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Examining the relationship between social capital, audit quality and financial reporting: Evidence from certified public accountants in Iraq

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Abstract

In recent years, social capital has become one of the main concerns of companies. From the perspective of audit firms, auditors and accountants, paying attention to social capital in order to increase audit quality is one of the concerns. In this regard, the aim of the present study is to investigate the relationship between social capital, audit quality and financial reporting in Iraq. The present study was conducted by distributing a questionnaire to the statistical community of certified public accountants in Iraq, with a statistical sample of 342 people based on the Cochran formula. To measure social capital, the questionnaire of Villanova and Josa (2003) was used, to measure audit quality, the questionnaire of Nickel et al. (2013) was used, and to measure financial reporting quality, the questionnaire of Wen (2014) was used. The results showed that the results of data analysis showed that there is a positive relationship between social capital and audit quality. There is also a positive and significant relationship between the subcomponents of social capital, namely between collective trust, collective cohesion and solidarity, collective identity, cooperation and mutual cooperation, empathy, mutual understanding and respect, voluntary cooperation and participation, and networks and common norms and audit quality. On the one hand, the results of data analysis showed that there is a positive relationship between social capital and the quality of financial reporting. There is also a positive and significant relationship between the subcomponents of social capital, namely between collective trust, collective cohesion and solidarity, collective identity, cooperation and mutual cooperation, empathy, mutual understanding and respect, voluntary cooperation and participation, and networks and common norms and financial reporting quality.

Keywords: Social responsibility, information quality, audit quality, accounting.

Introduction

The enormous expansion of economic entities and their complexity, the great increase in the share of small shareholders in companies and the subsequent conflict of interest make the audit needs more necessary than ever. In this environment, users need various information including financial information about business enterprises to make decisions (Al-Dmour et al., 2018). In this regard, financial statements are considered the most important set of financial information of companies and represent their performance results (Fisher et al., 2020). Financial reports should always provide reliable information to help users make decisions. Financial reports should contain relevant, reliable, comparable and understandable information (Salehi et al., 2021). Reliability is related to the quality of information and creates confidence that the information is generally free from error and bias and honestly reflects everything it is expected to express. An annual report can never be generally free from bias because the economic conditions presented in annual reports are always presented under conditions of uncertainty. Many estimates and assumptions are included in the report (Paternostro et al., 2021). Although complete absence of bias is not achievable, for this information to be useful in decision-making, a certain level of accuracy is required for the quality of reported financial statements (Wang et al., 2020). The more accurate the figures in financial statements are, the higher the transparency assessment will be. Financial reporting quality is about promoting transparency and publishing quality annual reports through accurate and complete disclosure. The quality of reports has always been a topic of interest to boards of directors, stakeholders, researchers, and professional accountants themselves. In recent years, the wave of accounting scandals that have occurred in international financial professions has led to increasing questions and concerns about the quality of financial reporting (Hu and Liu., 2017).

In recent years, significant developments have taken place in the accounting and auditing profession, and important steps have been taken in accounting research, and most research is focused on audit quality. As financial markets become more

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complex and the scope of accountability for managers expands, the role of transparency and quality of financial reports in organizations has become very important. High quality financial reports are realized through quality audits among financial statement stakeholders (Monsen., 2022). Achieving high quality financial reporting depends on the objectivity and accuracy of each link in the supply chain, and since audit quality is multifactorial and invisible, researchers are trying to find surrogates or components of audit quality, such as expert opinions, to identify audit quality outcomes (Rey et al., 2020). Audit quality is an abstract concept of a construct, and various dimensions and aspects of this concept have unique strengths and weaknesses. Assessing audit quality is very difficult because the amount of evidence and accuracy that the auditor provides is not visible; therefore, to assess audit quality, we can consider the audit process, which is limited by financial reporting (Monzur and Habib., 2023). Daoust and Malsch (2022) believe that due to the development of economic activities in financial markets and the development of investment in capital markets, access to accurate and reliable information and its correct and realistic assessment are the main tools for making useful decisions and using financial information optimally and correctly. In today's world, information plays a key role in human life, and the more advanced a society is, the more accurate information it uses. Extensive research on financial markets and drawing correct conclusions can accelerate the growth and development of these markets. The world's reputable financial markets have shown that they have been successful in providing and collecting capital and this is the result of shareholders' trust in companies' financial reports, capital market audit reports, and market efficiency, so that they are sure that their capital has not been wasted and will bring reasonable profits. Dakhli (2022) believes that one of the reasons for progress in developed societies is the optimal and effective use of financial information, which has increased the awareness of stakeholders about the company's responsibilities and ethical obligations towards society, especially after the Enron scandal, which has increased the need for social responsibilities. Various studies have shown the willingness of stakeholders to pay attention to companies' social responsibility and, as a result, its financial information. Therefore, social responsibility to stakeholders should be considered by all companies (Coram wt al., 2022).

