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The Statutory Audit for Small Companies; Necessary or Not?

- A Study of the Swedish Tax Authority's Viewpoint

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**Title: “The Statutory Audit for Small Companies; Necessary or Not?
- A Study of the Swedish Tax Authority’s viewpoint”**

Background and research problems: In Sweden all limited companies have to submit themselves to an audit. Most member-countries in the European Union have chosen to exempt small companies from the statutory audit requirement. In 2003 the Ministry of Justice presented a memorandum that, among other things, suggested an extended regulation about auditor’s and agency’s conflict of interest. Some advisory bodies to the memorandum fear that this will either lead to increased costs for small companies, when they have to engage two different agencies to do their accounting and auditing, or inferior quality if they do the accountancy themselves. This has led to a discussion about the statutory audit for small companies. Small owner-managed companies are a major part of the companies in Sweden. For these companies the annual report serves little purpose, both internally and externally. The external interested party that everyone thinks wants to keep the statutory audit is the Tax Authority. This thesis will try to find out what opinion the Tax Authority has about a possible removal of the statutory audit for small companies, if they see the statutory audit as a guarantee for good quality in the companies’ accountancy and if they see any alternatives to it.

Purpose: The purpose with this thesis is to find out whether the Tax Authority attaches a great importance to the statutory audit for small companies or not. Furthermore, the purpose is to find out if they look upon the audit as a quality guarantee for the company’s bookkeeping and if they see any alternatives to the statutory audit.

Delimitations: The authors have chosen to look at the statutory audit focusing on small owner-managed limited companies with only a few employees and with the Tax Authority as the main external interested party. No company-owners will be interviewed as we focus on the Tax Authority’s perspective.

Method: A qualitative method has been used when collecting primary data through interviews with five representatives from the Tax Authority and one from the Ministry of Justice.

Conclusions: The study has shown that the Tax Authority do not see any reason to remove the statutory audit, since it is important both as a control-instrument and source of information. They also think the audit have a positive affect on the company’s accountancy. On the question of whether there are any alternatives to the statutory audit the respondents answered in unison: no!

Suggestions for further studies: It would be interesting to study alternatives to the statutory audit in countries that have removed it and their development since the removal, and how the tax authorities in these countries obtain information about the companies and if they find the accountancy reliable.

Table of Contents

1 INTRODUCTION	1
1.1 BACKGROUND	1
1.2 GENERAL DESCRIPTION OF THE RESEARCH PROBLEM	2
1.3 DEFINITION OF THE RESEARCH PROBLEM.....	3
1.4 PURPOSE OF THE STUDY	4
1.5 RESEARCH METHOD	4
1.6 DELIMITATIONS	4
1.7 CENTRAL CONCEPTS.....	4
1.8 TRANSLATIONS.....	4
1.9 OUTLINE OF THE RESEARCH PAPER	5
2 RESEARCH METHOD	6
2.1 RESEARCH APPROACH.....	6
2.2 DATA COLLECTION.....	6
2.2.1 <i>Collection of Information</i>	6
2.2.2 <i>Collection of Primary Data</i>	7
2.3 METHOD FOR ANALYSIS	8
2.4 CREDIBILITY	9
2.4.1 <i>Validity</i>	9
2.4.2 <i>Reliability</i>	9
2.4.3 <i>Relevance</i>	9
2.5 CRITICISM OF THE SOURCES	9
3 THEORETICAL FRAMEWORK.....	11
3.1 THE STATUTORY AUDIT	11
3.1.1 <i>The Development of Auditing</i>	11
3.1.2 <i>The Purpose of the Auditing</i>	12
3.2 LAWS REGULATING AUDITORS AND AUDITING	13
3.2.1 <i>The Swedish Companies Act (1975:1385)</i>	13
3.2.2 <i>The Swedish Auditor's Act (2001:883)</i>	13
3.2.3 <i>The Swedish Auditing Act (1999:1079)</i>	13
3.3 THE SWEDISH TAX AUTHORITY	13
3.4 THE MEMORANDUM "A FEW QUESTIONS ABOUT AUDIT"	14
3.5 THE QUESTION UNDER DEBATE.....	14
3.6 ANSWERS FROM THE ADVISORY BODIES	16
3.6.1 <i>Lindebergs Grant Thornton (LGT)</i>	16
3.6.2 <i>Företagarna</i>	16
3.6.3 <i>The Swedish Bank Association</i>	16
3.6.4 <i>The Swedish Association of Lawyers</i>	17
3.6.5 <i>The Swedish Association of Trade and Industry</i>	17
3.6.6 <i>FAR</i>	17
3.6.7 <i>The Swedish Association of Auditors</i>	18
3.7 EARLIER RESEARCH	19
4 EMPIRICAL FINDINGS.....	21
5 RESEARCH FINDINGS AND INTERPRETATION	28
5.1 THE OPINION ON THE STATUTORY AUDIT	28
5.2 A QUALITY MATTER?.....	30
5.3 ARE THERE ANY ALTERNATIVES?.....	31
6 CONCLUSIONS	33
6.1 THE INTERPRETATION OF THE STUDY	33
6.1.1 <i>What is the Tax Authority's Opinion about a Possible Removal of the Statutory Audit for Small Companies?</i>	33

6.1.2	<i>Does the Tax Authority See the Statutory Audit as a Guarantee for Good Quality in the Accountancy?</i>	34
6.1.3	<i>Does the Tax Authority See any Alternatives to the Statutory Audit?</i>	35
6.2	PREJUDICED OR NOT?	36
6.3	SUGGESTIONS FOR FURTHER STUDIES	36
REFERENCES		37
	LITERATURE	37
	ARTICLES, THESES AND REPORTS.....	37
	INTERVIEWS.....	38
	INTERNET	39
	LAWS	39
	DATABASES.....	39
 LIST OF ILLUSTRATION		
	FIGURE 1: THE INTERESTED PARTIES OF THE STATUTORY AUDIT	12
 APPENDICES		
	APPENDIX A: INTERVIEW MANUAL 1	
	APPENDIX B: INTERVIEW MANUAL 2	
	APPENDIX C: INTERVIEW MANUAL 3	
	APPENDIX D: INTERVIEW MANUAL 4	

1 Introduction

This opening chapter illustrates the background of this thesis. It also describes and defines the research problem, the purpose and the papers delimitations. Central concepts will be defined, as well as translations of words important to the paper, and finally the papers outline is described.

1.1 Background

In Sweden it is compulsory for all limited companies, regardless of size, to submit themselves to an audit. This is regulated in the Swedish Bookkeeping Act, the Swedish Companies Act and the Swedish Auditor's Act. The question about the future of the statutory audit for small companies has been discussed several times. In the 1990s the debate started with an official letter from the Government about deregulation and the abolishment of statutory audit for small limited companies. Several articles in *Balans* 1994 and 1995 supported the proposition, but by a parliamentary resolution the proposition was put aside without any legal action (FAR INFO, no. 2, 1995). The European Union's Fourth Directive authorizes the member-countries to exempt small companies from the statutory audit requirement, which most countries have done. When the European Commission 1996 published the Green Paper "The role, the position and the liability of the statutory auditor" they saw no reason to change this. However, the Commission did point out the risk for money laundering and other economic crime without a statutory audit. (FAR INFO, no. 13, 1996)

Due to the on-going discussion concerning auditor's conflict of interest, the question about the statutory audit has arisen again. The discussion is based upon the opinion that the company's external privies should be able to trust the auditor's independence when executing the audit. This will guarantee that the company's financial situation is correctly shown. In its memorandum "A few questions about audit" (JU2003/3072/L1), the Government follows the same point of view, and proposes an amendment of law to preventing an auditing company conducting both the annual financial statements and the audit. Some advisory bodies, for example the Swedish Association of Shareholders and the Swedish Authority of Economic Crime, also share this view. The responding auditing companies, Lindebergs Grant Thornton and Öhrlings PricewaterhouseCoopers, on the other hand, are certain that their internal methods and procedures are sufficient enough to prevent the problem with auditors' independence. (Balans, 2003, pp.41-45)

In connection with the discussion, some advisory bodies have reacted on how an amendment of the law would affect small limited companies. In the response from the University of Uppsala it is being questioned whether small and large companies should follow the same regulation, considering the Government's aim to facilitate the conditions for small and medium-sized companies. The University doubt that such a thorough alteration in law can be carried out without an analysis of the consequences first being made. The above mentioned auditing companies also think that the consequences should be investigated, and that the question of the statutory audit should be included in the discussion. *Företagarna* opposes all changes that complicate the situation for small companies, and would rather see an abolishment of the statutory audit for small companies. (Balans, 2003, pp.41-45)

The analysis of consequences is a decree regulating the public authorities. When altering a law they have to analyse the effects on small companies' conditions. (SFS no. 1998:1820)

1.2 General Description of the Research Problem

After several accountancy scandals, for example Enron in the USA, auditors have been accused of not being independent enough in their relation to the companies. This has led to an international discussion concerning auditing and accounting principles (FAR:s Revisionsbok 2002, p.116). An effect of this in the USA is the Sarbanes-Oxley Act (SOX), which affects board of directors, management as well as auditors. To insure that the auditor is independent, the law fundamentally bans the auditor from performing services other than auditing for their clients. (FAR INFO, no.8, 2002) The European Union has created new regulations, which form the base for the Swedish Ministry of Justice's memorandum, proposed to further harmonise the Swedish set of rules and regulations with the Union's (JU2003/3072/L1). The memorandum treats both the rules regarding the auditor's report and the auditor's term of office regulated in the Swedish Companies Act, as well as the question of auditor's conflict of interest and who is eligible to perform certain accounting services. It also includes a change concerning agency's conflict of interest, which would be a tightening of the law. This would prevent an auditing company from both performing both an audit as well as the client's bookkeeping. This has again started a debate as to whether the statutory audit is being justified in small limited companies. It is being claimed that their situation is being complicated due to the large companies' accountancy scandals, which is in contradiction of the Government's aim to facilitate the conditions for especially this group (Balans, 2004, pp.15-27).

In April 2004 there were 858,064 companies in Sweden, of which 240,258 were limited companies. Of these 194,766 are small ones, with not more than five employees. (www.scb.se) They represent an important part of the labour market and their accountancy is controlled by the same regulations as the large companies. There is, however, some alleviation for companies with a turnover below 10 millions and not more than 24 employees (the Swedish Bookkeeping Act 6 chap. 1 §). They can make an annual accounts book instead of an annual report and the requirement of information is less demanding. (Thomasson *et al.*, 2000, p.118) The small companies usually do not have any employee capable of keeping the books. Instead they might have to engage external help for both the bookkeeping and the audit. The consequences of the memorandum would therefore be that even the smallest limited company, perhaps consisting of one person, must engage two different agencies. According to the memorandum, there is a belief that a change of the regulation will lead to an increased competition between the agencies, which would prevent any increased costs for the companies (JU2003/3072/L1). In Balans (2004, pp.15-27) several auditors are of an opposite opinion – a change will lead to a waste of time and increased costs for the companies.

The annual report serves little purpose in the owner-managed companies, internally as well as externally, and therefore it is being looked upon as mainly a cost. In addition to this, there is also the cost for the statutory audit, and these costs along with the extra work are being stressed from several advisory bodies as the reasons why an analysis concerning the small companies' situation must take place before any decision is made.

