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Article

Factors Influencing the Audit Quality of the Municipalities: Perceptions of Accountants and Internal Auditors

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ABSTRACT - The study aims to analyze the Audit Quality (AQ) factors that were perceived to be necessary by the accountants and internal auditors in municipalities of Palestine. A survey of 309 accountants and internal auditors from 155 Palestinian municipalities was conducted. The questionnaire data was statistically analyzed using Smart PLS3 software. The study discovered that auditor ethics, independence, and competence were the most significant elements in determining AQ. Meanwhile, Internal Auditing (IA), Accounting Basis (AB), and the Laws and Regulations (LR) have a moderate effect. However, the least crucial factors were Audit Fees (AF) and Audit Firm Size (AFS). The study is limited by the survey questionnaire method's general limitations and the perceptions of accountants and internal auditors. It offers evidence on AQ from Palestine, helps the audit firms distinguish their marketing and service delivery strategies, and understands the AQ aspects sought by those clients. Moreover, the study provides the municipal councils and the regulators of the municipalities with greater knowledge on how to select the best auditors and maintain internal control measures, notably IA and the use of the accrual basis in accounting procedures. Since the findings are generally consistent with previous studies, more emphasis can be placed on the effectiveness of municipal internal control.

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INTRODUCTION

High Audit Quality (AQ) enhances public trust in government accountants' audited financial reports (DeFond & Zhang, 2014) since auditing in Public Sector Organizations (PSOs) always adds value to financial reports. Furthermore, auditors are recognised as critical participants in producing trustworthy and reliable financial statements (Ismail et al., 2019). Watson (2019) observed that the concept of AQ differs between the public and private sectors and is dependent on the audit's objectives. Since AQ is a characteristic that is sensed rather than observed, it is possible to pinpoint circumstances in which it is at risk (Knechel et al., 2013). Researchers gain access to new and improved data on AQ drivers, whether from audit firms, clients, regulators, or other sources, in order to advance their understanding of AQ (Knechel et al., 2013). Prior research identified audit firm values, sector expertise, audit partner rotation, audit committee oversight, adherence to auditing standards, client awareness, the auditor's financial independence, and audit inspection as factors influencing AQ perception (Beattie et al., 2012).

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According to the AQ literature, this study examines specific factors of the AQ related to the auditors' characteristics category (ethics, independence, and competence) and audit firm attributes category (Audit Firm Size (AFS) and Audit Fees (AF)). It also investigates the effectiveness of municipal internal control (Internal Auditing (IA), Accounting Basis (AB), and the applicable Laws and Regulations (LR)). Since the AQ is unobservable (Francis, 2004; Knechel et al., 2013), this study focuses on the AQ perception of accountants and internal auditors, who have first-hand knowledge of the financial statements being audited and regularly communicate with external auditors. Meanwhile, Carcello et al. (1992) examined the perspectives of auditors, users, and preparers (accountants) on AQ. The authors discovered that, in an increasingly competitive environment, understanding both perspectives of users and preparers regarding AQ becomes crucial. Additionally, auditing firms may build their audit effectiveness on these perspectives (Iskandar et al., 2010). However, there is minimal research on AQ in PSOs despite there being a lot of it conducted in the private sector (Harris et al., 2019), and no framework is capable of interpreting all PSOs' AQ issues (Cohen et al., 2013; Copley, 1991; Greenwood & Zhan, 2019; McLelland & Giroux, 2000).

This study seeks to fill a gap in the literature by investigating the factors of AQ in Palestinian municipalities through the eyes of their accountants and internal auditors. This is to identify the most critical factors that have more significant effects on the AQ in the municipalities and the factors of the AQ that are associated with the AQ provided by the external auditors in the municipalities of Palestine. The study will address two related research questions using Carcello et al. (1992), Behn et al. (1997), Boon et al. (2008), Butcher et al. (2013), Sawalqa (2014), Ghebremichael (2018), and Lai and Pham's (2020) perceptions of AQ approach. First, what are the AQ factors that Palestinian municipalities' accountants and internal auditors are worth highly when assessing the quality of audit rendered by the external auditor? Second, what are the aspects that indicate that the external audit process is being conducted with high quality according to accountants' and internal auditors' perceptions? It is crucial for regulators, audit firms, and clients to understand the AQ factors that clients appreciate when assessing the quality of audits in municipalities. At the same time, regulators can create auditing standards to enhance both actual and perceived AQ using this information to determine what is likely to make an audit service of higher quality. These details can help audit firms better distinguish themselves in terms of service quality, enhance the level of quality of their own audits, and increase client satisfaction (Carcello et al., 1992; Behn et al., 1997).

The necessity of investigating AQ in Palestinian municipalities stems from the importance of achieving a high-quality auditing procedure in Palestinian organizations. The municipalities sector is one of Palestine's most important sectors. It is critical to the Palestinian citizens and plays a vital role in providing basic services as the PSOs in any country, offering fundamental services like infrastructure (roads, bridges, public buildings, parking), energy, water, sewage treatment, health, and other services (Besley & Ghatak 2017; Avis et al., 2018). Notably, most of these critical services are provided in Palestine by the local government units (UNDP, 2009). As a result, one may argue that auditors are essential in the municipalities; therefore, this study investigates the AQ for many reasons. This includes (1) the Ministry of Local Government (MOLG) encourages all municipalities to audit their financial statements annually in order to receive extra government contributions (Rustum, 2018); (2) the stakeholders of municipalities interested in the credibility and transparency of the financial reports, hence the importance of external audit (Yamamoto & Kim, 2019); (3) the management of the municipality is interested in the positive public's perception of the credibility of the financial reports. Accordingly, a reliable independent auditor who offers top-notch audit services is required (Hay & Cordery 2018); and (4) the citizens who pay taxes view such audits as crucial to know where their money is going and whether it is being used in an efficient, effective, and economical manner (Bojkovska et al., 2019).