Burke and Gunny (2022) believe that the attention paid to the quality of financial reports of companies has increased by stakeholders. This has happened due to weaknesses in the quality of auditing in companies. Weaknesses in the quality of

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financial auditing have caused investors to lose confidence in the reliability of companies' financial reports. Therefore, the quality of published audited financial reports is an important element for gaining the trust of stakeholders. These essential elements have led to the importance of social capital, which plays an important role.

Social capital is known as a general and transformative solution to the problems of building trust, cooperation and synergy, as well as opportunistic behaviors and trust in individuals' adherence to laws and regulations (Djaballah., 2019). Social capital is mainly defined as a set of environmental characteristics and social relationships that can enhance and facilitate mutual trust, cooperation, coordination and synergy between individuals to achieve common goals and interests (Ben et al., 2018). In fact, social capital is a broad and flexible perspective that expands, adjusts and adapts itself depending on the subject under study to encompass the comprehensiveness and all dimensions and changes of the studied environment and to explain them in a meaningful, comprehensive conceptual framework in order to achieve a sustainable state of development, transformation and prosperity (Azimli and Cek., 2023). In other words, social capital is a multiple and complex concept, so that gaining knowledge of it requires an in-depth study of the specific contextual factors under study (Salehi, M Ajel and Zimon., 2022). In this regard, the aim of the present study is to examine the relationship between social capital, audit quality and financial reporting in Iraq.

A review of theoretical foundations and research background

In the social capital literature, seven factors of collective trust, collective cohesion and solidarity, collective identity, mutual cooperation and collaboration, networks and common norms and empathy, mutual understanding and respect, voluntary cooperation and participation are considered as the foundation and source of social capital in the environment (Wang et al., 2020). Social trust, as the main component of social capital, is the goodwill of an individual towards the members of the society (Agustia et al., 2020). Social trust means truthfulness and honesty, cooperative tendencies and confidence and respect for the rights of others, which is one of the important aspects of human relationships that lays the groundwork for participation and cooperation between members of the society. Trust lowers the costs of social and economic interactions and various actions. Increasing mutual trust in a company can significantly increase the efficiency of systems, and some management experts consider its value to an organization to be higher than information (Alfaro et al., 2018). Collective cohesion and solidarity is a sense of

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mutual responsibility between several people or groups who have will and awareness. Collective cohesion and solidarity are also an agreement on values and attitudes that are born in a social process and are the product of rational action (Fisher et al., 2020). Collective identity is the attachment of a number of people to common matters with a specific title. Mutual cooperation and collaboration are used in contrast to the term competition and express the collective action that members act with others in their community or group in common cases (Hu and Liu., 2017). Shared networks and norms refer to the position of an individual's communication network in the organization, that is, the position of an individual in social networks determines the social capital of an individual, which leads to different career outcomes and connects the individual to a human and social network (Rouf., 2018). Mutual understanding means that an individual can understand the lives of others even when he is not in that situation. Mutual understanding improves social relationships and leads to the creation of supportive and accepting behaviors towards other people. The aforementioned skills create mutual friendship between members of the organization and develop and improve social relations (Algan and Cahuc., 2014). Voluntary cooperation and participation are achieved through interaction between individuals and the existence of appropriate norms of cooperation and collaboration. In all the aforementioned dimensions of social capital, mutual trust, beneficial cooperation, achieving collective benefits and synergies, and avoiding any self-interest, norm-breaking, and obvious opportunistic actions are emphasized. Accordingly, in the field of financial reporting, if the client has more social capital, it is expected that he will take fewer opportunistic actions (Arif et al., 2016).