There is naturally a difference in the role that the annual report plays in a small private company compared to a public one. In large companies the external accountancy becomes an important instrument for the owners to control whether the management is doing a good job, and to decide whether to buy or sell any shares. In small companies the owner and manager is usually the same person, with access to the internal accountancy why the external becomes less important. (Smith 2000, pp.17-22)

The regulation of Swedish accountancy belongs to the continental tradition with a strong connection between the civilian- and tax legislation (Smith 2000, p.73). Common interested parties for the companies, irrespective of size, is the Government, whose need of information is based upon the need to find out whether the companies taxable income has been calculated in accordance with generally accepted accounting principles (Smith 2000, pp.17-22). According to Dan Brännström, it is likely that the statutory audit for small companies exist due to the Government in order to look after their interests, but also in order to prevent economic crime. When the Minister of Justice, Thomas Bodström, answered an interpellation concerning the small companies' situation, he said that the consequences are important factors to consider before he is prepared to make up his mind about the memorandum. (Balans, 2004, pp.15-27)

1.3 Definition of the Research Problem

With the present discussion as background, the authors find it interesting to study the question whether the statutory audit for small companies should be abolished or not. Earlier papers have looked upon the question from both the auditors' and owner-managers' point of view, why the authors think it would be interesting to focus on the Swedish Tax Authority, the external interested party everyone takes for granted is eager to keep the statutory audit as it is. This leads to the papers main question:

- *What is the Tax Authority's opinion about a possible removal of the statutory audit for small companies?*

If the memorandum is accepted the companies have two alternatives. They can either engage both bookkeeping and an auditing agency, or they can take care of the bookkeeping themselves. This could, according to some of the advisory bodies, lead to an inferior quality of the accountancy, which raises one more question:

- *Does the Tax Authority see the statutory audit as a guarantee for good quality in the accountancy?*

According to the Fourth Directive, the statutory audit for small and medium-sized companies can be decided on a national level in the member-countries within the European Union. Several countries have used the opportunity and abolished it. This makes the authors wonder whether the Swedish Tax Authority is following the development in other countries and leads to the final question:

- *Does the Tax Authority see any alternatives to the statutory audit?*

1.4 Purpose of the Study

The main purpose with this paper is to find out whether the Swedish Tax Authority attaches great importance to the statutory audit for small companies or not. Further purposes are to find out if the Tax Authority looks upon the audit as a quality guarantee for the company's bookkeeping and if they see any alternatives to the statutory audit.

1.5 Research Method

To improve the knowledge of the subject information from journals, papers and databases has been collected. The information has then formed the basis for the following interviews with the representatives from the Swedish Tax Authority and the Ministry of Justice. The interviews are the primary data in this paper. The method will be described in detail in chapter two.

1.6 Delimitations

To avoid this paper from becoming too extensive a few delimitations have been made. The authors have chosen to look at the statutory audit focusing on small owner-managed limited companies with only a few employees and with the Tax Authority as the main external interested party. No owners of small companies will be interviewed as the paper focus on the Tax Authority's perspective.

1.7 Central Concepts

The statutory audit is a company's obligation to become audited by an external, independent auditor. This obligation is applicable to all limited companies in Sweden, irrespective of size. Other forms of companies are limited by different regulations (the Swedish Bookkeeping Act 6 Chap. 1 §).

An audit means that an auditor examines a company's annual report, bookkeeping as well as the board and management's administration afterwards (the Swedish Companies Act 10 Chap. 3§). The purpose with the audit is to give credibility to the company's financial information; so that the company's different external parties experience it as reliable. It is for example important to the Governmental authorities, since the accountancy forms the base for taxation calculations.

1.8 Translations

The Swedish Bookkeeping Act	Bokföringslagen
The Swedish Companies Act	Aktiebolagslagen
The Swedish Annual Accounts Act	Årsredovisningslagen
The Swedish Auditor's Act	Revisorslagen
The Swedish Auditing Act	Revisionslagen
The Swedish Tax Authority	Skatteverket
The Swedish Association of Shareholders	Aktiespararna
The Swedish Authority of Economic Crime	Ekobrottsmyndigheten
The Swedish Enforcement Authority	Kronofogdemyndigheten
The Swedish Bank Association	Svenska Bankföreningen
The Swedish Association of Lawyers	Svenska Advokatsamfundet

The Swedish Association of Trade and Industry	Svenskt Näringsliv
The Swedish Association of Auditors	Svenska Revisorssamfundet
The Swedish Supervisory Board of Public Accountants	Revisorsnämnden
Generally Accepted Accounting Principles	God redovisningssed
Generally Accepted Auditing Standards	God revisionsssed
Auditor's conflict of interest	Revisorsjäv
Agency's conflict of interest	Byråjäv
Article of Association	Bolagsordningen
Statutory audit	Revisionsplikt
Qualified auditors' report	Oren revisionsberättelse

1.9 Outline of the Research Paper

In this the first chapter the background of the paper has been described, as well as the definition of the research problem and the papers purpose. Below the disposition of the following chapters is shown.

- Chapter 2 In the second chapter the method used is being described and furthermore will a discussion concerning the paper's credibility be carried out.
- Chapter 3 This chapter forms the theoretical framework and accounts for the development of auditing and the regulation of today. Further on the answers of the advisory bodies are being summarized and lastly earlier research is being presented.
- Chapter 4 In this chapter the information from the conducted interviews is compiled. The empirical findings form the base for the following analysis and conclusions.
- Chapter 5 Based upon the theoretical framework the research findings will be analysed and interpreted, as well as connected with the earlier research found.
- Chapter 6 The final chapter summarizes the principle findings of the analysis, and the authors answer the research problem defined in the introduction chapter. Lastly, suggestions for further research will be made.

2 Research Method

This chapter describes two different methods of data collection, the qualitative and the quantitative methods. Thereafter, the authors' procedure in collecting information and primary data is presented to give the reader a possibility to evaluate the paper's credibility. The method of analysis is also described. The relevance and credibility of the paper is discussed, and finally the sources are critically reviewed.

2.1 Research Approach

It is possible to distinguish between two different methodical approaches: qualitative and quantitative method. The *qualitative* method does have a small grade of formalisation, and primarily, an understanding purpose. The most important is that through different ways collect information, and also gain a deeper understanding for the problem complex being studied, and describe the entirety that it is part of. It is not interesting to test if the information has universal validity. The distinguishing mark for the method is the closeness to the source of information. (Holme & Solvang, 1997, pp.13-14)

The *quantitative* method is more formalised and structured. The method defines the circumstances that are of special interest for the chosen formulation of the question, and decides possible answers. The distance to the source of information is longer in this method. Statistical methods of measuring have a central part when analysing quantitative information. (Holme & Solvang, 1997, pp.13-14)

The authors are of the opinion that for the paper's questions a qualitative methodical approach is most appropriate. The reason for this is that the study's character is such that the result can not be processed statistically. The result is a mass of text and the goal is to gain understanding for the chosen field of study, and draw conclusions in order to answer the questions that the authors want to answer from it.

2.2 Data Collection

The following section gives an account of the writers' procedure in collecting information and primary data.

2.2.1 Collection of Information

The idea to this paper comes from a Master thesis in business management at the School of Economics and Commercial Law at the University of Göteborg. The title of the paper is "What use is an annual report to small businesses?" where the authors suggest further research in this topic. This is how the idea about the Swedish Tax Authority's opinion regarding an eventual removal of the statutory audit for small companies was found. (Alonso & Andersson, FE R/F 02-55)

The collection of information has mainly been conducted through searching in databases, literature and journals. Most of the information has been found in databases available at the Economic Library at the University of Göteborg. To get started with the search an appointment was made with a librarian at the Economic Library, who informed us of the appropriate databases suitable for the thesis and also appropriate search-words. This help was invaluable. Databases used were among all Business

Source Premier, Affärsdata, Emerald and Ebsco. Another database used was FAR-Komplett, which often refers to articles in the professional journal Balans, which is being published by FAR. In case these articles have been used, they have been read in Balans to verify the contents. Search-words in Swedish databases have mainly been “revisionsplikt” and “småföretag”. When searching in foreign databases the words “audit” and “small business” have been used. Written material used consists of books, investigations and articles in newspapers and journals.

Information about the statutory audit debate of the 1990s and today’s debate has been collected from articles in Balans and the database FAR-Komplett. A summation of the article in Balans is presented in the theoretical framework. Information about today’s debate has also been obtained from the Ministry of Justice’s memorandum “A few questions about audit” and the answers from some advisory bodies. The memorandum, too, is summarized in chapter three. To get knowledge of which advisory bodies answered the memorandum “A few questions about audit” a summation of the advisory bodies was printed out from the homepage of the Ministry of Justice (JU2003/3072/L1). Answers presented in detail are mainly those who brought up the consequences for small companies. The chosen advisory bodies are Lindebergs Grant Thornton, Företagarna, the Swedish Bank Association, the Swedish Association of Lawyers, the Swedish Association of Trade and Industry, FAR and the Swedish Association of Auditors. To procure correct information about their answers some of the advisory bodies were contacted in order to obtain their complete answer. Other answers were found on the homepages of the advisory bodies.

To get a concept of what the statutory audit requirement entails and its development, a description of this is included in the theoretical framework. Information has also been obtained from the Swedish Companies Act, the Swedish Annual Accounts Act and the Swedish Auditing Act. To get the background of today’s discussion, the memorandum is summarized in the theoretical framework. A description of the Swedish Tax Authority’s mission is also enclosed in the theoretical framework.

2.2.2 Collection of Primary Data

Primary data are basic data collected by the authors themselves from the original source (Lekvall & Wahlbin, 2001, p.212). The authors have chosen interviews as method, since this is the most suitable form to enter deep into a subject. It is also possible to alter the order of the questions in the interview manual, make attendant questions and to set forth the discussion. A tape recorder was not used during the interviews; instead the answers were compiled and mailed to the respondent who had a possibility to make sure that he was correctly quoted and also to make further comments. This in order to make sure that the answers was correctly understood.

The empirical base of primary data for this thesis is composed of interviews with Jan Sandvall, Magnus Wallin, Lars Osihn, Tommy Andersson and Alf Hallgren, who work in different cities and in different positions within the Swedish Tax Authority. First, the interview manual was composed and then the Tax Authority was contacted and the purpose with the thesis was explained. This was made in order to find respondents suitable for the subject. An interview with Jacob Aspegren at the Ministry of Justice has also been conducted in order to get a background to the memorandum and to get a picture of the Ministry’s view on the statutory audit for small companies.

It is possible to distinguish between qualitative and quantitative interviews where the quantitative one is equal to the poll with a standardized questionnaire. The qualitative interview is informal and has to be adjusted to the interviewee. An advantage with qualitative interviews is that the respondent is not forced into a certain way of thinking. Instead he gets a margin of discretion for his own thoughts and opinions. The personal presence of the interviewer makes it possible to explain ambiguities. When the interview manual is formulated, it is important that the questions are relevant and that the formulation of the question is possible to answer. It is also important that the number of questions is not too many, so that the interviewee loses interest. (Holme & Solvang, 2001, pp. 99-108) The authors formulated different interview manuals since the knowledge about the topic was improved along the way. All interview manuals are appendices to the paper.

Telephone interviews are special; they cannot take too long time so the number of questions has to be limited. The questions cannot be too difficult but has to be answerable without too long time for consideration. The big advantage with this method is that it is fast to conduct. (Dahmström, 2000, pp.75-78) Two interviews were conducted by e-mail. The personal contact is lost but the respondent can answer when he has time and take the time needed in order to answer.

Jan Sandvall and Magnus Wallin were interviewed personally at the Tax Authority's office in Rosenlund, Gothenburg. The interviews with Jacob Aspegren at the Ministry of Justice and Alf Hallgren were conducted via telephone by one of the authors. The interviews with Tommy Andersson and Lars Osihn have been conducted via e-mail.