The procurement of external audit services by the municipalities in Palestine is governed by the General Procurement Law, and the MOLG was issued in 2016 as a guideline on how the

municipalities can prepare price quotations to hire an external auditor. In addition, the auditor must be recorded in the Palestinian Association of Certified Public Accountants (PACPA), which adopts the International Standards of Auditing (ISA) in its bylaw (Hassan, 2016). In addition, MOLG required the municipalities to establish internal audits in their organization structures and convert their accounting practices to accrual instead of cash. However, the MOLG Annual Performance Report for 2020 revealed that 30 municipalities out of 130 in the West Bank used the accrual basis (MOLG, 2020). These interventions by MOLG may influence the AQ inaccordance to the public interest theory, which can interpret and provide a foundation for the AQ model in the municipalities suggested by this study.

LITERATURE REVIEW

Audit Quality and Measures

The auditor assures the audited financial accounts. However, the level of assurance is indestructible, making AQ measurement a cloudy and complex subject (Chadegani, 2011; Dickins et al., 2018; Knechel et al., 2013). Alareeni (2019) claimed that prior research had covered numerous aspects and characteristics of the audit firm that affect AQ in various ways. However, researchers still have no agreement on which measures are best, and there is no proper evaluation guidance (DeFond & Zhang 2014). According to Kusumawati and Syamsuddin (2018), the behavior of auditors during audit engagement determines how well the AQ is measured. Therefore, the tools to measure AQ are still unclearly defined, and there is no agreement among scholars about the effectiveness of the proxies of AQ, seeing that they have mixed effects on the correlations between audit criteria and AQ (Alareeni 2019; DeFond and Zhang 2014).

Meanwhile, Hussein and Hanefah (2013) reported that researchers have taken numerous direct and indirect approaches to measuring AQ. They added that the direct approach is related to the likelihood of discovering and reporting misstatements or breaches in the accounting system under audit, which will be reflected in the contents of the audit process, including the errors of the auditor. Conversely, the indirect approach is concerned with using proxies of AQ (Ashfaq et al., 2023) or assessing AQ by examining the factors perceived to affect AQ.

Perception of Audit Quality Factors

Some prior studies used the perception of one group of the stakeholders of the audit process to determine the AQ factors. Nevertheless, others used more than one group. For example, Carcello et al. (1992) surveyed 245 audit partners, 264 controllers (financial statement preparers), and 120 investors and creditors (financial statement users) to investigate the factors associated with AQ as perceived by auditors, preparers, and users.

In the public and private sectors, many researchers have studied the perception of accountants and internal auditors on AQ, e.g., Behn et al. (1997), Pandit (1999), Boon et al. (2008), and Iskandar et al. (2010). All these studies adopted the 12 attributes of AQ, which they determined by Carcello et al. (1992) after making some modifications to these attributes. For example, Boon et al. (2008) inspected the AQ attributes perceived to be relevant in Compulsory Audit Tendering (CAT) in local councils in New South Wales (NSW). At the same time, Iskandar et al. (2010), adopting Behn et al.'s (1997) instrument, examined the influence of AQ factors and client contentment on audit performance at the audit firm and audit team levels.

Integrated Framework of Audit Quality in Prior Research

The most important frameworks of AQ in previous studies stated that the factor of AQ can be classified by outputs of audit engagement, audit processes, and inputs of audit engagement (Chadegani 2011). DeFond and Zhang (2014) offered a different paradigm for comprehending and assessing the AQ proxies widely employed in the literature. This framework consists of three elements: AQ demand, AQ supply, and the intervention of the regulators in both demand and

supply of AQ. The Financial Reporting Council (FRC) in the UK developed the first official framework for AQ in 2008 in the U.K, which includes five factors that affect AQ are listed in this framework: (1) the culture of an audit firm; (2) the expertise and character of audit partners and personnel; (3) the efficiency of the audit process; (4) the accuracy and value of audit reporting; and (5) elements impacting AQ that are not under the control of auditors (Knechel et al., 2013). Other formal AQ frameworks have been established by the Australian Treasury (Commonwealth of Australia, 2010) and the International Auditing and Assurance Standards Board (IAASB, 2011). The frameworks suggest that the auditor's attributes, the auditor's report, and contextual circumstances (LR) all influence AQ (Knechel et al., 2013).

Measuring AQ in the public sector is challenging for academicians and practitioners since no single model can explain and define the factors of AQ. At the same time, the auditor must comply with the Generally Accepted Auditing Standards (GAAS) and relevant ethics and code of professional conduct in the public sector (Ismail et al., 2019).

Determinants of Audit Quality

The study aims to improve understanding of the nature of AQ and its determinants in municipalities by evaluating selected factors such as ethics, independence, competence, AF, AFS, internal audit, AB, and the applicable LR.

Auditor Ethics

The auditor's commitment to adhering to ethics will lead to higher AQ (AlBeksh, 2016). Furthermore, Haeridistia and Fadjarenie (2019) confirmed that AQ is influenced by professional ethics. Blay et al. (2019) defined two fundamental principles in the auditing profession: responsibility and honesty, and they utilised both to assess an individual's potential for moral reasoning in auditing. Notably, trust in the audited financial statements can be improved when the auditor concentrates on their core values of competence, integrity, objectivity, independence, and AQ (Rezaee et al., 2016). According to Knechel et al. (2013) and Parsimin et al. (2023), ethical and moral thinking are personal traits of auditors that, when combined with professional skepticism, lead to higher AQ. Moreover, Chang et al. (2007) discovered that professionalism and ethical behavior have a substantial effect on public confidence in the accounting and auditing industry. Based on the preceding discussion, the following hypothesis was formed:

H_1a: There is a positive relationship between auditor ethics and Audit Quality (AQ).

Auditor Independence

The auditor is independent when his mental attitude is free from any limitations and constraints, and his decisions are not under the control of or dependent on others. He considers only the facts and performs his duties objectively and honestly (Kusumawati & Syamsuddin, 2018). Moreover, auditor independence is higher as his financial and family ties with the client are reduced (Dickins et al., 2018).

