Audit from Audit Exempted Small and Medium-sized Entities (SMEs) in Sweden

Authors: Biswas Kaji Lakhe Shrestha
Honey Htun Wai

Supervisor: Catherine Lions

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Supervisor: Catherine Lions
Authors: Biswas Kaji Lakhe Shrestha and Honey Htun Wai
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Biswa Kaji Lakhe Shrestha
Honey Htun Wai

Dedicated to my late grandmother, Ganga Maya Shrestha. God rest her soul in peace.

-Biswa
Audit from audit exempted SMEs in Sweden

Abstract

Small and medium-sized enterprises (SMEs) are seen as backbone for economic growth because they are regarded as catalyst for entrepreneurial skills, innovation and employment. Since in Sweden approximately 99.89% of enterprises are SMEs, they take an important role in country’s economic development.

Most of the countries especially EU nations have abolished the statutory audit provision for (SMEs). The new Swedish legislation of statutory audit exemption came into effect on 1st November, 2010. In accordance with this new legislation, (SMEs) within two out of three following criteria; turnovers 3 million Swedish Kronor, balance sheet total 1.5 million Swedish Kronor and 3 total numbers of employees are exempted from statutory audit requirement. Despite the fact that audit exempted SMEs are voluntarily conducting financial statements audited.

As per above matters, this study finds the expected benefits of audit exempted SMEs in Sweden when they go for voluntary audited financial statements. In order to attain our research findings, this study chooses to conduct qualitative research method by semi-structured interviews with respondents from SMEs. Besides that, bankers’ opinion on audited financial statements and voluntary audits are discussed in order to complement our main research finding. When it comes to collect empirical data, we use convenient data sampling from Sweden, particularly in Umeå due to the cost and time limitations.

According to our empirical results, the expected benefits for audit exempted SMEs in Sweden voluntarily conducting their financial statements audit are as follow:

- Security with the audited financial information
- Right amount of tax paid to tax authorities
- Easy to get bank loan
- Better relation with creditors, investors and suppliers

In accordance with empirical results of bankers, we can confirm that bank will grant loan easily to clients who have their financial accounts audited. As a contribution of new knowledge we find that in Sweden, banks used credit scoring lending technique when it comes to grant bank loan. The interest rate determination is also relied on credit rating of companies. Companies who have good credit rating will be granted loan with lower interest rate. As for small companies who would like to get external financing from banks, the requirement criteria could describe as; audited financial statements, collaterals, business plan, owners’ grantee for loan repayment and good credit history.

Keywords: Audit demands, Audits for small and medium-sized entities (SMEs), Audit exempted SMEs, Bank loans, Swedish legislation of statutory audit exemption, Voluntary audits.
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Chapter 1

Chapter 1: Introduction

This chapter represents the introduction of research, problem background of the study, the research question and purposes of the study. In order to make this study attainable, limitation of study is also disclosed, besides for readers, definitions of the keywords are given and we will end the chapter with general disposition of the research.

1.1 Introduction of SMEs and Nature of Audit in Sweden

Small and medium enterprises (SMEs) take a significant role in the economic development of each nation around the world. SMEs are seen as backbone for economic growth because they are regarded as catalyst for entrepreneurial skills, innovation and employment. For instance in EU of 25 countries, about 23 million SMEs provide around 75 million jobs and represent 99% of all enterprises (European Commission, 2009). Despite this fact, SMEs most often encounter limited financial as well as non-financial resources. They do have less access to the public funds, which restricts them in obtaining capital or credit, particularly in the early start-up phase which ultimately results in less access to new technologies and innovation, so most often they depend upon the creditors like banks and other financial institutions, or private equity. In this regard, banks have become one of the prominent sources for SMEs fulfilling their financial requirements. According to Deakins et al. (2001), a majority of small firm manager-owners lack formal qualifications, financial skills and knowledge about financial control systems.