Van (2025) based on a sample of 5167 companies in the United States from 2017 to 2024 and using regression analysis method concluded that the establishment of companies in an environment with more social capital results in paying lower audit fees. Also, after studying all companies in the CompuStat database using regression analysis method, they found that companies located in areas with more religiosity engage in unethical behavior and unfair financial reporting to a lesser extent. In this regard, Noury et al Noury (2024) studied 10168 companies in the United States from 2016 to 2023 and applied regression analysis method showed that there is a positive and significant relationship between the social capital of the company's environment and the quality of financial reporting. Also, Azimli and Cek (2023), by examining 5,678 companies in the United States from 2015 to

2022 and using regression analysis, stated that companies located in environments with greater social capital face easier conditions in debt contracts.

The quality of financial reporting reflects the accuracy and truthfulness of financial reports in expressing information related to the company's operations, especially expected cash flows, in order to inform investors. According to the Financial Accounting Standards Board (FASB) Concept Statement No. 1, financial reporting should provide useful information that helps actual and potential investors make rational decisions. The degree of conservatism in preparing financial reports or the quality of accruals presented in these reports is criteria through which the quality of financial reporting can be measured (Agustia et al., 2020). The existence of transparent and reliable financial information is one of the main factors in assessing the current situation and performance of a company in its activities, as well as making decisions about trading its securities. In today's economic environment with the presence of diverse economic actors and the complex structure of economic relationships between them, reliable information is considered to be prepared, presented, monitored and commented on by a professional group with complete honesty and adherence to family, religious, etc. values. A prominent example of oversight groups are audit firms, which mainly examine and monitor the internal control structure of the reporting entity and its final product, namely financial statements, and express an opinion on this matter. Therefore, audit quality is very important because it allows high-quality financial statements to be monitored (Hasan et al., 2020). Today, auditors have their social status, Because they have a social duty to protect their clients and other stakeholders against any improper performance and distortion by managers. In order for this status of auditors not to be damaged, they are expected not to work for their own personal gain in economic terms. Rather, they always observe independence, honesty, and integrity in order to promote the public interest (Monsen., 2022).

The increasing expansion of economic units, the development of communication technology, and the existence of conflicts of interest create regulatory needs. The issue of economic globalization and the information revolution has caused the auditing profession to gradually try not to lag behind and move in line with the needs of society in line with technological changes. In this environment, users need various information including financial information about economic enterprises, to make decisions. Financial statements are considered the most important set of financial information. However, an important issue is the doubt

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about the reliability of this information, which stems from conflicts of interest (Paternostro., 2021). In addition to conflicts of interest, other issues such as the lack of direct access of users to information have led to the demand for independent auditing services. In fact, one of the roles of auditing is to assess the quality of information for users. However, since audit quality is difficult to observe in practice, research in this field has always faced many problems (Bozanic., 2017). Audit quality is one of the important issues in the field of auditing and capital markets. In order to understand the concepts and different dimensions of audit quality, various studies have been conducted to discover the relationship between audit quality and its other variables. However, since audit quality is difficult to observe in practice, research in this field has always faced many problems. The auditing profession, like other professions, needs to gain public trust to maintain its position. What society expects from the auditing profession is to provide audit reports of desirable quality. This is the added value that only the auditing profession is able to add to the financial information of companies (Dakhli., 2022).

In recent years, the theory has been proposed that business should not only lead to profit and increase the wealth of shareholders, but should also accept responsibilities towards employees, the environment and society. This theory has become one of the characteristics of companies under the name of corporate social responsibility. Corporate social responsibility is the result of four components: economic responsibility, legal responsibility, ethical responsibility and humanitarian responsibilities (Lin et al., 2016). The European Commission considers corporate social responsibility to be a concept that, in addition to reporting business activities, includes issues such as environmental issues and social reporting and the company's interactions with multiple stakeholders. To summarize, corporate social responsibility can be defined as follows: Corporate social responsibility is the obligation to respond to and satisfy the expectations of external stakeholder groups, including customers, suppliers, distributors, environmentalists and residents of the location of the production or service unit, while protecting the interests of internal stakeholder groups, including owners or shareholders and employees of the unit (Rey., 2020). Based on the review of theoretical foundations and research background, the following study hypotheses were formulated as follows:

Main Hypotheses

1. There is a positive relationship between social capital and audit quality.

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2. There is a positive relationship between social capital and financial reporting quality.

