to divide the sample into two sub-groups: highly experienced auditors (length of experience > median) vs. less experienced auditors (length of experience < median). Levene’s tests indicate that these two sub-groups are different in their variations of the interpretations for only two uncertainty expressions, but in the opposite direction. Thus, H2b is not supported. H3 predicts that accounting standard setters have lower variations in the interpretations for the uncertainty expressions than auditors. Levene’s tests with bootstrapping procedures show that accounting standard setters have lower variances in interpretations than auditors for five uncertainty expressions: “expected,” “not expected,” “reasonable assurance,” “reasonable expectation,” and “remote.” This result provides some support for H3 in that increasing communication can reduce the variations in interpreting the uncertainty expressions. Finally, H4 predicts that audit structure is negatively related to the interpretative variance. Spearman correlations indicate that an audit firm’s audit structure is negatively related to the firm’s interpretative variance for two expressions: “improbable” and “highly probable.” This result provides partial support for H4.

**Conclusion and Implications**

This study contributes to the literature in two major ways. It is the first study that employs audit practitioners and accounting standard setters to examine the interpretation of Chinese (verbal) uncertainty expressions in accounting standards. In doing so, we recruited as the respondents audit managers, senior managers, and partners from 17 audit firms for which the total number of audit clients accounts for 94 percent of listed companies in Taiwan. Second, it is the first study that proposes and tests factors related to person, interpersonal interaction, and environment in reducing the variations in the interpretations of uncertainty expressions. Our results indicate that auditors’ interpretations for the 14 (verbal) uncertainty expressions are quite diverse at both individual and firm levels. Our results also support the hypothesis that educational level is helpful in reducing the interpretative variation. We obtain some evidence to support the expectations that communications as well as audit structure are helpful in reducing the variations. These results have important implications for audit firms. First, audit firms are suggested to enhance auditors’ communication through discussions or even debates on the accounting standards when conducting on-the-job training for auditors. Second, the fact that audit structure improves the interpretative consensus only for some uncertainty expressions may suggest that audit firms in Taiwan do not differ much in their audit structures and that these firms prioritize to observe the procedures stipulated by the regulatory agency, which is almost uniform as far as audit structure is concerned. Finally, we provide suggestions for future research. First, our study focuses on auditors and standard setters; future research may consider recruiting chief financial officers and financial analysts as the respondents. Second, we only include 14 uncertainty expressions; future research may consider expanding the set of uncertainty expressions.
REFERENCES


