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Policeman Theory of Auditing: Review of the Past and Present

Olusola E. Igbekoyi[1], Israel S. Akinadewo[2], & Muyiwa E. Dagunduro[4]
[1]Department of Accounting, Adekunle Ajasin University Akungba-Akoko, Ondo State, Nigeria.
Email: Olusola.igbekoyi@aau.edu.ng[1]
[2&3]Department of Accounting, Afe Babalola University Ado-Ekiti, Ekiti State, Nigeria.
Email: omoeri@abuad.edu.ng[2]; dagundurome@pg.abuad.edu.ng[3]
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Abstract
Over the years, Policeman Theory has undergone dynamic transformations, responding to the ever-changing complexities of business environments, regulatory landscapes, and societal expectations. As auditors play a crucial role in ensuring transparency, accountability, and the reliability of financial information, understanding the nuances of the Policeman Theory becomes imperative for both scholars and practitioners. This study embarks on a comprehensive review of the past and present dimensions of the Policeman Theory, shedding light on its origins, evolution, and contemporary relevance. This study utilized an exploratory research design, and data were collected from secondary sources through a thorough review of relevant existing literature. The findings underscore the relevance of the Policeman Theory, emphasizing auditors' role as vigilant overseers in detecting and deterring financial irregularities and fraud. The study reinforces the importance of auditors acting as proactive guardians against financial improprieties, resonating with the call for innovative approaches such as the integration of forensic accounting practices. Independence, highlighted as a cornerstone, aligns with the principles of the Policeman Theory, emphasizing the role of auditors as independent evaluators safeguarding against financial misconduct. Based on the findings, it is recommended that auditors embrace continuous learning and adaptation to stay abreast of technological advancements. The integration of forensic accounting practices should be explored as a proactive strategy to address the inadequacies of traditional audit reports and enhance fraud detection capabilities.

Keywords: *Policeman Theory, Auditing, Past, Contemporary, Statutory Duties of Auditors*

1. Introduction

In the realm of auditing, the evolution of theoretical frameworks has been instrumental in shaping the practices and principles that guide the profession. The "Policeman Theory of Auditing" stands as a distinctive and enduring concept that has influenced auditors' roles and responsibilities throughout history (Akinadewo et al., 2024; Fijabi, 2020). The Policeman Theory posits auditors as guardians and enforcers of financial integrity, akin to vigilant policemen safeguarding the interests of stakeholders in the corporate landscape. Over the years, this theoretical perspective has undergone dynamic transformations, responding to the ever-changing complexities of business environments, regulatory landscapes, and societal expectations (Al-Dhubaibi, 2021). As auditors play a crucial role in ensuring transparency, accountability, and the reliability of financial information, understanding the nuances of the Policeman Theory becomes imperative for both scholars and practitioners (Janat, 2022; Omodero & Okafor, 2020).

This study embarks on a comprehensive review of the past and present dimensions of the Policeman Theory, shedding light on its origins, evolution, and contemporary relevance. This study engages in a rigorous exploration of the historical foundations of the Policeman Theory, tracing its roots to seminal works and influential figures in auditing literature. Furthermore, it critically examines the theoretical developments, and paradigm shifts that have occurred over time, analyzing the impact of global events, technological advancements, and regulatory changes on the conceptualization and application of the theory. As the study navigates the complexities of the contemporary auditing landscape, this review aims to provide a nuanced understanding of how the Policeman Theory has adapted to meet the challenges and demands of the 21st century. By synthesizing insights from historical perspectives and contemporary practices, this article contributes to the ongoing discourse on the role and responsibilities of auditors in ensuring financial probity and maintaining public trust.

In the subsequent sections, this study delves into key themes, theoretical debates, and empirical studies that have shaped the Policeman Theory, offering a comprehensive and insightful analysis of its implications for auditing practices in the present day. Through this exploration, we aim to contribute meaningfully to the academic literature, fostering a deeper understanding of the Policeman Theory's significance and relevance in the ever-evolving landscape of auditing.

2. Literature Review

This section presents important studies relevant to the variables analyzed in this research. It examines earlier findings to offer context and background, emphasizing the connections between these studies and their contributions to the current investigation.

2.1.1 Policeman Theory

The concept known as the Policeman Theory, first introduced by Charles F. Hickson and attributed to Limperg in the late 1920s, outlines a dual role for auditors: preventing and detecting fraud and ensuring the accuracy of financial reports. This theory affirms auditors as proactive watchdogs, prioritizing preventive measures. Scholars like Davidson (1975) and Salehi (2010) supported this perspective. While the Policeman Theory gained prominence for its emphasis on auditors' proactive fraud prevention stance, it faced criticism as audit demand theories evolved in the 1940s. Critics highlighted its limitations, particularly its failure to address the broader objective of establishing truth and fairness in financial statements.