2.3 Method for Analysis

In order to be able to answer the thesis's questions the collected information in a research work has to be systematized, compiled and processed. The methods for processing text material are called qualitative methods. Qualitative methods are often time- and work consuming, since a lot of text material has to be processed. It is not unusual that thoughts regarding the problem area come up during the data collections and the initial analysis. It is important to record these thoughts before the final analysis. A good way is to write a diary, about everything happening in the investigation and all original thoughts and reflections that come up during the work process. (Patel & Davidson, 1991, p.100)

It is often practical to do regular analyses when working with a quantitative investigation. New and unexpected information can for example come up during an interview. Before the finalizing, the whole text material has to be reread, if possible several times. It is important, in the paper, to account for how the researcher methodically has done the processing, since it is not possible to find one collectively agreed method to conduct a qualitative process. It must be possible for the reader to follow the researcher's line of work. (Patel & Davidson, 1991, p.100)

After having conducted the interviews the notes were looked through and compiled. When ideas, useful for the analysis, came up they were written down in order not to be forgotten. The paper was also reread several times to obtain new ideas for the analysis. These ideas were also written down. From these ideas the authors have analysed and discussed the way to the conclusions.

The authors have been particular about making sure that there is a main thread through the paper, in other words, that the different parts/chapters are connected with each other, as well as making sure that the questions have been answered. As the thesis is written in English, a lot of effort in finding the right words has been made. To get the translation as correct as possible, the programmes FAR's Dictionary and Word Finder, a Swedish-English Business Dictionary, have been used.

2.4 Credibility

A thesis has to give a true and fair view of the reality. It has to fulfil the requirements for validity, reliability and relevance. These requirements are described below.

2.4.1 Validity

Validity is a measurement of how good a measuring or measuring instrument is. Validity means measuring what the formulation of the question says you should measure. (Eriksson & Wiedersheim-Paul, 2001, p.38). When collecting primary data it is important that the interview manual is formulated in accordance with the papers purpose and problem. The interviews were conducted after the in advance fixed interview manual. The respondents were able to speak freely and also to give information about their background, so the authors could themselves envisage a picture of it and their knowledge of the subject, and also to create confidence. The questions were not made available to the respondents in advance in order not to get prepared answers.

2.4.2 Reliability

The reliability has to do with the measuring method to resist influence from different coincidences in the interview situation. If it is possible to conduct the same measuring several times and obtain the same result, the reliability is considered to be high. The more clearly and less vague questions that are put to the respondent the larger the possibility to obtain an acceptable reliability. (Lekvall & Wahlbin, 2001, pp. 306-307) Through clear and evident questions, and by letting the respondent read through the compiled answers, and also contribute with things they want to clarify, the authors feel that a good reliability has been secured.

2.4.3 Relevance

Relevance means that the investigation should have a message, a "point", in other words it should be interesting to others than the authors (Eriksson & Wiedersheim-Paul, 2001, p.38). Since the debate about the statutory audit has been going on several times, and the European Union does not mind if the member-countries remove it, this is something that are interesting to a great number of people. The Swedish Tax Authority's opinion on this question has not been examined before, and therefore this paper can give a new angle in the debate.

2.5 Criticism of the Sources

The purpose with criticism of the sources is to determine if the used source measure what is supposed to be measured (is it valid), if it is important for the formulation of the question (is it relevant) and if it is free from systematic faults (is it reliable). When writing, criticism of the sources is a method of selection, where the collected material is being judged, clearing away that which is considered not good and keeping that which is considered acceptable. You also have to evaluate the result presented in the paper in

order to be able to know the result. The reader has to make the same critical examination of the authors' choices and evaluation of the different sources. (Eriksson & Wiedersheim-Paul, 2001, p.150)

The answers collected from the advisory bodies are those that have been sent in to the Ministry of Justice's memorandum "A few questions about audit" (JU2003/3072/L1). These sources probably answer in their own interest. The interviews may have been affected by the respondents' personal opinions. Since it is the Swedish Tax Authority's opinion that is the essential in this paper several people on different levels, and in different cities, have been interviewed. By including several advisory bodies with different views on the statutory audit the authors feel that the requirements for credibility are met. In spite that several articles from research journals have been used, some of them, according to the authors, can be considered as contributions in a debate. But since they are published in verified research journals, they have to be considered as reliable.

3 Theoretical Framework

This chapter describes the theoretical framework, which forms the basis for the continuing work with this paper. Initially the statutory audit's development and purpose is described, followed by the laws regulating it. The Swedish Tax Authority and its mission are briefly explained, the answers of the advisory bodies are summarized, and finally previous research within the field is discussed.

3.1 The Statutory Audit

Below follows a short description of the development of the statutory audit, its purpose and regulation of today.

3.1.1 The Development of Auditing

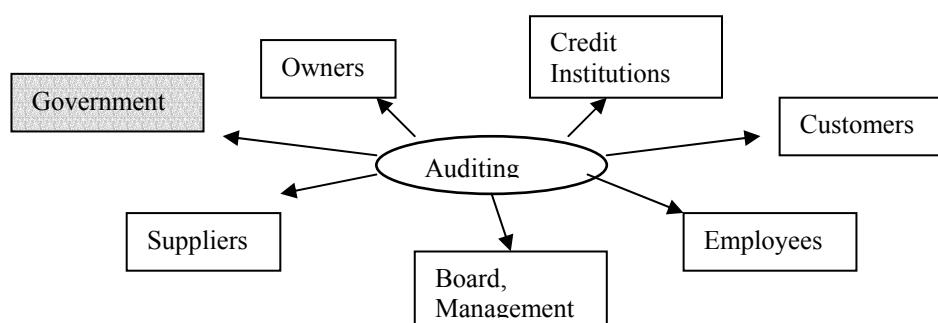
At the end of the 19th century the industrialization of Sweden was at full swing. From 1897 to 1907 there was an increase in the number of limited companies with 117 per cent, which meant a change in the business world and the structure of ownership. Frauds were frequent in trade and industry, which led to a discussion within the Swedish Parliament concerning the limited companies' legislation. As a result the law was rewritten and in the Swedish Companies Act of 1895 it was for the first time prescribed that a limited company should have an auditor. The argument against a statutory audit was as early as then that the costs for small companies would increase, and besides, the Government should interfere as little as possible. Those who were in favour meant, that a statutory audit on a voluntary basis would hardly prevent the increase of economic crime. The auditor in those days were usually a man of good name, who accepted the roll as an auditor mainly as an honorary task and not always because he was the most suitable for the job. (Sjöström, 1994, pp.29-32)

The law has been changed several times through the years. Issues constantly being discussed have been economic crime, the education of the auditors and their independence. In the Swedish Companies Act of 1910 the first stipulations concerning the conflict of interest was introduced, forbidding the auditor from being in neither the company's nor any member of the board's service. In 1944 the Government stepped in and decided in detail how the auditor's tasks were supposed to be performed. The reason was among other things the Kreuger-crash and its consequences. In 1975 the Government left it to the profession to decide how the annual report should be audited, by introducing the words generally accepted accounting principles (GAAP). During this year further tasks for the auditor were introduced. Despite that 21 out of 27 advisory bodies opposed, it was decided that the auditor from now on must remark if the company has not fulfilled its obligations concerning taxation and other charges. It was furthermore decided that the auditor has to give information about the company if there is an economic crime being investigated and the leader for this investigation so demands. Since 1980 the companies have to register their auditor at the Swedish Patent and Registration Office. This was decided in order to prevent the companies from changing auditor if he would become uncomfortable and in that respect strengthens his independence. Not until 1983 have all limited companies become obliged to engage an approved or authorised auditor. It was not until then the Government thought there were auditors enough to fill the need by such a regulation. (Sjöström, 1994, p.47) Today's regulation is being described under the Swedish Auditing Act of 1999.

3.1.2 The Purpose of the Auditing

The audit's aim is for the auditor to present the auditor's report. This consists of two parts where he comments the company's accountancy and management, based upon the auditing and judgement of these. In the auditing of the accountancy he examines whether the company has been following what the law and GAAP stipulate and the aim is to certify the credibility in the company's financial information. The audit of the management is to examine whether the board and manager are following the rules stipulated in the Swedish Companies Act, the Swedish Annual Accounts Act and the Article of Association. This is the only official report the auditor presents, but while examining the company he can submit different kinds of reports to the management. These can be critical towards different functions within the company and is usually handed over together with suggestions on how to make improvements. Substantial faults being attended to, do not have to be reported and become official. If, conversely, real falsifications are being discovered the auditor has to inform the management at once. In this way he is handing over the responsibility to the management to take action. Substantial derogation from the law and GAAP must be shown in the auditor's report and is taken very seriously. In specific cases the qualified auditors' report has to be handed in to the Tax Authority. This is the case if for example the board or/and the manager have done something for which they can become liable to pay compensation, if they have not fulfilled their obligations concerning the tax payment or broken any other law. It also has to be handed in if the auditor does not recommend the report and accounts to be adopted. (FAR:s Revisionsbok, 2002, pp.14-62)

The audit is not beneficial only to the owners of a limited company, though they are the main interest party to large companies. Other interested parties are credit institutions, which have to judge whether the company will be able to pay its debts or not. Suppliers want to know if it is safe to deliver on credit and customers if the deliveries will continue. Even the employees are, due to their situation of dependency, interested in the company's situation and future development. The different interested parties mentioned all have an interest in the company's future, while the last ones – the Government and other authorities – are more interested in that the accountancy, which forms the base for taxes and other dues, is calculated according to the GAAP. (Smith, 2000, p.22)



Figur1: The interested parties of the statutory audit. (Interpreted from FAR:s Revisionsbok, 2002, p.17)

3.2 Laws Regulating Auditors and Auditing

There are several regulations controlling the audit and the auditor. Below some of them are briefly described. Further laws and regulations are the European Union's Fourth, Seventh, Eighth and Eleventh Directives, the Law of Economic Associations, the Swedish Annual Accounts Act, the Swedish Bookkeeping Act, the Auditors' Decree, the EC's Recommendation of Qualitycontrol, the Directives of the Swedish Supervisory Board of Public Accountants, FAR's ethical rules (generally accepted auditing standards) and FAR's Recommendations of Auditing. (FAR:s Revisionsbok, 2002)

3.2.1 The Swedish Companies Act (1975:1385)

In a limited company the owners are usually not responsible for the company's debts and the main purpose of the law is therefore to protect the company's creditors. The purpose is also to protect owners with small holdings of shares in companies with many owners. (Andersson *et al.*, 2000, p.86) The law contains detailed regulations concerning almost everything about the limited companies, from starting the company to how to go into liquidation. The regulation about auditing is found in the tenth chapter, as well as the tasks the auditor has to perform.

3.2.2 The Swedish Auditor's Act (2001:883)

This law defines the difference between an approved and an authorised auditor and in what form their business can be practised, which is as a private business, partnership firm together with another auditor and as a trading or limited company. Furthermore, the auditor's obligations are being accounted for, where the GAAP comes first followed by the regulations that will guarantee the auditor's independence, an issue being discussed since the demand for an auditor became mandatory. The law also clarifies what information auditors and auditing agencies are obliged to give to the Swedish Supervisory Board of Public Accountants and what disciplinary measures will be taken if an auditor deliberately does something wrong in his business.

3.2.3 The Swedish Auditing Act (1999:1079)

This law contains several regulations also found in the Swedish Companies Act and the Swedish Auditor's Act, for example that a company must have at least one auditor and what the tasks of the auditor are. It furthermore clarifies how to choose an auditor and which qualifications are required. The law also supports the auditor in his auditing business, by enjoining the management to provide the auditor with all the help he finds necessary. It is also stipulated how the auditor should proceed if he has to leave an assignment, what an auditor's report must contain and how to act if the auditing ends up with a qualified report.