The AICPA Code of Professional Conduct and the IESBA Code of Ethics for Professional Conduct define independence as a notion comprising two components: independence in appearance and independence of mind (Arens et al., 2017). Other than that, IESBA (2018) stated that independence is linked to the fundamental principles of objectivity and integrity. According to Francis (2011), AQ emerges when auditors can work competently and independently. Octavia and Widodo (2015) and Bouhawia et al. (2015) confirmed that auditor independence and competence significantly affect AQ. Haeridistia and Fadjarenie (2019) stated that many researchers discovered that auditor independence influences AQ. Haeridistia and Fadjarenie (2019) concluded that auditor independence positively affects AQ since independence enables the auditor to perform tasks without bias. This improves users' perception of the AQ and enhances their

confidence in the audited report. Based on the preceding discussion, the following hypothesis was formed:

H_1b: There is a positive relationship between auditor independence and Audit Quality (AQ).

Auditor Competence

Auditor competence is the main factor in the audit input (Rezaee et al., 2016; Dickins et al., 2018) and refers to the auditor's capability to perform tasks seriously and in accordance with professional standards (Abbott et al., 2016). A thorough understanding of the client's operations and client-specific knowledge are necessary for successful audits (Ball et al., 2015). Moreover, the auditor possesses extensive knowledge and practical experience, enabling him to perform a high-quality audit and provide proper opinions on the financial statements (Ismail et al., 2019). The auditor must be competent, possessing various qualities gained through formal education, practical experience, professional exams, good moral standing, and training (Allen & Woodland, 2010; Kusumawati & Syamsuddin, 2018). Accordingly, auditor competence has a significant and positive effect on AQ (Octavia & Widodo, 2015; Bouhawia et al., 2015). Based on the preceding discussion, the following hypothesis was formed:

H_1c: There is a positive relationship between auditor competence and Audit Quality (AQ).

Audit Fees

Auditors can charge higher fees when (i) there is more client demand for further audit efforts, (ii) the auditor has specific industry knowledge, or (iii) the auditor can provide more added value to the client (Yebba & Elder, 2019). Therefore, prior research utilised AF to proxy AQ as they are expected to reflect the level of the auditor's effort in completing his job; higher effort implies higher AQ (DeFond & Zhang, 2014; Hardies et al.,, 2015; Wu et al., 2024). Consequently, Yebba and Elder (2019) suggested that the mandated disclosure level for state governments requires fee premiums for specialised audit firms. However, the market conditions that determine these fee premiums are unclear. Prior research revealed mixed results, and audit firms specializing in PSOs may compete on pricing rather than the value added to their services, particularly in a state without regulation for specific disclosure on the financial statements (Yebba & Elder, 2019). Notably, government auditing is a complex process; however, the auditor charges a lower fee than audit engagements in the private sector. Most AF in PSOs are determined by public tender, and the AF is the most crucial determinant of a winning bid (Elder et al., 2015). Based on the preceding discussion, the following hypothesis was formed:

H_2a: There is a positive relationship between Audit Fees (AF) and Audit Quality (AQ).

Audit Firm Size

Alareeni (2019) and Saeed et al. (2024) reported that past studies confirmed the positive connection between AFS and AQ. However, some studies did not find this relationship in PSOs (Lowensohn et al., 2005; Yuniarti, 2011; Ali & Aulia, 2015). Also, Elder et al. (2015) discovered a positive association between AFS and AQ in municipalities and other municipal organizations. Large, geographically dispersed audit firms are more likely to be decentralised and have a higher degree of individual responsibility. They are also more likely to offer higher-quality audit services since they risk losing their reputation and clientele if they offer lower-quality audit services (Boon et al., 2008). Moreover, a larger size allows the audit firm to build a hierarchal organizational structure and rank its staff as partners and senior managers, improving the AQ (Boon et al., 2008). Based on the preceding discussion, the following hypothesis was formed:

H_2b: There is a positive relationship between Audit Firm Size (AFS) and Audit Quality (AQ).

Internal Audit

Internal audits guide businesses on how to accomplish their goals better by controlling risks and enhancing internal controls (Asare, 2009). Auditing Practice Committee of the Institute of Internal Auditors of the US defined the internal audit as "one element of the internal control system put in place by the management of the institutions for valuation, examination, and disclosure of the accounting and other internal controls in operation" (Chalmers et al., 2019; Dimitrova & Paneva, 2019). Internal audit helps the organization accomplish its goals by methodically and systematically evaluating and enhancing the effectiveness of the risk management, control, and governance systems (Goodwin, 2004; Pilcher et al., 2013). Furthermore, the internal auditors interact with the external auditors, and the external auditor relies on the work of the internal audit in the private and public sectors (Barr-Pulliam et al., 2024). In the audit process, the external auditor must comply with the requirements of ISA 610 (Revised 2013) on using the work of internal auditors (IFAC, 2018). In general, Aikins (2011) concluded that local government auditors (internal auditors) conduct further audits in operating areas, including fiscal receipts and expenses. At the same time, DeFond and Zhang (2014) and Sari et al. (2019) determined that internal audits have a quality assurance function, which can enable higher-quality audits. Based on the preceding discussion, the following hypothesis was formed:

H_3a: There is a positive relationship between internal audit and Audit Quality (AQ).