2.1.2 Policeman Theory: Review of the Past and Present

The early 2000s, marked by corporate scandals like Enron and WorldCom, led to a reevaluation of the Policeman Theory. The need for auditors to reclaim their watchdog role became evident, responding to calls for renewed assurance in financial reporting (Olaoye et al., 2019; Salehi, 2010). In this context, the Policeman Theory regained significance, acknowledging both the demand for audit services and supply-side considerations. Limperg (1932) argued that the demand for audit services is linked to external stakeholders' involvement in a company. This renewed focus on auditors as proactive overseers has become integral to discussions on restoring trust in financial reporting systems. In the face of contemporary challenges reshaping the auditing profession, the Policeman Theory serves as a historical anchor and a renewed call for auditors to act as vigilant guardians, ensuring financial transparency and integrity (Enofe et al., 2013; Fadzly & Ahmad, 2004).

Nguyen and Nguyen (2020) emphasize that the primary function of an audit assignment is to provide assurance services, assuring stakeholders about the truthfulness and reasonableness of financial reports. Investors' expectations, as stressed by Jannat (2022), revolve around auditors' performance in fulfilling their audit responsibilities. However, between 1970 and 1980, the accounting profession faced widespread criticism due to corporate scandals, audit failures, and lawsuits against many accounting firms (Ali et al., 2008). The Companies and Allied Matters Act (CAMA), 2020, underscores the significance of auditors in ensuring financial transparency. Section 401 mandates every corporate entity to appoint an auditor responsible for examining financial statements and reporting to the company's members (Section 404, CAMA, 2020). Section 407 requires the auditor to conduct necessary investigations, forming an opinion on the financial statements while maintaining independence from the reporting entity (Section 403, CAMA, 2020).

2.1.3 Assumptions of Policeman Theory

The theory assumes that auditors have a dual responsibility: preventing and detecting fraud and ensuring the accuracy of financial reports. Policeman Theory assumes that auditors should adopt a proactive approach, prioritizing preventive measures over-reactive responses to fraudulent activities. The theory suggests that the demand for audit services is directly linked to the participation of external stakeholders in a company (Enofe et al., 2013).

2.1.4 Relevance of Policeman Theory

The theory is relevant as a historical anchor, reflecting the early emphasis on auditors as proactive watchdogs, especially in the prevention and detection of fraud. The resurgence of the Policeman Theory in the early 2000s demonstrates its relevance as a response to high-profile corporate scandals (Enron, WorldCom), highlighting the need for auditors to re-embrace their watchdog role (Ali et al., 2008). In the contemporary context, the theory remains relevant in discussions about restoring trust in financial reporting systems, emphasizing the importance of auditors in ensuring financial transparency and integrity (Akinadewo et al., 2024).

2.1.5 Application of Policeman Theory

The theory is applied to explain the demand for audit services, asserting that external stakeholders' involvement in a company necessitates the proactive role of auditors. Policeman Theory aligns with regulatory frameworks like the Companies and Allied Matters Act (CAMA), emphasizing the appointment of auditors and their responsibilities in examining financial statements (Agyei et al., 2013). The theory guides the application of auditors' duties, including efficient discharge, qualified staff employment, and maintaining independence from the reporting entity, as outlined in regulatory statutes (Akinadewo et al., 2024).

2.1.6 Criticisms of Policeman Theory

Critics argue that the theory has a limited scope, primarily focusing on fraud prevention and detection, neglecting broader objectives like establishing the truth and fairness of financial statements (Nguyen & Nguyen, 2020). Policeman Theory faced criticism as audit demand theories evolved, indicating that it may not adequately address the complexities of contemporary auditing, such as globalization, technological advancements, and expanded roles for auditors. The theory has been criticized for contributing to stakeholder dissatisfaction, particularly in the late 20th century, as expectations shifted from auditors primarily detecting fraud to verifying the precision and impartiality of financial statements (Janat, 2022). The theory's impact on how auditors' main duty is perceived has been associated with the Audit Expectation Gap, where public expectations may not correspond with the explicit responsibilities delineated by auditing norms. In summary, the Policeman Theory, while rooted in historical perspectives, has faced criticism for its limited scope and has undergone reevaluation in response to the evolving landscape of the auditing profession (Chandler et al., 1993). Its application and relevance continue to be debated, especially in light of contemporary challenges and changing expectations of auditors.