3.3 The Swedish Tax Authority

The Swedish Tax Authority is a freestanding authority under the jurisdiction of the Ministry of Finance. It has existed in its present form since January 2004 and was founded after a memorandum presented by the Government early in 2003 ("The new Tax Authority", 2002/03:99). The earlier Swedish Tax Board and ten different Tax Authorities have become one authority, responsible for the same tasks as before. The Authority administrates issues concerning taxes, welfare dues and value-added dues to the European Union budget. It is also responsible for the national registration and estate inventories and a central authority to The Swedish Enforcement Authority's field. (www.regeringen.se)

3.4 The Memorandum "A few questions about audit"

In June 2003 the Ministry of Justice presented the memorandum "A few questions about audit". It suggests, among other things, a change of the Swedish Companies Act and discusses a request from FAR that company's management should be obliged to provide the auditor with the information needed for the audit voluntarily, and that neglecting this should be penalized. The regulation of today says that the management must provide the auditor with the information he finds necessary and according to the memorandum, this is sufficient enough and several reasons are given why the request from FAR not should lead to a change in this matter.

The memorandum also contains a comparison between the European Union's Fourth Directive and the Swedish audit report as well as considerations as to how the changed Directive will affect the Swedish regulation. Since the national regulations should be harmonized with the EC-Directives, the changes in the Fourth Directive should affect the rules in the Swedish Companies Act concerning the audit report's form and content. Another difference is that in Sweden the auditors' term of office is four years, but according to EC-regulation, it should be seven years. It is therefore suggested that the term of office can sometimes be decided to three instead of four years. (JU2003/3072/L1)

According to the Swedish Companies Act, an auditor is not allowed to work at the same agency as the one that is taking care of the company's basic bookkeeping. Due to, among other things, the technical development it is suggested that this will be valid for all accountancy. It is considered that a combined assignment, where the auditor is auditing the accountancy performed by a colleague, can become a threat to the auditor's independence. According to the EC-recommendation, the regulation against combined assignments is already valid for companies of public interest.

For small companies combined assignments are usual and a change of the regulation will enforce them to engage an agency other than the auditor's for the bookkeeping or choose to do the job themselves. The Ministry of Justice thinks the competition between those who are providing the bookkeeping-services will increase, and therefore not influence the costs for small companies. The consequences for the auditing business are expected to be manageable, since the employees at the auditing agencies working with bookkeeping can be employed at the bookkeeping agencies instead. According to the memorandum, the positive effects on the quality of, and the credit in, the statutory audit might more than compensate for eventual problems in the beginning. (JU2003/3072/L1)

3.5 The Question under Debate

It has been possible to follow the debate concerning the statutory audit for small companies in Balans. Below is an article being presented, where representatives from different associations express their opinion. Lastly, the Minister of Justice is answering an interpellation on this matter. (Balans, 2004, pp. 15-27)

Arguments in the Debate

The debate in Balans is focused on the small companies' situation. Stefan Persson, in charge of Ernst & Young's National Auditing Department, agrees that accounting- and auditing assignments not should be combined, but is also of the opinion that the statutory audit can be removed. He claims that small companies need an accountant but

not necessarily an audit. Peter Bodin, COO of Lindebergs Grant Thornton, on the other hand, thinks that the regulation should remain in its present form. A tightening of the law concerning the agency's conflict of interest might force companies to engage two different agencies and lead to higher costs, which would affect the small companies most. Gunvor Engström, COO of Företagarna, reacted strongly against the memorandum's proposals. She does not think the small companies should suffer from the large companies' scandals and sees two possibilities; either they are exempted from the ban against combined assignments or the statutory audit should be removed. Dan Brännström, Secretary General of FAR, shares these opinions. "Engaging two different agencies would be complicated and expensive for them", he says.

Another concern most of them share is that a ban of combined assignments would affect the small companies' accountancy. According to Bodin, the ban might encourage the companies to take care of their accountancy themselves in order to lower the costs, which can lead to an inferior quality. Brännström is of the opinion that both the annual account and annual financial statement may be of inferior quality. Engström says, that with one agency handling both the bookkeeping and the auditing the quality may increase. This since the auditor knows how the bookkeeping has been made, and that ambiguities and misunderstanding can easily be cleared up.

Even with a removal of the statutory audit requirement some sort of auditing would take place, according to Persson. For example, the banks would require it when a company applies for a loan. A market-demanded audit would affect the audit's price and also improve its status. Bodin is expecting that the development in Great Britain, where the statutory audit has been removed and the auditing trade has seen some positive effects, would also take place in Sweden. Brännström is of the opinion that the Government, due to guarding the fiscal charges and to fight economic crime, wants to keep the statutory audit. He does, however, think that there will be a difference in the regulations between small and large companies and that the small company audits in the future will be executed when sought-after. Auditors, Brännström continues, may get new tasks, for example new forms of certifying to the Tax Authority and banks. Finally, he states that without the limitations from the statutory audit regulation, the possibilities increase for the auditor to give advice and assistance to the small companies. This viewpoint is shared by Engström, who argues that the auditor is one of the company's best friend and adviser. Without a statutory audit the company can engage the auditor for more counselling.

Thomas Bodström, Minister of Justice

In an interpellation Anna Grönlund (fp) asked Bodström what he is going to do to make sure that the work for a stronger auditing in the business world does not lead to an even harder burden and higher costs for the small businessman in Sweden. Bodström answered that the reasons for the proposals in the memorandum is that an auditor auditing accountancy completed by him is not independent; likewise if somebody else in the same auditing firm completes the accountancy. Combined assignments mainly exist in small companies but many of them already have chosen to let somebody other than the engaged auditors firm to do the accountancy. Bodström stated that he at the present was not prepared to take a stand on the memorandums proposals. He takes the view that the consequences for the small companies are a very important aspect and something that will be taken into account.

3.6 Answers from the Advisory Bodies

The upcoming section will summarize the answers from some advisory bodies to the Ministry of Justice's memorandum "A few questions about audit". The advisory bodies chosen are mainly those having an opinion about the statutory audit for small companies. These are Lindebergs Grant Thornton, Företagarna, the Swedish Bank Association, the Swedish Association of Lawyers, the Swedish Association of Trade and Industry, FAR and the Swedish Association of Auditors.

3.6.1 Lindebergs Grant Thornton (LGT)

LGT is one of the major auditing companies in Sweden, which carry out auditing, accounting and counselling mainly to owner-managed companies. Therefore, it is affected by the proposal concerning agency's conflict of interest. LGT does not think the proposal will strengthen the quality of either the audit or the accounting for the affected companies, and furthermore that the findings of the consequences lack support in reality. LGT also thinks that it has routines and methods to handle the problems of independence. The proposal is not in line with the Government's ambition to facilitate the terms for the small companies. If small companies must have one company to handle the accounts and another to make the audit the costs for these companies will increase, according to LGT. Non-public interest companies should be exempted from this regulation. Finally, LGT writes in its referral answer, if the Government consider realizing the proposal the consequences has to be investigated and analysed in a more thorough way and that the question of the statutory audit requirement for small companies must be taken under consideration. (www.lindebergs.se)

3.6.2 Företagarna

Företagarna is an interest organisation for the business owners with about 80,000 members. The mission of the organisation is to create better conditions for starting, running and developing companies in Sweden. In its referral answer the organisation questions weather the same rules can apply to both large and small companies. They feel that the proposals must be adapted further to the interest of the small companies and their privies. The organisation thinks the proposed regulations for auditor's conflict of interest should only apply for listed or public companies, alternatively that the statutory audit for small and medium-sized companies is removed. If the combined assignments are removed, Företagarna fears that the costs, mainly for the small companies, will increase. They also take the view that if the same firm performs both functions it is easier to communicate and the auditor puts more trust in the accounts, which will decrease the need for audit tests. Therefore, the quality of the audit increases and the price decreases factors that are especially important to small companies. The need to communicate with two different firms would mean an increased workload, something that increases costs. In order to decrease costs, Företagarna suggests that the statutory audit should be made voluntary for small and medium-sized companies. But they think that banks and lenders will continue to demand an impartial review of the company's accounts. (www.foretagarna.se)

3.6.3 The Swedish Bank Association

The Swedish Bank Association represents the banks in Sweden and spreads knowledge of the banks and their role in the society. It also works for a well-functioning and efficient banking sector. The association represents the member companies towards authorities and organisations both nationally and internationally. The Association does not think that the proposed change of the auditor's term of office should be realized.

They feel that the present term of office is good, should a change be made it should be to a one year term of office instead of European Union's seven years. The Association does not decide on how the regulations regarding auditor's conflict of interest should be formulated, but points out that a possible change must not complicate for small companies to get access to both auditing- and accounting services. (www.bankforeningen.se)

3.6.4 The Swedish Association of Lawyers

The Swedish Association of Lawyers is regulated in the Code of Juridical Procedure and the Government prescribes the association's statutes. Only members of the association may use the title lawyer. The Association is often engaged as an advisory body and gives opinion on practically all proposals on central legislation. The Association principally supports the proposals in the memorandum. However, they think that some proposals are not sufficiently far-reaching and clear, especially not regarding the auditor's term of office and the agency's conflict of interest. They also think that the board of directors' duty of disclosure and support duty should be penalty sanctioned. This in order to clarify their responsibilities and to stress the importance of correct information submitted. Finally, the Association is of the opinion concerning disqualified agencies, that it should not only be in regard to an auditor working in the same auditing firm but also in regard to an auditor working within the same group of auditing firms, as defined in the Swedish Auditor's Act. (www.advokatsamfundet.se)

3.6.5 The Swedish Association of Trade and Industry

The Swedish Association of Trade and Industry represents the companies in Sweden. Its mission is to increase the understanding for the companies' reality and to act for the best possibilities for the Swedish companies to operate and grow. The Association represents 54,000 small, medium-sized and large companies. The organisation thinks that the quality of the combined assignments has to be investigated and do not think this type of assignments lack in quality. On the contrary, they think the quality can be better if the same auditing firm execute both the audit assignment and the accountancy assignment. This since available competence is used to obtain the best quality of accounting and financial follow-up. The Association also thinks that the memorandum underestimates the costs for the small companies. The organisation thinks it is obvious that the burden of expenditure for the small companies will be much larger if the proposal is approved, due to the fact that they have to engage different firms for the accountancy- and the auditing assignment. (www.svensktnaringsliv.se)

3.6.6 FAR

FAR is the professional institute for authorised public accountants, approved public accountants and other highly qualified professionals in the accountancy sector in Sweden. FAR includes most of Sweden's 2,400 authorised public accountants and plays a leading role in the development of professional standards, education and information for the audit profession in Sweden. FAR is of the opinion that the regulation of auditor's conflict of interest should be taken out of the Swedish Companies Act and be regulated by the Swedish Auditor's Act; if its content does not already cover this. The memorandum takes the view that the quality of combined assignments is of inferior quality compared to if different companies make the accounting and the auditing. FAR does not agree with this, they think that the auditor in combined assignments gets valuable information about valuation problems and risk of mistakes. They think that the memorandum is influenced by the accountancy scandals in the USA, which according

to FAR, lacks correspondence with the small and medium-sized Swedish companies that uses their auditors' competence as help with the accounting. If an auditor's own firm takes part in the accountancy assignment FAR feels that that is an incitement to do a careful audit so that undetected faults do not affect the own auditing firm or the own group of auditing firms. Since most small companies do not do their own accounting, FAR is of the opinion that the proposal of agency's conflict of interest would entail a radical change in the way these companies handle their accountancy, and especially of closing the books and of drawing up the annual financial statements. The memorandum states that the cost increase for accountancy and auditing in small companies will only be minor because the competition between actors providing accountancy services will increase. FAR are of the opinion that it is unclear why the competition will increase. The quality of the accounts would decrease seriously if small companies would engage unqualified bookkeeping agencies. Finally, FAR takes the view that in a combined assignment the basics from the bookkeeping assignment can be used in the audit, which leads to a substantial decrease in costs. (www.far.se)