However, banks are less likely to provide loans without any reasonable assurance of creditability of the firms. Banks generally rely on the financial information of the firms. They do prefer credible audited financial statements by independent auditors as a matter of assurance. In other words, most banks view auditing as a guarantee for the quality of information disclosed in companies as well as a foundation for their credit rating process. Banks believe that the credit rating would be unsure without audit obligation Andersson & Paulsson (2005, cited in Ademi & Stigborn 2010, p. 41).

When the financial statements are audited, the companies can be benefited with lower borrowing costs from banks which ultimately help for higher returns from investments. In this regard, audit demand in firms is increasing day by day. To more extent, the statutory requirements by the government, the taxation authorities etc. for the audited financial statements have also contributed for the audit demand. The main objective of the statutory audit is to provide certified financial reports for the stakeholders of the companies (FAR SRS, 2007). Whether it is a small-scaled company having their accounts audited can enhance better information sharing within the company and transparent information disclosure for shareholders and other interested users. One might think auditing for micro and small-sized companies could be a financial burden.

At present, most of the countries especially EU nations have abolished the statutory audit provision for SMEs. Following the EU footprints, Sweden also implemented voluntary audits for SMEs effective from 1st July, 2010. According to (SOU, 2008) the companies which have turnover below 83 million Swedish Kronor, balance sheet asset total under 41.5 million Swedish Kronor and number of employees less than 50 can be qualify as small and medium-sized companies and exempt from statutory audit (SOU, 2008, p. 13). Those size criteria are consistent with 2008 EU maxima for audit exemption. This new legislation have made only 4
percent of the companies in Sweden mandatory for statutory audits, which means that the remaining 96 percent of the companies representing SMEs have an option not an obligation to audit or not to audit their financial statements (SOU 2008, p. 32).

However, on the 25th of March 2010, the Swedish government decided to significantly lower the limits for SMEs and that new legislation applicable after 1st November, 2010 (FAR Press Release, 2010-03-25). After 1st November, 2010, the requirement to audit applies only to companies in excess of at least two of the three following criteria: 3 million Swedish Kronor in turnover, 1.5 million Swedish kronor in balance sheet total assets, and three employees (FAR Press Release, 2010-11-01). However, the new legislation has given an option to the companies going for audit. The option is mainly aim for exemption from statutory audit and might relieve financial cost burden for SMEs (Collis et al., 2004, p. 87) and protection of too much information disclosed to competitors (Eierle, 2008, p. 491).

According to the data from (Economifakta, 2010), there were 981349 companies registered in Sweden. After a number of clear up done in terms of deducting form of ownership, legal form and traditionally public sectors there were 914043 companies registered in 2010. The following table presents the composition in total number of companies in Sweden.

<table>
<thead>
<tr>
<th>Types of Companies categorized by size</th>
<th>No. Of Employees</th>
<th>Share %</th>
<th>No. Of companies as at (2010.11.25)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sole proprietors</td>
<td>0</td>
<td>74%</td>
<td>676 302</td>
</tr>
<tr>
<td>Micro enterprises</td>
<td>1 to 9</td>
<td>22.2%</td>
<td>203 107</td>
</tr>
<tr>
<td>Small businesses</td>
<td>10 to 49</td>
<td>3.2%</td>
<td>29 202</td>
</tr>
<tr>
<td>Medium companies</td>
<td>50 to 249</td>
<td>0.5%</td>
<td>4 497</td>
</tr>
<tr>
<td>Large companies</td>
<td>Over 250</td>
<td>0.1%</td>
<td>935</td>
</tr>
<tr>
<td>Total</td>
<td>0 to 250</td>
<td>100%</td>
<td>914 043</td>
</tr>
</tbody>
</table>

Source: Economifakta for Year 2010 (Economifakta, 2010)

1.2 Problem Background
The EU fourth directive allows member states to exempt from statutory audit if they are qualifying small companies within their justification. The justification is using size test based on turnovers, balance sheet asset and number of employees. There are some entities which are qualified as SMEs even though they demand for auditing. Prior studies (Tauringana & Clarke, 2000; Collis et al. 2004) suggest that voluntary audits take part in controlling the conflict of interest between directors and shareholders. Collis (2010) indicate that management factors determining voluntary audit have an advantage of improved quality of financial information and better checking of accounting records and system. Moreover Collis (2010) finds that there is a significant relationship between voluntary audit and granting loans decision of banks but voluntary audit is not related with creditors or suppliers’ demands. (Collis, 2010, p. 227)