2.1.7 Statutory Primary Responsibilities of Auditors

According to Olaoye (2019) auditor's duties include efficient and effective discharge of responsibilities, employing qualified staff, and ensuring a true and fair view of the entity's financial position. Despite not being part of the entity's management, the auditor faces public scrutiny in cases of corporate failure, leading to questions about the audit process and potential calls for an Audit Expectation Gap (AEG) (Ojo, 2006). The misbelief that statutory auditors' main duty is to uncover fraud persisted, driven by the Policeman Theory, but encountered obstacles in the latter part of the 20th century. The auditing profession in Britain moved away from the idea that auditors were chiefly accountable for detecting fraud, highlighting instead their responsibility in ensuring the accuracy and impartiality of financial statements. This change aimed to shield auditors from legal liabilities but resulted in stakeholder discontent, as they anticipated auditors to take a more active stance in fraud detection (Omodero & Okafor, 2020).

To elucidate the main duty of auditors, International Standards on Auditing (ISA 240) specify that auditors are principally tasked with providing an impartial assessment of the accuracy, truthfulness, and fairness of financial statements, rather than actively uncovering financial fraud or errors. Instead, the responsibility for preventing and discovering fraud rests with an organization's management and governance through the establishment of robust internal control mechanisms (IFAC, 2009). Although auditors' primary focus has shifted away from direct fraud detection, there remains an expectation for them to uphold professional skepticism and remain vigilant for potential material misstatements attributable to fraud (Enyi et al., 2012; Fijabi, 2020). This viewpoint acknowledges the evolving nature of auditors' obligations concerning fraud, recognizing that while they are not the primary fraud detectors, they still play a role in identifying significant inaccuracies stemming from fraudulent activities (Salehi, 2010).

In today's auditing environment marked by heightened intricacy in business dealings, globalization, and advanced technologies, the pertinence and suitability of the Policeman Theory have come under scrutiny. Auditors are now required not only to serve as financial overseers but also as strategic consultants, contributing value beyond their conventional responsibilities (Owolabi et al., 2016).

2.2 Theoretical Review

This research examined both the Policeman Theory and the Confidence-Inspiring Theory as the foundational frameworks guiding the investigation.

2.2.1 Policeman Theory

The concept known as the Policeman Theory, originally introduced by Charles F. Hickson and attributed to Limperg in the early 20th century, suggests that auditors function as diligent supervisors, identifying and preventing financial irregularities, fraud, and inaccuracies in financial reporting (Hayes et al., 1999). This theory underscores the crucial role of auditors in maintaining the accuracy of financial information, a fundamental aspect of the efficient functioning of capital markets, and the confidence of various stakeholders. Also referred to as the "watchdog theory," the Policeman Theory posits that auditors serve as guardians or overseers of financial systems, entrusted with the responsibility of uncovering and preventing financial misconduct, fraudulent activities, and errors (Akinadewo et al., 2024). This theory highlights the auditor's role as an impartial and objective evaluator, ensuring that financial statements faithfully reflect an organization's financial position. It positions auditors as vigilant monitors of financial operations, acting as a protective shield against financial improprieties (Humphrey et al., 1993).

2.2.2 The Theory of Inspired Confidence

Proposed by Dutch professor Theodore Limperg, this theory explores the complexities surrounding the demand for and provision of audit services. According to Limperg, as cited by Salehi (2011), the need for audit services arises directly from the involvement of external stakeholders in a company. Shareholders, who contribute to the company's investments, expect transparency and accountability from management. Recognizing the potential bias in management-provided information and the likelihood of conflicting interests between management and external stakeholders, there arises a need for an audit of this information, as emphasized by Adeyemi and Uadiale (2011). Limperg suggests that, regarding the level of audit assurance, auditors should fulfill their responsibilities in a manner aligned with the expectations of well-informed external parties.

2.3 Empirical Review

Numerous scholars have investigated the principal duties and functions of auditors in historical as well as modern audit contexts. The findings of these studies are outlined below, highlighting a deficiency in the existing literature that this research aims to address. Tjeng and Nopianti (2021) conducted empirical research to investigate the influence of auditors' professional competence on different aspects of information quality within financial statements. Their explanatory approach unveiled a notable positive association between auditors' technical expertise and the quality of information presented in financial reports. Al-Dhubaibi (2021) delved into understanding auditors' perceptions of their responsibilities and potential legal liabilities in cases where they fail to detect fraud or significant misstatements and subsequently report these findings. The study, involving various types of audit firms, including global and local ones, revealed significant variations in auditors' perceptions influenced by their anticipated exposure to litigation risks.