3.6.7 The Swedish Association of Auditors

The Swedish Association of Auditors is Sweden's oldest organisation for qualified auditors with about 1,500 authorised public accountants and approved public accountants as members. Focus is on auditing and accounting in small and medium-sized companies and to support and develop its members through information, advice, insurances, resources and reference books. According to the Association, auditors have a very important function to make sure that the accounts in small and medium-sized companies works satisfactory and studies made prove a well-established positive connection between the work of qualified auditors and the company's quality of accounting. If the proposal of agency's conflict of interest is implemented the companies might engage independent bookkeeping agencies and because they are not quality assured there is a risk that the quality of the accounts will decrease in many small companies. The opinion is further that there are benefits with the combined assignments, since the knowledge from the accountancy assignment substantially reduces the risk for misdirected declarations in the auditor's report. The risk for errors in the accountancy would thereby increase if the proposal were implemented. Sweden is one of the countries within the European Union with the most far-reaching requirements for statutory audit in small companies. According to the Association, the proposal entails that small and medium-sized companies in Sweden have to adapt to the same regulations as listed companies in European Union's recommendation, and thinks it is necessary to analyse the proposals effect on these companies. By contrast to the memorandum the Association thinks that costs for the small companies will increase if the proposal of agency's conflict of interest is implemented, since two different companies have to be engaged. If, on top of that, the quality of the bookkeeping agency is inferior to that of the accounting firm, it might lead to increased costs for correcting the errors. All in all, the Association thinks it is difficult to assess the effects of these different variables, but estimates that the increase in costs will be at least 25 per cent and often double or even more. (www.revisorssamfundet.se)

3.7 Earlier Research

Discussions of a statutory audit or not, usually centre on the small owner-managed companies. The conventional focus when evaluating the need for a statutory audit is the economic size of the company usually measured in the company's turnover, net assets and/or number of employees. According to Tabone and Baldaccino (2003, pp. 387-398), a classification based on economic size is too limiting in scope. The ownership-management structure must also be considered, since this concept is more stable over time and less sensitive to economic pressure and other external influences. They raise the question whether a mandatory annual statutory audit requirement is justified in such circumstances, where the auditor is merely reporting information already known to the same person acting in a different role. English (1978, pp.64-65) expresses the same opinion: "What purpose does the annual audit serve where the shareholders are also the directors? To tell Mr and Mrs A (as shareholders) that they, Mr and Mrs A (as directors) have not misled or cheated them."

An argument against the statutory audit is also the cost. Page (1984, pp. 271-278) claims that the financial reporting is burdensome because it involves costs in preparing and auditing the information. Wills (1999, p.73) argues, with other alternatives to undertake a financial check by independent outsiders, the small company would be given freedom to match their financial process to their individual needs. English (1978, pp.64-65) argues that the time spent on the statutory audit could be utilised more fruitfully for credibility reviews and future cash flow planning. If it were abolished, there would still be "one-off audits" required by banks and purchasers, but English is certain that the Inland Revenue would not object. This since they accept accountants certificate without audit for unincorporated companies larger than many small companies.

Another argument against is whether the auditor is really being independent towards the owner-manager while performing the statutory audit. Small companies do not always possess the elaborate system of internal control to produce adequate evidence of all transactions, and therefore the auditor has to rely largely upon management assurances (Page, 1984, pp. 271-278). This raises the doubt as to the meaning of the term "true and fair" in the audit report (Keasey *et al.* 1988, pp. 323-333).

There are counter arguments to the above. According to Page (1984, pp.271-278), it is difficult to reject the argument that business contacts need some means of evaluating the stability of small companies. Keasey *et al* (1988, pp. 323-333) found in a recent survey, that irrespective of the size of a client company, to bankers the full statutory audited accounts were the most important source of documentary information when making lending decisions. Furthermore, the annual audit means that the "housekeeping" and "discipline" imposed on the staff and management is essential for the production of any reliable and consistent financial information for both internal and external users. Acher (1999, p.75) takes the same standpoint, and claims, "the audit brings assurance that a company's underlying accounting records are being properly kept." He fears that an abolishment might lead to a departure from accounting standards and an increase in company failures, through either inadequate financial advises or accounts misstatement.

Güntert (2000, pp.75-76) points at several benefits of an audit: it will give the director an increased confidence in the reported figures. It will also give credibility to the financial information, which should help in dealings with banks and other lenders, hire

purchase and leasing companies, suppliers and Government agencies, such as the tax authority. It gives the auditor a possibility to provide the owner-manager with quality advises in areas such as tax planning opportunities and improvement to the accounting process. He furthermore argues that the audit can play an important role in preventing frauds.

Several countries, within and outside the European Union, have changed the legislation for small companies concerning the statutory audit. In England, after 31 July 2000, companies with turnovers of under £1million will not need an audit for yearends and will at some point exempt companies with turnovers up to £4.8 millions (Güntert, 2000, pp.75-76). Canada has abolished it as well as New Zealand (English, 1978, pp.64-65). In the USA the companies have three different alternatives to the traditional auditing. These are audit, review and compilation. The differences are to what extent the auditor is being responsible for the reports. The audit gives the best insurance that the financial information is correct, a review gives a limited insurance, while the compilation only states that the annual report is free from obvious faults. (Bushong & Cornell, 1996, pp.45-57) It is usually a cost/benefit-decision what alternative they choose to use (Korpi-Nilsson and Lindstrij, 2003).

Those who oppose a review report claim that the external user cannot tell the difference between the review and the audit report, and therefore the audit expectation gap increases. In a study made in USA though, all different groups of users perceived that the review report gives less insurance than the audit report does (Gay *et al.* 1977, pp. 472-494).

4 Empirical Findings

In this chapter the information from the conducted interviews is compiled and begins with a description of the respondents and their background.

Interviews

The answers from the interviews are presented below. One of the interviewees is working at the Ministry of Justice, and the other are employed at the Swedish Tax Authority (STA) at different departments, and at different levels, within the authority. Two of the respondents have direct contact with qualified auditors' report that has been sent in; the other respondents express their opinion from an overall perspective. All respondents have not answered all questions, since the interview manuals were changed a little bit along the process of writing this thesis.

Jan Sandvall, STA, Gothenburg

For several years Jan Sandvall worked at Öhrlings PricewaterhouseCoopers, until he became an authorised public accountant. Since 1994 he works at STA, as a tax investigator and team leader at a department that conducts tax investigations focused on small companies. He also takes part in the internal education of future tax investigators and is responsible for two out of seven courses. This interview was conducted at STA's office in Gothenburg.

Tommy Andersson, STA, Örebro

Tommy Andersson has the position as a national expert of accountancy, with focus on the connection between accountancy and taxation. He is, among other things, working with reports and opinions on auditors to the Swedish Supervisory Board of Public Accountants. Andersson graduated 1972 at the School of Economics and Commercial Law at the University of Göteborg as a Master of Business Administration and has since then been working in different positions within STA. This interview was conducted by e-mail.

Lars Osihn, STA, Solna

Lars Osihn has been working at STA for twenty years. He is a Master of Business Administration with earlier experience from working at a bank and the Swedish State railways. At STA he is an official in charge of co-ordinating STA's auditing business. This interview was conducted by e-mail.

Magnus Wallin, STA, Mölndal

Magnus Wallin has the position as office manager at the STA office in Mölndal. He has worked within the STA since 1991 and has a legal training and has also worked for the Immigration Board. This interview was conducted at STA's office in Gothenburg.

Alf Hallgren, STA, Jönköping

Alf Hallgren is a Master of Business Administration and has been working at STA for twenty-five years. His position is as the manager of the auditing section. This interview was conducted by telephone.

What is your opinion of the memorandum "A few questions about audit" presented by the Ministry of Justice regarding the suggested tightening concerning the auditor's conflict of interest? (that is, the same agency can not produce the accountancy and then perform the auditing as well)

This memorandum is familiar to Osihn, who has a positive opinion on its proposals. He thinks that a tightening of the regulation will make the distinction of the conflict of interest more obvious. He is being supported by Hallgren, who says that since the auditor is supposed to be a guarantee for companies' external privies, it is important that he does not have a "close" relationship with the company-owner. He furthermore finds it difficult to know what is the most reasonable in this matter, but his opinion is that there ought to be clear distinctions in what an auditor can do or not do. The next respondent, Wallin, has not heard about the memorandum and finds it therefore difficult to comment. Spontaneously he does not consider that the auditor's conflict of interest is a large problem.

If this proposal is accepted, do you then think that the statutory audit can be removed for small companies? (Our definition of small companies: manager-owned with few employees)

On this question the respondents all share the same view. Small companies should not be exempted from the statutory audit if the proposal becomes accepted. Osihn and Wallin both say a firm no and Hallgren adds that the audit is too important, not only to STA, but also to other external privies, such as banks and suppliers.

What is the STA's view on the statutory audit? Arguments for and against? What is your personal opinion?

The statutory audit has a slightly different importance to the respondents. Sandvall's basic opinion is that the statutory audit and today's system works well. The counselling a business owner may require can STA understandably not give, he continues, since their role is one of reviewing. The auditor, on the other hand, performs the function of a sounding-board not only to the business owner but also to STA, who finds it easier to discuss possible questions with someone who is familiar with financial terms and the legislation in force. The business owner is often unaware of these matters and oriented towards the day to day running of the company. Without the auditor the company's accountancy might be of inferior quality, depending on how qualified personnel there are within the company. If a bookkeeping agency is engaged, the quality may also vary.

Andersson looks at this question from a different angle. He thinks that in the first place the statutory audit in small limited companies should be preserved due to the control aspect. The examination of a limited company made by STA starts with a judgement of the external auditor's statement concerning the company's accountancy and management. The statement affects to what extent and with what direction the examination of the company's declaration will be made. Osihn refers to what Sandvall mentioned and assumes that the statutory audit contributes to secure that the companies' accountancy shows a true and fair view. He too states that the audit is an important factor when planning a tax investigation. Osihn's personal opinion is that since the knowledge within the companies concerning the existing law usually is limited, with company-owners focusing on the production, the statutory audit secures law and order, both for the owner and other interested parties. He understands, however, that the cost can be burdensome to the companies and not experienced as motivated.

Wallin is of the opinion that the statutory audit puts pressure on the companies. It furthermore provides good information and a picture of inaccuracies. Inaccurate loans to owners are something that is detected in tax investigations of small companies. Wallin therefore claims that there is a value in the statutory audit for small companies. Hallgren claims that the statutory audit helps to avoid any suspicious thoughts about a company's bookkeeping and works as an assurance to the external parties. There are no arguments against it from STA's point of view, he says, but they are familiar with what some company-owners find is mainly an expense.

If the statutory audit is removed, do you see an increased risk for economic crime? (40 per cent of the notification of offence to the Swedish Authority for Economic Crime is made by STA).

Here, too, the respondents have different thoughts about the audit's significance. Sandvall says that a removal of the statutory audit for small companies does not automatically have to lead to any major consequences in form of economic crimes. The reason is that the auditors normally do not discover the inaccuracies the owner of the small company can make, which according to the respondent, usually is that the owner's private expenses are entered in the company's books or that revenues are not being entered in the books. These are the inaccuracies that STA discover in a tax investigation.

Both Andersson and Osihn are assuming that the risk increases. According to Osihn, a removal can have a negative affect on the quality of the accountancy, and therefore increase the risk for mistakes. Those mistakes can lead to an increased number of notifications and thereby increased economic crime.

Wallin, on the other hand, finds it uncertain whether a removal will have this affect. According to him, the audit does not prevent economic crime; what the auditor finds are mostly careless mistakes. Hallgren thinks it would be possible to some extent. It is though, he says, usually the same group of people who are using the existing system for economic crime and it is not certain, not even likely, that this group would increase with a change in the regulation.

The auditor has to submit a qualified report to STA. Are you of the opinion that the number of qualified reports is large in proportion to the total number?