Sub-hypotheses

1) There is a positive and significant relationship between collective trust and audit quality.

2) There is a positive and significant relationship between collective cohesion and audit quality.

3) There is a positive and significant relationship between collective identity and audit quality.

4) There is a positive and significant relationship between cooperation and mutual cooperation and audit quality.

5) There is a positive and significant relationship between empathy, understanding and mutual respect, cooperation and voluntary participation and audit quality.

6) There is a positive and significant relationship between networks and common norms and audit quality.

7) There is a positive and significant relationship between collective trust and financial reporting quality.

8) There is a positive and significant relationship between collective cohesion and financial reporting quality.

9) There is a positive and significant relationship between collective identity and financial reporting quality.

10) There is a positive and significant relationship between cooperation and mutual cooperation and financial reporting quality.

11) There is a positive and significant relationship between empathy, understanding and mutual respect, cooperation and voluntary participation and financial reporting quality.

12) There is a positive and significant relationship between networks and common norms and financial reporting quality.

Research Method

The present study is an applied and survey type that was used to collect information from three questionnaires. The statistical population of the present study is the certified accountants of Iraq, which includes all certified accountants. According to the Cochran formula, the sample size is 342 people. The following questionnaires were used to measure the variables.

Social capital: It was measured using the questionnaire of Villanova and Josa (2003). This questionnaire examines six dimensions of social capital, including 1-

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social trust, 2- networks and common norms, 3- cooperation and mutual cooperation, 4- collective cohesion and solidarity, 5- empathy, mutual understanding and respect, voluntary cooperation and participation, and 6- collective identity, which is organized into 31 items and scored based on a five-point Likert scale including: 1- strongly disagree, 2- disagree, neutral, 4- agree, and 5- strongly agree.

Audit quality: It was measured using the questionnaire of Nickel et al. (2013). This questionnaire has 16 items. It was scored based on a five-point Likert scale including: 1-strongly disagree, 2-disagree-neutral, 4-agree, and 5-strongly agree.

Financial reporting quality: It was measured using the Wen (2014) questionnaire. This questionnaire has 22 items. It was scored based on a five-point Likert scale including: 1-strongly disagree, 2-disagree-neutral, 4-agree, and 5-strongly agree.

Structural equations were used to analyze the data.

Research findings

Descriptive analysis of gender of research participants

Table 1: Gender description of the people participating in the research

Accountants		Gender
Frequency percentage	Frequency	
9.2	16	Female
90.8	158	Male
100	174	Total

Examination of Table 1. shows that 9.2% of accountants (including 16 people) are female and 90.8% of accountants (including 158 people) are male.

- Descriptive analysis of the level of education of the people participating in the research

Table 2: Descriptive of the level of education of the people participating in the research

			Education Level
Cumulative Frequency Percentage	Percent Frequency	Frequency	
9.2	9.2	16	Bachelor's Degree
85.1	75.9	132	Master's Degree
86.8	1.7	3	PhD Student
100	13.2	23	Doctorate
	100	174	Total

Examination of Table 2. shows that 9.2 percent of accountants (including 16 people) have a bachelor's degree, 75.9 percent of accountants (including 132 people) have a master's degree, 1.7 percent of accountants (including 3 people) are PhD students, and 13.2 percent of accountants (including 23 people) have a PhD degree.

- Descriptive analysis of the work experience of the people participating in the research

Table 3: Descriptive of the work experience of the people participating in the research

Cumulative Frequency Percentage	Frequency percentage	Frequency	Work Experience
0.0	0.0	0	Under 5 years
0.0	0.0	0	Between 5 and 10 years
14.9	14.9	26	Between 10 and 15 years
37.4	22.4	39	Between 15 and 20 years
63.2	25.9	45	Between 20 and 25 years
100	36.8	64	Over 25 years
		174	Total

Table 3 shows that 14.9% of accountants (including 26 people) have between 10 and 15 years of experience, 22.4% of accountants (including 39 people) have between 15 and 20 years of experience, 25.9% of accountants (including 45 people) have between 20 and 25 years of experience, and 36.8% of accountants (including 64 people) have more than 25 years of experience.