Accounting Basis

Dewi et al. (2019) reported that according to IFAC (2018), in the world, 25% of governments use accrual accounting to publish their financial statements, whereas 30% continue to report on a cash basis. The remaining governments are switching to accrual accounting and publishing their reports on either a modified cash basis or a modified accrual basis. PSOs frequently adopt cash-based budgeting since it is simple to understand (Eulner & Waldbauer, 2018). However, the accrual basis increases the amount of useful information available to decision-makers and promotes public administration's effectiveness and efficiency. It also promotes transparency, makes it possible for taxpayers and voters to access the same data, and offers contemporary financial reporting that is appropriate for cross-border comparison (Dewi et al., 2019; Eulner & Waldbauer, 2018; IFAC, 2012; Ademola et al., 2019; Setyaningrum et al., 2020). In addition to the above benefits, the adoption of accrual basis accounting, or International Public Sector Accounting Standards (IPSAS), reduces corruption in PSOs and increases financial reporting quality (Cuadrado-Ballesteros et al., 2019; Ademola et al., 2019).

The accounting foundation affects the quality of pre-audited financial statements, which are the primary inputs into the audit process (DeFond & Zhang, 2014). As a result, the AB affects AQ by resulting in accurate financial statements. Based on the preceding discussion, the following hypothesis was formed:

H_3b: There is a positive relationship between accrual Accounting Basis (AB) and Audit Quality (AQ).

Laws and Regulations

According to Alareeni (2019), the legal environment, auditing standards, and accounting practices all have a significant impact on the accuracy of an audit. The LR is considered a component of the client's internal controls, and they impact the effectiveness of audits (Alareeni, 2019). Furthermore, Yebba and Elder (2019) discovered that Michigan, a Generally Accepted Accounting Principles (GAAP)-regulated state, has better AQ due to its regulations, enhancing the reporting environment and requiring specialist auditors with practical experience in the applicable regulations. The auditor may be made aware of non-compliance or suspected non-compliance with applicable LR while performing an audit service for a client. In addition, the effectiveness of

internal control over financial reporting may be improved by more investment in the system to comply with rules, which could reduce the auditor's finding of control inadequacies (Yebba & Elder, 2019). Moreover, the clients are guided in how to perform their activities. This includes how to select external auditors, the terms of the audit agreements, the scope of the audit process, and its results by the LR that apply to them. This makes the auditor more cautious when developing audit procedures and methodologies and more determined to complete the audit most effectively. Based on the preceding discussion, the following hypothesis was formed:

H_3c: There is a positive relationship between Laws and Regulations (LR) and Audit Quality (AQ).

Research Structural Models

The research structural model is intended to test the direct effects of Ethics (ET), Independence (IN), Competency (CM), AF, AFS, IA, AB, and LR as independent variables on AQ as dependent variables, which refer to hypotheses H1a, H1b, H1c, H2a, H2b, H3a, H3b, and H3c, respectively. Figure 1 illustrates the hypothesised direct effects in the research structural model.

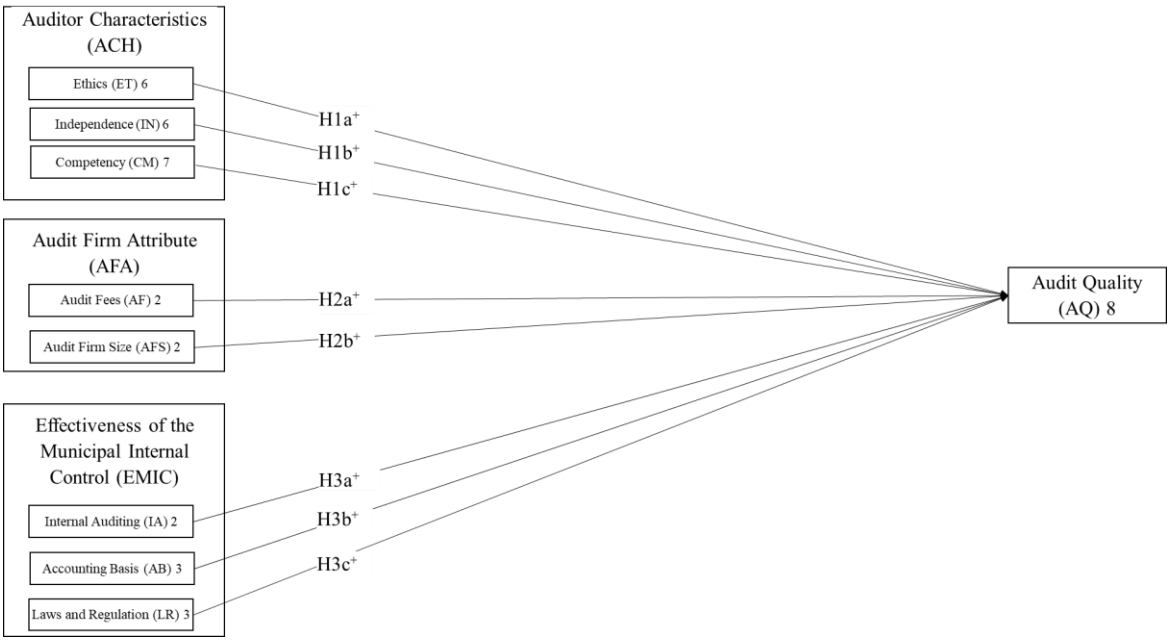

Figure 1: Research hypotheses in research structural model

METHODOLOGY

Research Method

We distribute questionnaires to 155 Palestinian municipalities, which include around 309 principal accountants and internal auditors with relevant experience in financial statement preparation, as well as maintaining direct contact with the municipalities' external auditors. The study used the quantitative method to analyze the independent variables that influence AQ in municipalities.

Questionnaire Design

The questions used in the study were adapted and utilised by previous studies to evaluate the audit service quality in various organizations, mainly municipalities, like Boon et al. (2008) and Butcher et al. (2013) studies. The questionnaire employs 39 closed-ended questions from the investigations of Boon et al. (2008) and Butcher et al. (2013) in order to elicit exact responses and urge respondents to provide honest responses. Accordingly, 31 questions cover the AQ factors, eight cover the AQ, while the rest are about the respondents' profiles. A five-point Likert scale with the

words "strongly disagree" (1) to "strongly agree" (5) is used to evaluate each item. Each statement is followed by a question asking respondents to rate how much they agree or disagree with it. Seven senior accountants with extensive experience working in large cities and joint services councils and four academics in the governance and auditing fields validated the questionnaire before it was made available.