According to Sandvall, qualified auditors' reports are not so common. A qualified auditors' report is not made out unless there are strong reasons. It is important for the auditor to keep a good relationship with the client. When a qualified auditors' report is submitted an analysis is made, STA runs over which auditor submitted it and the way he expresses himself. Even if the auditor expresses himself vaguely it is a signal to STA that there may be more inaccuracies than has been disclosed. If STA finds that the qualified auditors' report is "interesting", it can lead to a tax investigation, otherwise it is filed.

All respondents answer the same – no, the number of qualified auditors' reports is not large. Andersson does point out though, that the number has increased compared with the number being sent in when it was the company's responsibility to attach it to its income declaration. The number does not correspond with the number of faults found in tax investigations, Wallin comments.

How important is the information STA receives through the qualified auditors' reports?
The respondents all find the information in a qualified auditors' report important. Andersson even uses the words "very important". This is because the information controls to what extent a company's declaration will be examined. Osihn too finds it important and says the information is useful when a risk analysis is being made and that the value should not be minimized. According to Wallin, the information received is fairly important and mostly used as a method of selection whether to do a tax auditing or not. To Hallgren the information is very important. He says, "we usually learn about forbidden loans this way, ones that we would not find out about otherwise".

The information that you get from the auditor, how would you get it if the statutory audit were removed? Does STA have any further information sources?

According to Sandvall, it would be difficult for STA to obtain the information from any other source, but one way could be to review the companies' tax return and compare the ratios. Andersson also claims it would be difficult to replace the information. STA does not have any corresponding source of information, he says. Osihn means that in specific cases similar information can be obtained through audits performed by STA, but otherwise it is not likely that STA gets access to it. According to Wallin, a removal of the statutory audit would require an active search for information from STA. Hallgren confirms what the other respondents stated – STA would not get access to that information at all without a statutory audit.

In previous essays small business owners say, "STA find out what they want to regardless of annual financial statements and auditing". What do they mean?

"I do not know," is Sandvall's spontaneous comment. But there are some possibilities for STA to make investigations. An example is to check out if the owner has any income. If not, and that lasts for years it can be questioned, you have to live on something. A company being run at a loss for many years can be questioned – why is it still being operated. If the company is successful and the owner makes a good salary, it indicates that the accounts hold a good standard. Also, Osihn lists a number of different possibilities to find useful information about a company. He mentions public information from other authorities and institutions, annual reports, the Patent and Registration Office, the Tax database, the motor vehicle register and an analysis of the surrounding world, which means through the Internet, magazines and so on.

"The STA lives on people thinking we have more information than we actually have", Wallin answered with a laugh. The STA gets qualified auditors' reports and tax returns, which give information. STA can also sometimes request annual financial statements and accounting records from companies. The problem is though to find something interesting. STA can also decide to investigate entire lines of businesses.

Hallgren says it can be difficult to find information, since the facilitated systems of today do not contain much of it. He does mention that STA have their own internal systems and can for example do an analysis of a company's surplus value.

Would a removal of the statutory audit lead to an increased number of tax audits?

This is a question where the respondents have totally different opinions. Andersson says that an increase of performed tax audits probably would be the consequence. Osihn is of the opposite opinion; no more tax audits would take place. Wallin, who explains that

STA does not have resources to do that, is supporting this. He furthermore thinks that as a result there would be less security when STA is doing controls. Hallgren finds this difficult to answer. He thinks a removal could result in a marginal increase of tax audits, but he too refers to the limited resources.

Stefan Persson, in charge of Ernst & Young's National Auditing Department, suggests that the auditor place his signature on the income tax form, as an alternative to the auditor's report. Would such a declaration be worth more from STA's point of view?

The respondents do not seem to be impressed by this suggestion. According to Sandvall, it would be better than nothing, but he asks how the auditor would be able to signal that something is wrong. Andersson has "no" as an answer and nothing more, while Osihn, who is negative as well, declares that this would not be an alternative since it is the taxable person being responsible for the information in the tax form. Wallin considers that the tax return is limited and does not give any information about the accountancy. Besides, he says, the auditor's report is short and standardized if there is nothing wrong with the accountancy and do not provide the auditor with that much work. Hallgren thinks it might be possible as an alternative, but only if the generally accepted accounting principles and generally accepted auditing standards are maintained and that the auditor is still responsible to some extent.

Can STA see any additional alternatives to the statutory audit in small companies?

This question gives short answers. Sandvall has not considered the matter. The laws in force are what are important to him, because they run his daily work. But his reflection is that a change of them would mean an increased burden for STA through an increased need for control, since someone has to make sure that the companies' accounts are correct. It would probably mean a change of the number of employees – from the accounting firm to STA. Andersson and Osihn answer shortly no and Wallin has not thought about this. Hallgren does not know of any alternatives. He says he is not involved in this type of questions.

Do you think that the quality of the accounting will be inferior if the company compile it themselves instead of engaging external help like bookkeeping agencies or accounting firms? (Which some advisory bodies feared in their answers to the memorandum "A few questions about audit").

Here, the respondents are of similar opinions. Sandvall thinks that the quality might be inferior but that it depends on the competence within the company. He does think it is important to avoid agency's conflict of interest and puts a higher value to the memorandum's proposal concerning combined assignments than to the fears of some advisory bodies. He thinks that in the on-going discussion the auditors plead for their own case. "You can only sit on one chair at a time", he claims.

Osihn too thinks that the quality might be affected, and Andersson says that STA has for a long time has stated that the companies that do not have to submit themselves to a statutory audit, and where the company-owner is taking care of the accountancy, have an inferior quality. According to Wallin, this is often the result. He says, there are variations in quality of the accounts for small companies. They often keep their accountants in paper bags, which can be avoided if the statutory audit is being kept. People starting small companies are often not interested in administrative work, and in companies with few employees the owner's wife often handles the accounts. Wallin's thoughts are supported by Hallgren, who says that bookkeeping does not have the first

priority in small companies. He thinks it is possible that the accountancy lose in quality if the company-owner takes care of it instead of someone professional. Furthermore, he thinks the company-owners can easily fool themselves by not learning about accountancy. They can have a very good business concept, he says, but not realize what growth rate is realistic to the company and therefore make wrong decisions.

The major parts of the member-countries within the European Union have chosen to remove the statutory audit for small companies. What do you think is the basic reason for Sweden to keep it?

From STA's point of view it is mainly a question of reliability, Andersson answers. According to Osihn, there has not been any argument strong enough to remove a system that is being experienced as a working one. Tradition, justice and law and order are reasons why the system is being kept. Wallin does not have an opinion about this. But he thinks it can have something to do with different accountancy regulations in different countries. Hallgren does not have any opinion about this, but he thinks the main reason probably is because the limited company is a legal representative separated from the owner.

In, for example, the USA small companies can choose between three different auditing levels, with a different level of responsibility for the auditor and at a different cost for the company. Is the Swedish Tax Authority interested in other countries' legislation and are their developments being followed?

Sandvall says, that this is not a major concern for those working with small companies. Those working with large companies probably know more about this, which is a must since they work with international contacts. The respondent says he is working in today's reality, not in a reality that might come. According to Andersson, it is fairly given that STA is following what is happening in other countries.

Do you experience that there is an on-going discussion concerning the statutory audit in small companies, publicly as well as within STA?

Sandvall and Hallgren are aware of the articles in Balans, but do not experience that there is a discussion in this matter at STA. As far as Andersson is concerned, STA sees it as more or less obvious that the small limited companies should be included in the statutory audit as well. Osihn does not think there is a discussion concerning this issue at all. Wallin says that when there is a discussion it rather concerns the auditor's independence. Since the companies are engaging the auditor, STA never assume that he is being independent. There have been discoveries of auditors with hundreds of clients; in these cases the statutory audit is not a guarantee for quality.

Interview with Jacob Aspegren, the Ministry of Justice, May 17, 2004.

Aspegren has many years' experience from working in different courts of law. He has been working at the Ministry of Justice as an expert in issues of law for the past four years. He is also the author to the memorandum "A few questions about audit". This interview was conducted by telephone.

If the proposition from the memorandum "A few questions about audit" is accepted, is the Ministry of Justice then of the opinion that the statutory audit for small companies can be removed?

The Ministry, according to Aspegren, does not think of it as a necessary consequence, and when the Government last week proposed a change of the Swedish Companies Act

there were no changes concerning the small companies' situation mentioned. For the time being there is no work being done from the Ministry in this matter.

The major parts of the member-countries within the European Union have chosen to remove the statutory audit. What do you think is the basic reason for Sweden to keep it? Aspegren is aware of the fact that Sweden, together with Denmark, has among the strictest regulations in the Union. The reasons are several, and the basic one is that the audit is beneficial for the company, for example does it give the owner a better understanding of the economic side of the business, and it also gives the company a higher credibility towards banks and other lenders. Another factor is that the statutory audit is of great value to the Swedish Authority of Economic Crime, which probably would strongly oppose a removal. The Tax Authority too values that the companies' accountancy is in good order.

Does the Ministry follow the development in countries that have removed it?

No, that would be interesting first when a change of the regulation was being considered. There is, however, an on-going discussion within the Union concerning a stricter company legislation, which may make it difficult to retain the same legislation for small as for large companies in the future.

Would a removal of the statutory audit lead to an increased number of tax audits, and therefore allocate the costs from the companies to the society?

That is possible, Aspegren answers. But if the statutory audit is being removed, the Authorities probably will demand an alternative to replace it with. It would still be at the companies' expense.

The University of Uppsala says in its answer to the memorandum that an analysis of the consequences concerning the small companies' situation should be done. Is this something that will be done?

There is no analysis of the consequences being made right now. Although, Aspegren says that it is of importance to look closer to the problem. How this will be done is not yet decided.

Do you think the quality of the accountancy is being jeopardized if the company-owners do it themselves, instead of engaging external help, as some advisory bodies fear?

This does not have to be the result, according to Aspegren. One can look upon it from a different point of view. If the owner of the company becomes more involved with the accountancy, the knowledge of the cash flow and the company's efficiency might increase, and therefore lead to something positive. But the argument from the advisory bodies is important and must be considered when an analysis is being made.

The memorandum was presented in June 2003. What has happened with it since then?

Since the answers from the advisory bodies have been received nothing has happened. It is not likely that any results will be presented before the summer.

5 Research Findings and Interpretation

Based upon the theoretical framework the research findings will be analysed and interpreted, as well as connected with the earlier research found.

5.1 The Opinion on the Statutory Audit

When interviewing representatives from the STA it emerged that their opinion about the statutory audit requirement is that today's system works well. Sandvall, at the STA, points out that the auditor can help with counselling to a company in a way that the STA cannot. STA also experience that the auditor can be someone for the Authority to discuss with, who is familiar with the legislation in force. Some of the respondents mean that the knowledge within the companies concerning the existing laws is limited and therefore the audit can contribute to that the companies' accounts become correct and show a true and fair view. One respondent says that the most important reason for keeping the statutory audit requirement is the control aspect since the qualified auditors' report can be a first indication that something is wrong, and therefore form the base for a tax audit. The statutory audit gives good information about the companies' accounts and a picture of inaccuracies. There are no arguments against the statutory audit from STA's point of view, one respondent says, but he is aware that to some company-owners it is merely looked upon as a cost.

It is clear that STA thinks that the audit can have a positive effect on the companies' accounts. This is supported by Acher (1999, p.75) and Güntert (2000, pp.75-76), who both argue that the audit makes the accounts more reliable. English (1978, pp.64-65), on the other hand, thinks that the time spent on the audit can be used for something better and more worthwhile for the company. Page (1984, pp.271-278) means the statutory audit requirement mainly increases the cost for the companies. The earlier research shows that no matter what the opinions are, everybody is convinced that the audit plays an important role for the company in its contact with banks and different authorities, such as the Tax Authority.