Reliability analysis of research constructs

Reliability refers to the ability of a measurement tool to maintain its stability over time. In simpler terms, reliability means that if we give the collection tool several times to the same group of people in a short period of time, the results obtained are close to each other. The reliability of the research measurement tool was also evaluated by calculating Cronbach's alpha coefficient and composite reliability coefficient (CR).

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Table 4: Examination of the average values of the extracted variance of each of the research components

AVE	Component Title
0.566	Social Capital
0.58	Financial Reporting Quality
0.563	Trust
0.517	Collective Cohesion and Solidarity
0.515	Cooperation and Mutual Collaboration
0.566	Shared Networks and Norms
0.556	Empathy Mutual Understanding and Respect Voluntary Assistance and Participation
0.601	Collective Identity
0.681	Financial Reporting Quality

Reliability Analysis of Research Constructs

Reliability refers to the ability of a measurement instrument to maintain its stability over time. In simpler terms, reliability means that if we give the collection instrument several times in a short period of time to the same group of people, the results obtained are close to each other. Measuring the reliability of the research measurement instrument has also been investigated by calculating Cronbach's alpha coefficient and composite reliability coefficient (CR).

Table 5. Examining the values of composite reliability coefficient and Cronbach's alpha for each of the research components

Composite Reliability Coefficient (CR)	Cronbach's alpha coefficient	Component Title
0.57	0.89	Social Capital
0.58	0.70	Quality of Financial Reporting
0.56	0.80	Trust
0.52	0.84	Collective Cohesion and Solidarity
0.52	0.80	Cooperation and Mutual Collaboration
0.57	0.81	Networks and Shared Norms
0.56	0.65	Empathy Mutual Understanding and Respect Voluntary Collaboration and Participation

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0.60	0.86	Collective Identity
0.68	0.62	Quality of Financial Reporting

Examining the results in Table 5 shows that the magnitude of Cronbach's alpha coefficients and composite reliability for all components are greater than their acceptable level (the acceptable level of Cronbach's alpha coefficients is 0.7 and the acceptable level of composite reliability coefficients is 0.6), so it can be concluded that the questionnaire constructs have desirable reliability.

Testing research hypotheses

Table 6: Results of testing research hypotheses based on structural equation analysis of the research.

Hypothesis test result	Probability of non-significance	Amara T	Path coefficient	Title of the study hypothesis
Not rejected at the 0.05 error level.	0.00	6.65	0.73	Main hypothesis 1: There is a positive relationship between social capital and audit quality.
Not rejected at the 0.05 error level.	0.00	10.91	0.24	Main hypothesis 2: There is a positive relationship between social capital and financial reporting quality.
Not rejected at the 0.05 error level.	0.00	7.04	0.77	Sub-hypothesis 1: There is a positive and significant relationship between collective trust and audit quality.
Not rejected at the 0.05 error level.	0.00	10.82	0.18	Sub-hypothesis 2: There is a positive relationship between collective cohesion and solidarity and audit quality.
Not rejected at the 0.05 error level.	0.00	11.59	0.33	Sub-hypothesis 3: There is a positive relationship between cooperation and mutual cooperation and audit quality.
Not rejected at the 0.05 error level.	0.00	10.49	0.11	Sub-hypothesis 4: There is a positive relationship between networks and common norms with audit quality.
Not rejected at the 0.05 error level.	0.00	10.60	0.11	Sub-hypothesis 5: There is a positive relationship between empathy, understanding and mutual respect, cooperation and voluntary participation with audit quality.