Data Collection and Analysis

Since an online survey is, by nature, confidential and encourages truthful responses, the study uses it to collect data. It is also frequently used in audit and social research (Mazlan & Shahimi, 2022), especially when travel restrictions occur due to the COVID-19 pandemic (Mazlan & Shahimi, 2022). Many researchers have reportedly used online surveys, according to Al-Dhubaibi (2020). According to previous research, Confirmatory Factor Analysis (CFA) and multiple linear regression are frequently used to analyze the gathered data. In this study, SmartPLS 3 will be used to analyze the data. Sarstedt et al. (2016) claimed that Partial Least-Squares (PLS) allows for the approximate approximation of cofactor models that include effect indicators with virtually no constraints while providing the best estimate for composite models. Notably, PLS estimates data with little to no bias, regardless of whether the measurement models are reflective or formative, according to Hair et al. (2017).

Analysis of Survey Response

Through direct contact with accountants and internal auditors via phone, mobile, email, WhatsApp groups, and other social media, a total of 186 questionnaires were gathered, yielding a response rate of 60.2% overall. Prior studies reported 31% and 26% response rates for email surveys sent to accountants who prepare financial statements (Al-Dhubaibi, 2020). However, there were no missing values in the study's variables since every question's response was valid; hence, all the collected questionnaires were used for analysis**.**

Sample Profile

All of the Palestinian municipalities' accountants and internal auditors make up the study's population. The characteristics of the respondents that were examined were related to characteristics of occupation, gender, age, level of education, and work experience. The result revealed that (38.7%) of the respondents work as Accounting Department Heads, (34.9%) were between the ages of 41 and 50, (44.6%) had more than 15 years of experience, (77.4%) bear a bachelor's degree, and 71% of the respondents were men and 29% were women. This suggests that the respondents were competent in responding to the distributed questionnaires.

Construct Measures

According to Hair et al. (2006), if a case exceeds a standard score of ±3.0, it is regarded as an outlier. The findings revealed that none of the cases' values exceeded the ±3.0 threshold, with the cases' standardised (z) scores for the research variables ranging from -2.708 to 1.604. Also, to gauge the univariate normality, the values for skewness and kurtosis are used. Skewness and kurtosis values should both range from ±2 and ±7, respectively (Ho, 2006; Olsson et al., 2000; Oppenheim, 1966). The outcome demonstrates that the skew of all 39 items ranged from -0.925 to -0.412; however, the kurtosis ranged from -0.537 to 0.555, indicating that the data appear to support this hypothesis with sufficient normality.

Measurement Model (Confirmatory Factor Analysis) – Stage 1 of SEM

Manifest and latent variables are compared using the measurement model or CFA. Since latent variables are evaluated in relation to manifest variables, it can be claimed that the measurement model describes how this is done (Ho, 2006). It was determined whether each construct in the CFA models was reliable and valid. While constructs, such as convergent and discriminant

functions, are used to test validity, reliability is measured by Cronbach's alpha, Construct Reliability (CR), and Average Variance Extracted (AVE). Smart PLS3 calculated the model's overall measurement, which included all latent constructs and associated markers.

Convergent Validity and Reliability

Convergent validity refers to the degree of similarity between the items that are indications of a certain construct. Convergent validity might be determined by considering the magnitude of factor loading (standardised regression weights), AVE, and CR among construct sets. Table 1 represents the result of convergent validity Cronbach alpha for the measurement of the model.

Table 1: Convergent Validity and Cronbach's alpha for Measurement Model

The Construct	Code	Item Construct	Factor Loading	AVE	CR	Cronbach Alpha
Ethics (ET)	ET1	The overall reputation of the audit firm is positive	0.882	0.790	0.957	0.947
	ET2	The audit team members as a group always exercise due care throughout the engagement	0.894			
	ET3	The audit firm has strict guidelines on the procedures that must be completed before signing the audit report	0.884			
	ET4	The audit firm actively encourages staff members to take courses and attend seminars in fields where the firm has major clients	0.902			
	ET5	The senior auditors supervise junior audit staff	0.882			
	ET6	The engagement auditors maintain high ethical standards	0.888			
Independence (IN)	IN1	The audit firm has a skeptic's mindset, not a client advocate's mindset.	0.867	0.781	0.955	0.944
	IN2	The audit fee is less than 10% of the total revenue of the audit firm	0.881			
	IN3	The audit firm and individual audit team members never participate in any conduct that might undermine its/their independence, either in fact or in appearance, in any of your contact with them	0.887			
	IN4	The audit firm performing the audit does not provide consultancy services to the municipality	0.908			
	IN5	The audit firm has a high audit staff turnover rate	0.878			
	IN6	Members of the audit team are cycled off the audit on a regular basis.	0.884			
Competency (CM)	CM1	The audit team assigned to the audit engagement (partner, manager, and supervisor) is well-educated on local government units	0.874	0.727	0.949	0.937
	CM2	Other municipalities are audit clients of the auditor that is conducting the audit	0.861			