In Balans, and in the answers to the memorandum, representatives from different organisations expresses their opinion. Gunvor Engström, COO of Företagarna, means that the small companies should not suffer because of the scandals in the large companies. According to her, there are two possibilities to mitigate the consequences for the small companies; either they are being exempted from the regulations of auditor's conflict of interest or they are being excluded from the statutory audit requirement. These are opinions shared by several of the advisory bodies, among others LGT and The Swedish Bank Association. Something pointed out by many of the advisory bodies is that the extended auditor's conflict of interest would lead to the need of engaging two different companies for accounting and auditing. This would, according to among others the Swedish Association of Trade and Industry, lead to increased costs, which affects smaller companies more than the large ones. Although, not all advisory bodies are paying attention to the small companies' situation. On the contrary, the Swedish Association of Lawyers' opinion is that the memorandum's proposals are not far reaching enough and that they have to be more clarifying regarding, for example, the auditor's term of office, the board of director's responsibility and the auditor's conflict of interest.

Most of the member-countries in the European Union have removed the statutory audit for small companies. Aspegren, in the Ministry of Justice, gives several reasons for why Sweden has kept it. One reason is that the audit is beneficial for the companies, since the owners get a picture of the economic situation in the company and gives credibility in the relationship with external parties. He also thinks that the Swedish Authority of Economic Crime and the Swedish Tax Authority would be apposed to a removal. Osihn, at the STA, means that tradition, justice and law and order are reasons for keeping the statutory audit. Other reasons are that it is a question of reliability and that Sweden might have different accountancy regulations than the other member-countries.

It is found that in earlier research some people are questioning the purpose with the statutory audit. Tabone and Baldaccino (2003, pp. 387-398) and English (1978, pp.64-65) express the opinion that it is questionable if the audit is necessary if it gives information to persons who already know about it but in a different role, for example, when the manager and the shareholder is the same person. According to Wills, (1999, p.73) it would be better if the companies could be able to match their financial process to their individual needs.

Stefan Persson from Ernest & Young points out that the small company need an accountant but not necessarily an audit. Brännström, Secretary General of FAR, is convinced that in the future the small companies' audits will be executed when sought-after. Another aspect mentioned by Engström is that the auditor is of great importance to the company as an adviser and if the statutory audit is removed the company can engage the auditor for more counselling then what is permitted by today's regulation.

The auditor has to submit a qualified auditors' report to STA. Since it is important for the auditor to keep a good relationship with the clients, it is not common that the auditors produce qualified auditors' reports. At STA it is not considered that the number submitted is large in comparison with the total number of audits. If a qualified auditors' report is submitted it indicates that there are more inaccuracies to be found. The reports are sometimes used as a background for decisions about tax investigations. According to STA, a removal of the statutory audit would lead to a loss of the information obtained from the qualified auditors' report. The information is used as a method of selection when deciding about tax investigations and auditing statements. Getting this information would entail an active search from the STA, for example through tax investigations, which would lead to increased costs and less security when doing controls. The number of tax investigations would probably increase. Aspegren says that if the statutory audit is removed the Authorities will find an alternative to replace it, still at the companies' expense. Some of the respondents claim that without the annual financial statements and auditing it would be more difficult to get any information about companies. STA does however, have other possibilities to collect information. Some of them are public information from other authorities and institutions, annual reports, the Patent and Registration Office, the tax database and the motor vehicle register can be used. If someone is running a company at a loss for many years it can be questioned and attract the Tax Authority's interest. According to Wallin, the STA lives on people thinking they have more information then they actually have.

When asking the question whether a removal of the statutory audit would lead to an increased risk for economic crime a difference in the respondents' opinions were noticed. Osihn says "yes", because the quality of the accountancy can be inferior and

therefore increase the risk for mistakes. Wallin and Sandvall think that it is uncertain what would happen. According to Sandvall, the auditor normally does not discover the inaccuracies that the owner of a small company can make. These can later be discovered at a tax audit and usually consists of company-owners private expenses showing up in the company accountancy or revenues that not are being accounted for. But another respondent says that the most important information obtained is the one concerning loans made within the company. Hallgren says that it is usually the same group of people who are dealing with economic crime, and that this group does not necessarily has to increase due to a change of the regulations.

The audit's effect on economic crime is something that has been discussed earlier and according to Gntert (2000, pp.75-76), it can play an important role in preventing frauds.

When asking if the respondents have noticed that there is an on-going debate about the statutory audit in small companies they answer both "yes" and "no". Most of the respondents, but not all, are aware of the articles being presented in Balans and realize there is a discussion, but they do not have one within the Authority. This since STA sees it as obvious that the small limited companies also should have statutory audit and as mentioned in the beginning they think that the system works well. The question about the auditor's independence is, on the other hand, being discussed from time to time, since the company is paying the auditor, whose independence can therefore be questioned. One of the respondents thinks the auditor sometimes is being too close to the company and stresses the importance of a distinct regulation. This is a far more important matter to STA than the question about the statutory audit.

5.2 A Quality Matter?

An argument used in the debate is the quality of a company's accountancy. Both those who support the statutory audit and those who oppose it are using this argument. From STA's point of view the audit can imply the only contact between the owner-manager and someone qualified in the accountancy field. Therefore the statutory audit becomes a quality matter. The quality can, however, vary a great deal, the respondents from STA say. It depends on what qualifications the management or the employee's have or what bookkeeping agency is being engaged. In a worse scenario the accountancy is being kept in a paper bag, since administration do not have the first priority, but it does not have to be that bad at all. One respondent though, answers that STA stated a long time ago that companies not affected by the statutory audit requirement have accountancies of inferior quality. A couple of the respondents think it is more important to assure the auditor's independence than worry about how a possible change of the audit legislation would affect the quality of companies' accountancy.

There is some earlier research supporting the argument that the audit assures the accountancy quality. Keasey *et al.* (1988, pp. 323-333) found that with a statutory audit requirement the staff and management becomes more disciplined in producing reliable and consistent financial information. Acher (1999, p.75) too claims that the audit brings assurance that the accountancy is being properly kept. He fears that an abolishment might lead to an inferior quality and a departure from accounting standards. According to Gntert (2000, pp.75-76), the audit can be important from a quality-perspective to the company-owner too, since it gives reliability to the reported figures.

As mentioned above, some participants in the debate are using quality as a reason to remove the statutory audit. Bodin, COO of LGT, fears that with a ban of the combined assignment, owner-managers will take care of the bookkeeping themselves to lower their costs, which might lead to an inferior quality of the accountancy. Brännström thinks a tightening of the regulation would have a negative affect on both the annual account and the annual financial statement. Företagarna's viewpoint is that the combined assignment means a good quality; if the same agency performs both bookkeeping and auditing it is easier with communication, which means less need for audit tests. A ban would lead to higher cost, Engström claims, and therefore small companies should be exempted from such regulation and suggests furthermore that the statutory audit should be made voluntary for small and medium-sized companies. The Swedish Association of Auditors also sees a risk with banning the combined assignment; companies might engage independent bookkeeping agencies without quality assurances and this might lead to an inferior quality of the accountancy.

5.3 Are there any Alternatives?

As mentioned before, Sweden is one of the countries in the European Union with the strictest regulation concerning the statutory audit. It is up to each country to decide about their own set of laws for small companies. There is an international as well as a European trend in harmonizing accountancy standards and regulations, which makes it interesting to find out if there will be a harmonizing even in this matter – not least since Sweden has a strong connection between taxation and accountancy.

It has shown that several countries have facilitated for their small companies either by exempting them from the statutory audit or as in the USA where they have been given different choices (Bushong & Cornell, 1996, pp.45-57). They consist of three alternatives: the audit, the review and the compilation. The difference is to what extent the auditor is responsible for the reports. In Sweden some of those who argue against the statutory audit advocate some kind of alternative for the Swedish companies as well. Persson is certain that companies even in the future will have to submit themselves to some kind of audit. This since the banks will require it before lending any money to the companies. Also Företagarna thinks that banks and lenders will continue to demand an impartial review of the companies' accounts, but thinks the statutory audit should be voluntary and performed only when sought-after. According to Brännström, the statutory audit is being protected by the state in order to guard the fiscal charges and to prevent economic crime. He does expect a change in the future though, with differences in the regulation between small and large companies, and he also thinks that audits in the small companies will be sought-after when needed. This expectation is to a certain extent supported by Aspegren, who says that there is a discussion about a change of the regulations concerning limited companies in the European Union, which might make it impossible to keep the same set of laws for companies of different size.

According to one respondent, the Tax Authority is looking at the development in other countries where the statutory audit has been removed, but as far as Aspegren is concerned, the Ministry of Justice will not look at this until a change of the legislation becomes of an immediate interest.

Persson has presented an idea about an alternative to the statutory audit. Instead of the present form the auditor could put his signature on the companies income tax form. This suggestion has been presented to the respondents from the Tax Authority, as well as the circumstances in other countries, in order to find out the respondents' point of view about these alternatives. Their reactions to Persson's suggestion were more or less similar. They do not appreciate this as a suitable alternative. According to one of the respondents, it would be better than nothing, but he does not understand how the auditor then would be able to signal when something in the company is wrong. Another respondent uses the argument that the tax income form does not give any information about the accountancy. Yet another respondent says that this is not an alternative since the taxable person is being responsible for the information in the tax form.

On the question if the Tax Authority sees any alternatives to the statutory audit at all they all answer in unison: "no!" This is nothing they been thinking about. One of the respondents says that he is working after the present regulation, since it is running his daily work. When reflecting over the question he continues that a change of the regulation would probably lead to an increased burden for the Authority through an increased need of control.

6 Conclusions

This final chapter summarizes the principle findings of the analysis, which will enable the authors to answer the research problem defined in the introduction chapter. Lastly, suggestions for further research will be made.

6.1 The Interpretation of the Study

The authors started this study with curiosity about what result it would show. From earlier discussions it was found that most people are convinced that the Tax Authority is reluctant to a removal of the statutory audit, and therefore it would be interesting to find out whether this is correct or simply based upon peoples' prejudice. It is understandable that five interviews with personnel from the STA are too few to draw any general conclusions from. But, the five interviewees are spread over the country, and working in different positions and they all give concordant answers to most of the questions, which can be interpreted as if they are representing the attitude within the STA.

6.1.1 *What is the Tax Authority's Opinion about a Possible Removal of the Statutory Audit for Small Companies?*

From the respondent's opinion about the statutory audit it is obvious that they all think it serves a useful purpose. Their arguments in favour of the audit were far more than those against, if any at all. It is obvious that the information STA receives through the qualified auditors' report is important and that it would be difficult to obtain it otherwise. The authors also learnt that STA to some extent finds it easier to rely on the company's accountancy when it has been audited. The external auditor's financial statement is also interesting when STA is performing a tax audit. This, according to the authors, shows how much the external auditor is being valued by STA. Furthermore, they mean that the knowledge about the laws in force are limited within the small companies, and therefore the respondents feel that the statutory audit works as a guarantee that all companies follow the same rules and have accounts that follow the same accounting standards. Qualified auditors' reports that come to the STA are sometimes used as a background for decisions about tax investigations. If many qualified auditors' reports come from the same line of business, it can give STA indications that it could be interesting to investigate that line of business. Suspicions about inaccuracies in the account leads to controls being made, and then STA often discovers inaccuracies not detected or not reported by the auditor. If that information source were lost the accuracy in tax investigations would be inferior, which according to the respondents, would lead to higher costs for STA. The control aspect makes the respondents mean that qualified auditors' reports are important for STA. The authors find this a bit contradictory, since they at the same time say that the auditor does not discover all inaccuracies, which STA discovers in tax investigations.

On the question of whether there is an on-going debate about the statutory audit, publicly or within the STA, the respondents gave either vague answers or a firm "no". Some are aware of the articles in Balans, but do not seem to think this is a big issue. If there is an internal discussion it is mainly concerning the auditor's independence and not whether the audit should be removed or not. To the respondents it is obvious that the statutory audit shall remain. This is a bit strange since some of the respondents have confirmed that they read the journal Balans, and in several numbers in recent years the question of the statutory audit has been discussed. But most of the interviewees made it

clear that they work in today's reality, and do not concern themselves with what might come.