Owolabi and Olagunju (2020) conducted a comprehensive examination of the historical evolution of audit theory and practice, tracing their progression from ancient civilizations to the present era. Their study aimed to identify future directions for auditing practices. Through desk research, they observed significant shifts in audit theories and practices, particularly with the widespread adoption of digitalization in the business world, rendering many traditional audit theories obsolete.

Gaye and Colley (2020) explored the potential existence of an Audit Expectations Gap within The Gambia's public sector from the perspectives of auditors and non-auditing professionals. Through structured interviews, they identified characteristics of the gap and proposed ways to narrow it, emphasizing the need to improve the credibility of the auditing profession. Non-auditing professionals' expectations regarding auditors' roles in detecting and preventing fraud and providing assurance on internal controls contributed to the development of unrealistic expectations, thus widening the audit expectations gap.

Ogoun and Odogu (2020) conducted a qualitative analysis of existing literature to ascertain whether the scope and content of audits and auditors' reports meet the information needs and expectations of financial statement users, particularly in the context of anti-corruption efforts. Their examination of various auditing theories highlighted the existence of an expectation gap in terms of both assurance and content between auditors and financial statement users. The research also revealed that traditional auditing methods may be insufficient for detecting and preventing fraud and errors in the current information age, and conventional audit reports may not adequately address the information needs of anti-corruption agencies.

Akhidme (2019) focused on exploring the audit expectation gap within the context of integrating forensic accounting practices into financial statement audits. Through an extensive review of relevant literature, the study proposed that enhancing auditors' capabilities in fraud detection by incorporating forensic accounting techniques could effectively narrow the expectation gap. Collaborative synergy between auditors and forensic accountants was suggested as a means to improve fraud detection and bridge the gap between financial statement users' expectations and auditors' performance.

Olaoye et al. (2019) investigated the impact of statutory auditors' independence on the reliability of financial statements in Nigerian manufacturing companies. Their survey-based research found a positive and significant relationship between auditor independence and the reliability of financial statements, suggesting that greater independence enhances the credibility of financial reporting.

Owolabi et al. (2016) conducted a historical exploration of the auditing field, tracing the evolution of auditors' roles and responsibilities over time. Their review of the literature revealed significant changes in auditors' duties and highlighted the challenges inherent in providing complete assurance regarding the absence of fraud or financial irregularities in clients' reports.

Issahaku and Muntari (2015) investigated the audit expectation gap in Ghana, surveying auditors, bankers, and accounting students regarding their perceptions of auditors' responsibilities and performance. Their findings indicated a substantial expectation gap, particularly concerning auditors' roles in fraud detection and prevention, the effectiveness of internal controls, and the discretion exercised in selecting audit procedures.

These investigations collectively illuminate various aspects of auditors' duties, perspectives, and the Audit Expectations Gap, underscoring a gap in current literature that this study aims to fill. There is a shortage of research focusing specifically on the audit expectation gap within the context of contemporary auditing. Addressing this gap in research would enhance our comprehension of modern auditing practices and provide insights into how auditors can effectively meet stakeholders' expectations in today's ever-changing business landscape.

3 Methodology

This study employed an exploratory research design, which is particularly useful for gaining insights into a relatively uncharted area of inquiry. By focusing on exploration, the research aimed to identify patterns, relationships, and trends associated with the variables under investigation. Data were gathered from secondary sources, which involved conducting a comprehensive review of relevant existing literature. This literature review included academic journals, government reports, and industry publications that provide valuable information and findings related to the study's topic. By synthesizing this pre-existing knowledge, the study not only establishes a foundation for understanding the current research context but also identifies gaps in the literature that the current investigation seeks to address. This approach allows for a broader understanding of the subject matter and facilitates the development of informed hypotheses and conclusions based on established research.

4. Results and Discussion

The findings highlighted the intricate nature of auditors' roles and the dynamic challenges they encounter in the evolving landscape of auditing. The discussion revolves around key themes, such as the need for continuous adaptation influenced by technological advancements, the pivotal role of professional competence, the complexities of stakeholder dynamics shaping auditors' perceptions, and the crucial importance of bridging the Audit Expectations Gap for maintaining the credibility of the auditing profession. A notable observation is the inadequacy of traditional audit reports in meeting contemporary demands, as revealed by Ogoun and Odogu (2020) study. This inadequacy prompts a call for innovative approaches, and the integration of forensic accounting practices, as suggested by Akhidme (2019), emerges as a promising strategy. This integration not only addresses the shortcomings in traditional methods but also enhances fraud detection capabilities, directly connecting with the ongoing discourse on the Policeman Theory in auditing.