	CM3	The auditors assigned to the engagement have an extensive understanding of accounting and auditing standards, as well as professional certifications such as the CPA.	0.842			
	CM4	The audit team members, as a whole, have a good understanding of the municipality's operations	0.861			
	CM5	In completing the audit, the audit company makes considerable use of computers and statistical methodologies	0.843			
	CM6	Each audit area has a strict time budget that the audit firm wants its auditors to stick to	0.828			
	CM7	The total number of hours spent on the audit by the audit team (from the beginning of fieldwork to the audit report date)	0.857			
Audit Fees (AF)	AF1	The average amount of audit fees paid in the preceding years	0.930	0.860	0.925	0.837
	AF2	The amount of audit fees is related to the efforts of the auditors in the audit engagement	0.924			
Audit Firm Size (AFS)	AFS1	The suitable number of professionals in the audit team to achieve audit quality	0.932	0.873	0.932	0.855
	AFS2	The legal form of the audit firm and its size affect audit quality	0.937			
Internal Auditing (IA)	IA1	The nature and type of the internal audit function in the municipality	0.951	0.903	0.949	0.893
	IA2	External auditors work closely with internal auditors	0.950			
Accounting Basis (AB)	AB1	The accounting basis used in the municipality's accounting system	0.883	0.814	0.929	0.885
	AB2	The transition from a cash basis to an accrual basis improves the relevance and reliability of the financial statements	0.913			
	AB3	Accrual basis requires the auditor to increase his efforts in the auditing process	0.910			
Laws and Regulation (LR)	LR1	The existence of appropriate laws and regulations increases the audit quality	0.918	0.834	0.938	0.900
	LR2	The commitment of the client to the laws and regulations enhances audit quality	0.930			
	LR3	The commitment of the auditors to the investigation of the client's adherence to applicable laws and regulations increases audit quality	0.892			
Audit Quality (AQ)	AQ1	Audit quality detects and reports the material errors and fraud in the client's financial statements	0.836	0.717	0.953	0.944

AQ2	Audit quality detects and reports the material weakness of the internal control system	0.837
AQ3	The audit firm agrees to complete the audit by a deadline stipulated by the client	0.817
AQ4	The audit team and the audit committee of the council communicate often	0.885
AQ5	The audit team and the council's management communicate often	0.870
AQ6	Throughout the year, the audit firm keeps the council management informed about accounting and financial reporting developments that have an impact on the council	0.820
AQ7	During the audit, the audit engagement partner and manager conduct numerous visits to the council	0.847
AQ8	The auditor adds benefits to the municipality by generating useful improvement ideas	0.859

Factor loading estimates of 0.6 or greater and AVE of 0.5 or greater indicate adequate convergence among the construct's items (Hair et al., 2006). Table 1 provides that the factor loading for each item construct and the AVE values exceeded this requirement and varied from 0.817 for AQ3 to 0.951 for IA1 and 0.717 for AQ to 0.903 for IA, respectively. This demonstrates the total amount of variance in the indicators that the latent construct was able to explain. For every construct, the Composite Reliability (CL) values, which suggest how well the construct indicators predict the latent construct, exceeded the value of 0.6 suggested by Bagozzi and Yi (1988), ranging from 0.925 for the AF to 0.957 for the ET. Nunnally and Bernstein (1994) discovered that all constructions had Cronbach's alpha values higher than the cut-off point of 0.7, indicating how error-free a measure is. Note that the values for these factors ranged from 0.837 for AF to 0.947 for ET.

Discriminant validity

Fornell-Larcker Criterion and HTMT Discriminant Criteria are used to assess the measurement model's validity. Table 2 presents the results of the Fornell-Larcker criterion used to assess the discriminant validity of the measurement model.

Table 2: Fornell-Larcker Criterion in Measurement Model

	AB	**AF**	**AFS**	**AQ**	**CM**	**ET**	**IA**	**IN**	**LR**
AB	**0.902**								
AF	0.698	**0.927**							
AFS	0.691	0.715	**0.935**						
AQ	0.798	0.721	0.711	**0.847**					
CM	0.715	0.647	0.633	0.797	**0.852**				
ET	0.669	0.618	0.594	0.780	0.803	**0.889**			
IA	0.770	0.597	0.648	0.735	0.623	0.577	**0.950**		
IN	0.681	0.597	0.572	0.787	0.786	0.849	0.629	**0.884**	
LR	0.793	0.635	0.610	0.757	0.675	0.620	0.728	0.648	**0.913**

Note: Diagonals represent the square root of the average variance extracted, while the other entries represent the correlations

Table 2 indicates that the inter-correlations between the nine hypothesised latent constructs in the measurement model ranged from 0.572 to 0.849, falling short of the cut-off of 0.85 (Kline, 2005). The analysis also revealed, as summarised in Table 2, that the value of the off-diagonal elements was lower than the value of the AVE square root. This demonstrates that each latent construct measurement was completely discriminatory to each order based on the Fornell-Larcker approach (Fornell & Larcker, 1981; Hair et al., 2014). The findings of the HTMT discriminant criteria are summarised in Table 3.

Table 3: HTMT Discriminant Criteria in Measurement Model

	AB	**AF**	**AFS**	**AQ**	**CM**	**ET**	**IA**	**IN**	**LR**
AB									
AF	0.811								
AFS	0.797	0.845							
AQ	0.871	0.812	0.792						
CM	0.783	0.729	0.706	0.845					
ET	0.730	0.694	0.659	0.825	0.851				
IA	0.867	0.690	0.741	0.800	0.681	0.627			
IN	0.745	0.672	0.637	0.833	0.835	0.898	0.685		
LR	0.888	0.732	0.695	0.821	0.733	0.671	0.812	0.702	

As indicated in Table 3, all the HTMT values between the nine hypothesised latent components in the measurement model were less than 0.90, ranging from 0.627 to 0.898. As a result, it reveals that each latent construct measurement was discriminating from the others (Henseler et al., 2015).

After examining the measurement model's convergent and discriminant validity, it can be concluded that measurement is a valid and reliable tool for evaluating constructs, related items, and sub-constructs.