At present, accounting and auditing standards is also becoming more complex because of issues regarding harmonization and convergence of the standards. In July 2009, the International Accounting Standards Board (IASB) published the International Financial Reporting Standard (IFRS) for SMEs. This standard is intended to be applied by the entities which are not publicly accountable and publish financial statements with the general purpose for its external users. IFRS for SMEs are too complex with complicated accounting and reporting regulations, and comprehensive disclosures. The recent study done by Aamir & Farooq (2010) regarding the adoption of IFRS for SMEs, found that SMEs in Sweden are not
inclined towards IFRS for SMEs, and are not ready to adopt these standards, as SMEs are more familiar with the rules and principles applicable in Swedish GAAP. In this regard, cost of adopting the new standards would outweigh the benefits obtained. Collis et al., (2004) state that the higher cost of the audit, the greater the cost of saving if it is discontinued.

Tabone & Baldacchino (2003) say that in owner-managed companies, statutory auditing is required mainly because of information asymmetry between owner-manager and staff. Ownership management structure can also be one criterion when deciding to audit or not to audit. This factor is more stable and less sensitive from external influences than that of economic size measure turnover and balance sheet total (Tabone & Baldacchino, 2003, p. 388).

Large and small companies differ mainly because of their business strategy. Obviously large companies have more diffuse ownership structure and have more complex portfolio than small companies. Moreover, information asymmetries do exist and that problem is more severe in large companies than small companies and is reflected in the total value of the firm. Large companies demand for independent audit assurance service because reliable and transparent information has to be disclosed to external shareholders and all interested users (Collis & Jarvis, 2002, p. 101).

Numerous studies can be found in literature regarding the abolition of the statutory audit for most of the SMEs especially in EU nations. The main reason often outlined for exempting SMEs from statutory audit was the high audit costs than the benefits it derived. But this reason is still a matter of discussion. Besides abolition of the statutory audit for SMEs, results show that SMEs going for voluntary audit is quite high. Denmark is one of the good examples. The recent study conducted by L.R (2010, cited in Franzén 2010, p. 9) shows that about 78% of small and medium enterprises in Denmark has continued to conduct an audit of the financial information, despite not required by the law.

In regard to Sweden, a study by Svanström (2008) found that 68% of the respondents (SMEs) would continue to have their accounts audited when the statutory audit exemption comes into effect (Svanström, 2008, p. 287). In this circumstance, a question arises why SMEs are willing for having audited financial statements though it not required by the law. In search of answers to this question, one of the probable answers could be the expected benefits that SMEs get by voluntarily auditing their financial statements. If the higher cost of audit is the reason, why there is still a demand for audited financial statements brings up with the problem background, which needs to be addressed.

The next session will present formulation of research question of this study. The research question will be based on knowledge gap of prior studies. The accumulated research gap could be described as numerous studies have done research on audit demand for SMEs in UK, Germany and Denmark but there were few researches for Sweden. Even there were some researches for this subject matter in Sweden; most of them were carried out by quantitative analysis of publicly available data. Furthermore, there were few researches focused on different perspectives with different backgrounds regarding audit demand. More importantly, this study could be the first of its kind, especially after the statutory audit exemption legislation came into effect in Sweden.
1.3 Research Question

Our research question will be based on implementation of new legislation in regards to SMEs and research gap from prior studies. New legislation gives an exemption of statutory audit to SMEs in Sweden. Our research finding is:

**What are the expected benefits when SMEs in Sweden go for voluntary audited financial statements?**

1.4 Purpose of Study

This thesis will be focusing SMEs in Sweden since SMEs play most dynamic role in Swedish economy. The main idea of this study is to find the reason why SMEs demand voluntary audit since SMEs in Sweden has an option to do or not to do audit. To be detail, a prior study by Svanström (2008) finds that 68% of SMEs in Sweden would choose to have audited accounts even in the absence of mandatory requirement. With this regard, we would like to find the reasons behind why SMEs still conducting audits and what are the potential advantages and difficulties the SMEs might face and how do they plan to deal with it. As per these matters, our purpose is to find the expected benefits for choosing voluntary audit by the exempted SMEs despite not required by the law. Moreover, we would like to know how banks perceive the new audit legislation and voluntary audits of the SMEs. Those facts are the main motivations of this research.