The Policeman Theory, which posits that auditors act as vigilant overseers, detecting and deterring financial irregularities and fraud, aligns with the findings related to the inadequacy of traditional audit reports. The need for auditors to act as proactive guardians against financial improprieties resonates with the call for innovative approaches, including the integration of forensic accounting practices. This synergy emphasizes the importance of auditors playing a policing role in ensuring the integrity of financial information.

Independence, highlighted by Olaoye et al. (2019) findings, remains a cornerstone in the discussion. The role of auditors as independent evaluators is essential for the credibility of financial statements and aligns with the principles of the Policeman Theory. An independent auditor acts as a safeguard against financial misconduct, contributing to the overall integrity of the auditing process.

The substantial expectation gap identified in Ghana, as discussed by Issahaku and Muntari (2015), emphasizes the challenges related to fraud detection, internal controls, and auditors' discretion. These challenges resonate with the multifaceted nature of auditors' roles highlighted in the Policeman Theory. Auditors, in their policing role, face complexities in navigating stakeholder expectations, necessitating a delicate balance to bridge the gap and uphold the credibility of the profession.

In conclusion, the synthesis of these findings not only contributes to a comprehensive understanding of the challenges and dynamics within the auditing profession but also reinforces the relevance of the Policeman Theory. The identified gap in the existing literature, as addressed by this research, aims to enrich the discourse on auditors' roles and responsibilities, particularly in the context of contemporary audit engagements and the ongoing evolution of auditing practices.

This enriched understanding provides valuable insights for auditors, scholars, and stakeholders, aligning with the principles of the Policeman Theory in ensuring the integrity of financial information and maintaining public trust.

5. Conclusion and Recommendations

The study embarks on a comprehensive review of the past and present dimensions of the Policeman Theory, shedding light on its origins, evolution, and contemporary relevance. Key themes include the imperative for continuous adaptation influenced by technological advancements, the pivotal role of professional competence, the complexities of stakeholder dynamics shaping auditors' perceptions, and the crucial importance of bridging the Audit Expectations Gap for maintaining the credibility of the auditing profession. The inadequacy of traditional audit reports in meeting contemporary demands prompts a call for innovative approaches, with the integration of forensic accounting practices emerging as a promising strategy. This integration not only addresses shortcomings in traditional methods but also enhances fraud detection capabilities, aligning with the ongoing discourse on the Policeman Theory in auditing. The findings underscore the relevance of the Policeman Theory, emphasizing auditors' role as vigilant overseers in detecting and deterring financial irregularities and fraud. The study reinforces the importance of auditors acting as proactive guardians against financial improprieties, resonating with the call for innovative approaches such as the integration of forensic accounting practices. Independence, highlighted as a cornerstone, aligns with the principles of the Policeman Theory, emphasizing the role of auditors as independent evaluators safeguarding against financial misconduct. The substantial expectation gap identified in Ghana further emphasizes the multifaceted nature of auditors' roles in navigating stakeholder expectations, requiring a delicate balance to uphold the credibility of the profession.

Recommendations

Based on the findings, it is recommended that auditors embrace continuous learning and adaptation to stay abreast of technological advancements. The integration of forensic accounting practices should be explored as a proactive strategy to address the inadequacies of traditional audit reports and enhance fraud detection capabilities. Stakeholder communication and education are crucial to bridging the Audit Expectations Gap and fostering a realistic understanding of auditors' roles. Auditors should remain steadfast in upholding independence, recognizing its pivotal role in ensuring the credibility of financial statements. Future research should further explore innovative approaches in auditing, considering the evolving demands of the digital era.

Contribution to Knowledge

The study significantly contributes to a comprehensive understanding of the challenges and dynamics within the auditing profession. By linking the findings to the Policeman Theory, it reinforces the conceptual framework of auditors as vigilant overseers. The identified gap in the existing literature regarding auditors' roles and responsibilities in contemporary audit engagements is addressed, enriching the discourse and providing valuable insights for auditors, scholars, and stakeholders. The study contributes to the ongoing evolution of auditing practices, aligning with the principles of the Policeman Theory in ensuring the integrity of financial information and maintaining public trust.

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