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Not rejected at the 0.05 error level.	0.00	10.52	0.13	Sub-hypothesis 6: There is a positive relationship between collective identity and audit quality.
Not rejected at the 0.05 error level.	0.00	3.18	0.51	Sub-hypothesis 7: There is a positive relationship between trust and financial reporting quality.
Not rejected at the 0.05 error level.	0.00	10.49	0.89	Sub-hypothesis 8: There is a positive relationship between collective cohesion and solidarity with financial reporting quality.
Not rejected at the 0.05 error level.	0.00	11.78	0.86	Sub-hypothesis 9: There is a positive relationship between cooperation and mutual cooperation with financial reporting quality.
Not rejected at the 0.05 error level.	0.00	10.01	0.80	
Not rejected at the 0.05 error level.	0.00	11.87	0.85	Sub-hypothesis 10: There is a positive relationship between networks and common norms with financial reporting quality.
Not rejected at the 0.05 error level.	0.00	10.36	0.90	Sub-hypothesis 11: There is a positive relationship between empathy, understanding and mutual respect, cooperation and voluntary participation with financial reporting quality.

Conclusion

The results of data analysis showed that there is a positive relationship between social capital and audit quality. There is also a positive and significant relationship between the subcomponents of social capital, namely, collective trust, collective cohesion and solidarity, collective identity, cooperation and mutual assistance, empathy, mutual understanding and respect, voluntary assistance and participation, and shared networks and norms, and audit quality. The results can be explained as follows: when audit team members cooperate and interact collectively and respect other team members, this causes them to recognize their professional identity and have empathy, which increases social capital and leads to increased audit quality. Structural social capital encompasses various forms of social organization, in particular roles, rules, precedents, procedures, and various types of network relationships that help to create cooperation and, in particular, efforts to carry out collective actions with common interests. Social capital represents common goals among members of a social system, a phenomenon whose absence leads to deviation from the goals. In fact, from this perspective, social capital arises from the mental processes of individuals and includes ideas imposed by culture and ideology, especially norms, values, attitudes, and beliefs, which help to create cooperative behaviors and collective action for common interests. Social capital is distributed and developed by structural capital and shows the extent to which network members have a common understanding and approach to performing tasks and achieving results. Social capital is reflected in social homogeneity, trust, loyalty, mutual cooperation, cooperation, conservatism, and the density of internal relationships. Social capital is explained by the entry and exit of individuals into the group and their factors, working relationships with the supervisory body, and the number of cooperative groups. A wide range of social science literature has studied this theory at all levels, individual, organizational, national, and international, and the evidence shows that social capital not only has a significant impact on improving social diseases and disruptions such as distrust, division, norm-breaking, self-interest, and the like, but also has a high explanatory power in the field of how to achieve growth and development, economic, well-being, creating legitimacy, and attracting political and public support. On the one hand, the results of data analysis showed that there is a positive relationship between social capital and the quality of financial reporting. There is also a positive and significant relationship between the subcomponents of social capital, namely, collective trust, collective cohesion and solidarity, collective identity, cooperation and mutual cooperation, empathy, mutual understanding and respect, voluntary assistance and participation, and networks and common norms and the quality of financial reporting. The results can be explained as follows: when accountants have collective cooperation and interactions and respect other accountants, this causes them to have empathy while recognizing their professional identity, which in addition to increasing social capital leads to an increase in the quality of financial reporting. The users of financial reports include a wide range of people in society, such as financial providers of companies, shareholders, investors, employees and company management. The most important tool for making economic decisions is financial reports and the figures contained in them, and the accuracy of these decisions requires the accuracy, quality and freedom from fraud of these reports. The largest source of information for shareholders, potential investors and suppliers of resources of companies for making decisions and economic future is the financial statements of companies. Therefore, in order to protect shareholders and other stakeholders and prevent future fraud, special attention should be paid to factors that reduce or increase the quality of information. The results obtained can be analyzed as follows: from an ethical perspective, it is assumed that socially responsible companies are more inclined to pursue ethical activities to achieve social welfare; therefore they have less incentive to carry out fraudulent activities. However, from an opportunistic perspective, companies with a desire to be socially responsible try to cover up their unethical activities. From a financial perspective, corporate social responsibility increases the profitability of the company because it increases the competitive advantage and quality of financial reports. Companies that are pioneers in reporting social responsibility in order to fulfill their responsibility to society also have better financial performance than other companies. Social responsibility reflects the ethical image of the company and can increase management's desire for the quality of financial reports. Socially responsible companies have a stronger internal control system than companies without social responsibility, which in turn increases the quality of information.

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