The Descriptive Analysis

The descriptive function was computed using the covariance matrix approach to account for all of the elements in this investigation. The original measurement item scores were divided to obtain the variable composite scores. Note that parcels are the sums or averages of several separate indicators or elements based on their factor loadings on the construct (Coffman & Maccallum, 2005; Hair et al., 2006). Table 4 summarises the constructs' means and standard deviations on a 5-point Likert scale:

Table 4: Results of Descriptive Statistics for Variables

Constructs	**Mean**	**Standard Deviation**	**Minimum**	**Maximum**
Ethics (ET)	3.597	0.959	1.167	5
Independence (IN)	3.603	0.945	1	5
Competency (CM)	3.480	0.891	1.143	5
Audit Fees (AF)	3.761	0.960	1	5
Audit Firm Size (AFS)	3.659	0.949	1	5
Internal Auditing (IA)	3.642	0.949	1	5
Accounting Basis (AB)	3.633	0.916	1	5
Laws and Regulation (LR)	3.629	0.932	1	5
Audit Quality (AQ)	3.576	0.965	1.125	4.75

To determine central tendency, the mean was used, and it was discovered that all constructs had mean values greater than the third point on a five-point Likert scale. According to the findings, respondents in the consensus had a higher favorable assessment of these variables and believed they were above average. AF received the highest mean score (3.761), followed by AFS (3.659) and IA (3.642). With a mean score of (3.480), CM earned the lowest mean rating.

The standard deviation was employed as a dispersion statistic to assess how much each variable deviates from its mean. Competency suggested the lowest departure from the mean, with a standard deviation of 0.891.

The AQ individual value differed greatly from the mean of any variables under consideration (SD = 0.965). According to the standard deviation, there were some disparities in the respondents' perceptions of AQ. Table 5 provides the mean, standard deviation, minimum, and maximum of AQ items.

Table 5: Results of Descriptive Statistic for the Items of AQ Constructs

Code	Constructs	Mean	Standard Deviation	Minimum	Maximum
AQ	**Audit Quality**	**3.576**	**0.965**	**1.125**	**4.75**
AQ1	Audit quality detects and reports the material errors and fraud in the client's financial statements.	3.66	1.152	1	5
AQ2	Audit quality detects and reports the material weakness of the internal control system.	3.61	1.24	1	5
AQ3	The audit firm agrees to complete the audit by a deadline stipulated by the client.	3.49	1.126	1	5
AQ4	The audit team and the audit committee of the council communicate often.	3.61	1.173	1	5
AQ5	There is communication between the audit team and the council's management.	3.51	1.092	1	5
AQ6	Throughout the year, the audit firm keeps the council management informed about accounting and financial reporting developments that have an impact on the council.	3.59	1.058	1	5
AQ7	During the audit, the audit engagement partner and manager conduct numerous visits to the council.	3.61	1.115	1	5
AQ8	The auditor adds benefits to the municipality by generating useful improvement ideas.	3.53	1.159	1	5

Table 5 presents the mean and standard deviation of all items on AQ. The obtained mean values exceeded the three-point mark (above average), ranging from 3.49 (AQ3) to 3.66 (AQ1). Furthermore, AQ2 was determined to have the highest deviation (SD = 1.24) from its mean value, indicating that the responses obtained from respondents for AQ2 varied the most from one another, whereas AQ6 recorded the lowest deviation (SD = 1.085) from its mean value.

According to the results of Table 5, most respondents believe that AQ will be achieved if the auditors detect and report the deficiencies in the financial statements and internal control and satisfy the council and audit committee through effective communication.

Structural Models - Stage 2 of SEM

The structural model can be described by stating the links between the constructs. The structural model depicts the variables' relationships and illustrates how independent (exogenous) and dependent (endogenous) variables interact (Hair et al., 2006; Ho, 2006).

Examining Direct Effect Hypotheses - Structural Model

The structural model investigated the direct causal relationships between the dependent variable AQ and the independent variables ET, IN, CM, AF, AFS, IA, AB, and LR. As a result, the Smart-PLS model was utilised to investigate the following hypotheses: H1a, H1b, H1c, H2a, H2b, H3a, H3b, and H3c, as summarised and displayed in Figure 2.