When the information about the opinions on the statutory audit was gathered, it was found that the privies that are heard in today's debate are basically the same that took part in debate in the 1990s. The authors do realize that some of them are representing companies who, even when they express their concern regarding the small company's situation, might have an interest of their own to protect.

To summarize the answer:

The respondents do not see any reason to remove the statutory audit for small companies. To them it is important, both as a control-instrument as well as a source of information.

6.1.2 Does the Tax Authority See the Statutory Audit as a Guarantee for Good Quality in the Accountancy?

The quality of a company's accountancy is being discussed by some of the advisory bodies and participants in the debate. It is being argued that the quality might be inferior if the regulation concerning the auditor's and agency's conflict of interest is being tightened. One of the purposes with this study has therefore been to find out whether STA sees this as a risk too, and if this is something that has any importance to them.

Here, the authors found that the respondents have pretty much the same opinion. The quality might be affected by a change. From one respondent it was learnt that STA has noticed accountancies of inferior quality in companies not obligated to submit themselves to a statutory audit. Some do point out that it does depend on the competence within the companies. The interviewees depicted the situation from a worse scenario with the bookkeeping kept in paper bags, to small companies where the husband is working with the production and the wife, with little knowledge of accountancy-regulation, keeps the books, to the company that is engaging professional help.

When discussing the quality it was found that one of the respondents finds the question concerning the auditor's independence more important to discuss than to what extent a possible removal of the audit would affect the accountancy quality. His major concern is that there are clear limits between the company and the auditor, since the auditor is supposed to be a guarantee to the external privies that everything is correct. All respondents do stress, though, that the quality in the bookkeeping is significant and find the auditor's financial statement somewhat important in this matter. But to call the statutory audit a guarantee they think is a bit too far-reaching. STA thinks it is significant that companies follow the generally accepted accountancy principles. The authors find this understandable, since the accounts form the taxation base and furthermore think that when the auditor assures that the accounts are following the legislation in force, it becomes possible for STA to focus on issues more important to them.

Again, it is appropriate to mention that some of those who participate in the debate, and fear that the quality will be affected by a stricter regulation of the combined assignment are discussing something that will affect their own situation, and therefore can be questioned. Besides, it has shown that in earlier discussions as well as in earlier

research, the question about the accountancy quality and the audits affect on it has been used as an argument from both sides. One argument that makes sense is that without the statutory audit it would be possible for the company-owner to benefit from the auditor's knowledge in the accountancy field, in other words use him for more counselling. To STA though, the major concern is that the audit makes sure that the accountancy shows a true and fair view.

The short answer to this question is:

Yes, even though the word guarantee is too strong, the Swedish Tax Authority does look upon the auditor and the audit as important to the quality, since not every company has the knowledge and competence to uphold the accounting principles.

6.1.3 Does the Tax Authority See any Alternatives to the Statutory Audit?

The authors' interpretation of the respondents' answers to this question is that this is an issue that is not being discussed at all. This may be because the wrong people having been asked, that is, people who are not on the level where these kinds of questions are being handled, or because the question lack relevance to STA. The answers received on this question were mainly a short "no", or a vague "this is nothing I have thought about". It seems to the authors that there is no interest for this question. When the suggestion from Persson was presented, about the auditor placing his signature on the company's income tax form, the respondents were obviously negative. It became clear that they want the audit to make sure that the generally accepted accounting standard is maintained and that the auditor is responsible to some extent. As one of the respondents said; "Since the taxable person is responsible for the information in the tax form this would not be an alternative".

It has been found that within the European Union, on account of the Fourth Directive, it is voluntary, whether to have a statutory audit for the small companies or not. From this the authors understand that the Union has been weighing the pros and cons and decided that the advantages with facilitating for this business-group are larger than the problems that might show up with a removal of the same. The authors think the reason why Sweden has so far showed little interest in any possible alternatives can be traced to the strong connection between the taxation and accountancy-regulation. Another reason is the attitude to the statutory audit during the last century. Over time, the arguments for the audit have been rather similar and when changes have been made it has always led to a tightening of the legislation. Frequent arguments have been to prevent economic crime and to protect the external privies' interests.

Lastly, the authors think an approval of the memorandum's proposals can lead to a change of the regulation for small companies. The work within the European Union to harmonize the regulations will make it difficult for Sweden to preserve a legislation that is stricter than the other member-countries. This thought is supported by Aspegren's comment that "the changes now taking place within the Union regarding limited companies will make it difficult for Sweden to keep the same regulations for both small and large companies".

The answer to the last question can be summarized like this:

No, the Swedish Tax Authority does not see any alternatives to the statutory audit, and do not see any reason to give the issue any consideration. The attitude can simply be expressed: why change something that works?

6.2 Prejudiced or Not?

So, what did the authors find out – are people in general being prejudiced towards the Tax Authority for no reason? For some people the Authority is like a huge control machine, with information about everything and everyone. The control aspect should then be the reason to why they would be reluctant towards a removal of the statutory audit. This might be a bit exaggerated. It is clear though, that STA do have access to a lot of information and it was found, while conducting the interviews, that the respondents also to this question gave somewhat vague answers. But then again, maybe it is as one of the respondents said; "STA lives on people thinking we have more information than we actually have".

6.3 Suggestions for Further Studies

In some countries the statutory audit requirement for small companies has been removed, though with different national limits based upon the companies' economic size. Countries, which has chosen to facilitate for the small companies are among others the USA, Great Britain, Ireland and Germany. To study these countries' alternatives to the audit, and the development since the removal, would be interesting.

Another interesting thing to study would be how the Tax Authorities in those countries get access to the information previously received through the audit, and how much they rely on the companies' accountancy.

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Appendix A

Interview Manual 1

- What is your position at the Tax Authority?
- For how long have you been working at the Tax Authority?
- What education and experience from other employment do you have?
- What is the Tax Authority's view on the statutory audit? Arguments for and against?
- If the statutory audit is removed, do you see an increased risk for economic crimes? (40 per cent of the notification of offence to the Swedish Authority for Economic Crime is made by STA).
- The auditor has to submit qualified auditors' report to STA. Are you of the opinion that the number of qualified reports is large in proportion to the total number?
- How important is the information STA receives through the qualified auditors' reports?
- The information that you get from the auditor, how would you get it if the statutory audit were removed? Does STA have any further information sources?
- In previous essays small business owners say, "STA find out what they want to regardless of annual financial statements and auditing". What do they mean?
- Stefan Persson, in charge of Ernst & Young's National Auditing Department, suggests that the auditor place his signature on the income tax form, as an alternative to the auditor's report. Would such a declaration be worth more from STA's point of view?
- Can STA see any additional alternatives to the statutory audit in small companies?
- Do you think that the quality of the accounting will be inferior if the company compile it themselves instead of engaging external help like bookkeeping agencies or accounting firms? (Which some advisory bodies feared in their answers to the memorandum "A few questions about audit").
- In, for example, the USA small companies can choose between three different auditing levels, with a different level of responsibility for the auditor and at a different cost for the company. Is the Swedish Tax Authority interested in other countries' legislation and are their developments being followed?

Appendix B

Interview Manual 2

- What is your position at the Tax Authority?
 - For how long have you been working at the Tax Authority?
 - What education and experience from other employment do you have?
 - What is the Tax Authority's view on the statutory audit in small companies? Arguments for and against?
 - If the statutory audit is removed, do you see an increased risk for economic crimes? (40 per cent of the notification of offence to the Swedish Authority for Economic Crime is made by STA).
 - The auditor has to submit a qualified report to STA. Are you of the opinion that the number of qualified reports is large in proportion to the total number?
 - How important is the information STA receives through the qualified auditors' reports?
 - The information that you get from the auditor, how would you get it if the statutory audit were removed? Does STA have any further information sources?
 - Would a removal of the statutory audit lead to an increased number of tax audits?
 - Stefan Persson, in charge of Ernst & Young's National Auditing Department, suggests that the auditor places his signature on the income tax form, as an alternative to the auditor's report. Would such a declaration be worth more from STA's point of view?
 - Can STA see any additional alternatives to the statutory audit in small companies?
 - Do you think that the quality of the accounting will be inferior if the company compile it themselves instead of engaging external help like bookkeeping agencies or accounting firms? (Which some advisory bodies feared in their answers to the memorandum "A few questions about audit").
 - The major parts of the member-countries within the European Union have chosen to remove the statutory audit for small companies. What do you think is the basic reason for Sweden to keep it?
 - In, for example, the USA small companies can choose between three different auditing levels, with a different level of responsibility for the auditor and at a different cost for the company. Is the Swedish Tax Authority interested in other countries' legislation and are their developments being followed?
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- Do you experience that there is an on-going discussion concerning the statutory audit in small companies, publicly as well as within STA?

Appendix C

Interview Manual 3

- What is your position at the Tax Authority?
- For how long have you been working at the Tax Authority?
- What education and experience from other employment do you have?
- What is your opinion about the proposal in the memorandum “A few questions about audit” concerning an extension of the regulation regarding the auditor’s conflict of interest? (that is, the same agency shall not be able to both produce the bookkeeping and audit the same)
- If this proposal is being accepted, do you then think that the statutory audit can be removed for small companies? (Our definition of small companies: manager-owned with few employees)
- What is the STA’s view on the statutory audit? Arguments for and against? What is your personal opinion?
- If the statutory audit is removed, do you see an increased risk for economic crimes? (40 per cent of the notification of offence to the Swedish Authority for Economic Crime is made by STA).
- The auditor has to submit a qualified report to STA. Are you of the opinion that the number of qualified reports is large in proportion to the total number?
- How important is the information STA receives through the qualified auditors’ reports?
- The information that you get from the auditor, how would you get it if the statutory audit were removed? Does STA have any further information sources?
- In previous essays small business owners say, “STA find out what they want to regardless of annual financial statements and auditing”. What further information sources does STA have?
- Would a removal of the statutory audit lead to an increased number of tax audits?
- Stefan Persson, in charge of Ernst & Young’s National Auditing Department, suggests that the auditor places his signature on the income tax form, as an alternative to the auditor’s report. Would such a declaration be worth more from STA’s point of view?
- Can STA see any additional alternatives to the statutory audit in small companies?

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- Do you think that the quality of the accounting will be inferior if the company compile it themselves instead of engaging external help like bookkeeping agencies or accounting firms? (Which some advisory bodies feared in their answers to the memorandum "A few questions about audit").
 - The major parts of the member-countries within the European Union have chosen to remove the statutory audit for small companies. What do you think is the basic reason for Sweden to keep it?
 - Do you experience that there is an on-going discussion concerning the statutory audit in small companies, publicly as well as within STA?

Appendix D

Interview Manual 4

- What is your position at the Ministry of Justice?
- For how long have you been working at the Ministry of Justice?
- What education and experience from other employment do you have?
- If the proposition from the memorandum "A few questions about audit" is being accepted, is the Ministry of Justice then of the opinion that the statutory audit for small companies can be removed?
- The major parts of the member-countries within the European Union have chosen to remove the statutory audit. What do you think is the basic reason for Sweden to keep it?
- Does the Ministry follow the development in countries that have removed it?
- Would a removal of the statutory audit lead to an increased number of tax audits, and therefore allocate the costs from the companies to the society?
- The University of Uppsala says in its answer to the memorandum that an analysis of the consequences concerning the small companies' situation should be done. Is this something that will be done?
- Do you think the quality of the accountancy is being jeopardized if the company-owners do it themselves, instead of engaging external help, as some advisory bodies fear?
- The memorandum was presented in June 2003. What has happened with it since then?