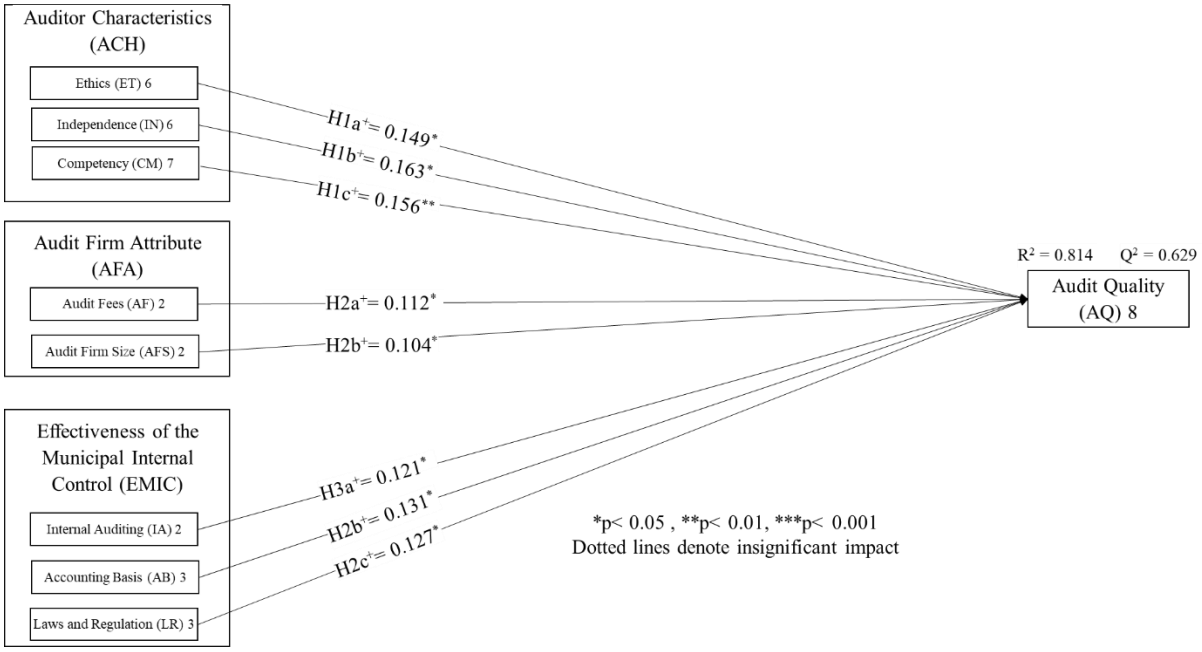

Figure 2: Direct Effect Hypotheses - Structural Model

Results of the Structural Model

The R^2 measures, as well as the level and significance of the path coefficients, are the primary evaluation criteria for the structural model. Since the prediction-oriented partial least squares structural equation modeling (PLS-SEM) approach seeks to explain the variance of endogenous latent variables, the key target constructs level of R^2 should be high, according to (Hair et al., 2011). The R^2 value AQ was 0.814, exceeding the cut-off value of 0.19 established by (Chin, 1998). This indicates that 81.4% of variations in AQ are explained by its eight predictors (i.e., ET, IN, CM, AF, AFS, IA, AB, and LR). According to Chin (2010), the value of Q^2 for AQ was 0.629, which is significantly higher than zero and speaks to the model's predictive relevance. The Goodness of Fit (GOF) for the model was a very high 0.764. The SRMR was 0.036, which was below the cut-off of 0.08. Within the acceptable range of 0.1 and 0.14, the RMStheta value was 0.127. Table 6 displays the path coefficients and results of examining hypothesised direct effects in the structural model.

Table 6: Hypothesised Direct Effects of the Constructs in Structural Model

Path	Std Beta	Std Deviation	t-value	p-value	95% LL-CI	95% UL-CI	f^2	VIF	Hypothesis Result
ET→AQ	0.149*	0.064	2.456	0.020	0.032	0.281	0.027	4.457	H1a+: Supported
IN→AQ	0.163*	0.070	2.293	0.019	0.025	0.300	0.033	4.313	H1b+: Supported
CM→AQ	0.156**	0.058	2.731	0.007	0.042	0.279	0.035	3.755	H1c+: Supported
AF→AQ	0.112*	0.055	2.116	0.044	0.002	0.218	0.026	2.599	H2a+: Supported
AFS→AQ	0.104*	0.052	2.976	0.045	0.005	0.200	0.022	2.584	H2b+: Supported
IA→AQ	0.121*	0.051	2.294	0.018	0.019	0.216	0.027	2.919	H3a+: Supported
AB→AQ	0.131*	0.063	2.019	0.039	0.007	0.254	0.022	4.229	H3b+: Supported
LR→AQ	0.127*	0.056	2.297	0.023	0.015	0.236	0.028	3.161	H3c+: Supported

*p< 0.05 , **p< 0.01, ***p< 0.001

As can be observed in Table 6, all paths were statistically significant since their *p*-values were below the 0.05 threshold for standard significance, and their t-values were greater than 1.645. Furthermore, the bias-corrected 95% confidence intervals did not suggest any intervals straddling a 0, the lower level of all variables is located between 0.002 for AF and 0.042 for Competence, and the upper level of all variables is located between 0.200 for AFS and 0.300 for Independence. The standard path coefficient for all items was between 0.104 for AFS and 0.163 for Independence. This indicates a positive relationship. However, the f-squared value was between 0.022 for AFS and AB and 0.035 for Competence. This indicates a small effect size of each variable on AQ. The findings also revealed that the Variance Inflated Factor (VIF) of all independent variables in predicting AQ was between 2.584 for AFS and 4.457 for Ethics, which was less than the five thresholds and demonstrated that collinearity was not present. According to the study findings, all the study hypotheses (H1a, H1b, H1c, H2a, H2c, H3a, H3b, and H3c) are supported. These findings are consistent with the prior research discussed in the literature review sections.

CONCLUSION

The current study investigated the AQ provided by external audit firms to understand the most influential factors that raise and improve the AQ in the municipalities. The findings confirmed a positive and significant relationship between AQ in Palestinian municipalities and the following factors: auditor ethics, independence, competence, auditing fees, AFS, IA, AB, and applicable LR. Auditor characteristics (ethics, independence, and competence) have the greatest positive impact on AQ, and elements of effective municipal internal control have a moderate influence. Meanwhile, audit firm attributes have the least positive impact on AQ as perceived by municipal accountants and internal auditors. Furthermore, the findings confirmed that total AQ in municipalities, as perceived by accountants and internal auditors, will be achieved at a rate greater than 71.5% (the mean of responses was 3.576 out of 5). This is if auditors detect and report deficiencies in financial statements and internal control, in addition to effective communication with the council and audit committee, which had the greatest influence on total AQ.

To the best of the researcher's knowledge, this study is one of the few studies conducted in developing countries to examine the AQ in the PSOs. The first study in Palestine discussed the quality of external auditing in the municipalities and the factors that impact the prediction of AQ. Therefore, this study adds to an expanding research stream on AQ by adding the Palestinian municipalities' accountants and the internal auditors' perspective. Moreover, the findings of the study help audit firms differentiate their advertising and service strategies to coincide with AQ criteria that are perceived by accountants and internal auditors involved in the procurement process of external audit services. Other than that, the study recommends that the Audit

Profession Council in Palestine and the PACPA add the IPSAS and related educational material to the Professional Exam and require the external auditor to get specific auditing training courses related to PSOs, particularly municipalities. Additionally, the management of the municipality is recommended to ask the candidate auditor to provide a technical offer before the financial offer to select a competent auditor without considering the AF as the main determinant for hiring a new auditor. It is also recommended that the municipality management employ competent internal auditors to maintain a reliable financial information system and provide high-quality pre-audit financial statements that increase AQ. Moreover, the study encourages the legislative parties to thoroughly review municipal LR to bring them more in line with recent changes in accounting systems and audit processes. Finally, the study evaluates AQ in the municipality without considering other AQ aspects, notably political and technological issues in public sector organizations. Hence, these shortcomings may be addressed in future studies.

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