The next section will mention the limitations of our research study.

1.5 Limitation of Study

- This research will be only focus in Sweden particularly in Umeå regarding with the limited time and cost perspectives.

- Regarding with the new legislation of audit exemption for SMEs in Sweden which came into effect by 1st July, 2010, this paper will define significance of SMEs as follow. The measure of small firms that is in terms of turnover maximum of 3 million Swedish Kronor, maximum of 3 employees and a balance sheet assets total maximum of 1.5 million Swedish Kronor. If the entity is matched with two out of three criterions above, it will be considered as small and medium scale entity and regard as our interested sample.

- When it comes to data sampling the target data sample will categorize into two respondent groups; representative from SMEs and bankers. At this point the research has limited opinions of audit demand from above two respondent categories.

- This research will not study regarding with each of every detailed explanation of auditing standards provided from ISAs (International Standard on Auditing). The research will be focused on SMEs’ willingness to have audited financial statements.

- Language barrier is one of the limitations for this study. When it comes to analysis disclosure statements of SMEs related with auditing, there might only be in Swedish Language since our interested group is not Multinational Corporations. Besides, language is also more or less difficult in interview session as most of the interviewees would be the Swedish nationalities, and language can also be one of the barriers when going through prior articles/ literatures written in other languages besides English.
1.6 Definition of Key Terms

**Small and Medium-Sized Entity (SMEs):** SMEs can be categorized into micro, small and medium-sized entities. Those entities’ sizes are measured by in terms of number of employee employed, annual turnover and annual balance sheet asset total. Moreover, different countries have different measuring scale in terms of annual turnover, balance sheet asset total and total employees employed for concerning SMEs.

**Small and Medium-Sized Entity (SMEs) in Sweden:** The category of micro, small and medium-sized entities in Sweden is made up of which have annual turnover under 41.5 million Swedish Kronor and/or an annual balance sheet asset total not exceeding 83 million Swedish Kronor and which employ fewer than 50 employees.

**Statutorily audit exempted Companies:** If an entity meets two out of three criteria given below than such company is statutorily not required to conduct audit effective from 1st November, 2010. The criterions are: i) Maximum of 3 employees, ii) maximum of 3 million Swedish Kronor turnover, and / or iii) maximum of 1.5 million Swedish Kronor balance sheet asset total.

**Auditing:** Auditing is a well-planned process of objectively attaining and evaluating evidence concerning assertions about economic events and actions to make sure the extent of correspondence between those assertions and launched criteria. And the evaluated outcomes have to communicate timely and effectively to interested users. (Eilifsen et al., 2006, p. 11)

Hussey (1999) said that “an audit is an independent examination of, and subsequent expression of opinion on, the financial statements of an organization” (Hussey, 1999, p. 33).

**Statutory Auditing:** The entities which have to conduct financial accounts audited required by law. In other word especially in European countries the entities that fail to qualify as SMEs and have to have audited financial statements regarding with countries’ law and regulations. Statutory audit is an external audit that involves ‘an independent examination of and the subsequent expression of opinion on, the financial statements of an organization’ (Owen et al., 2005, p. 34). When an entity conducts audit of their financial statements as required by law, it is called statutory auditing.

**Voluntary Auditing:** The entities which qualify as SMEs but have an option to audit or not to audit. Voluntary auditing means the entities which have exempt of auditing but prefer to have audited financial statements. When an entity conducts external audit despite not required by the law, it is called voluntary audit.

**International Auditing Standards (IASs):** Auditing standards are the guidelines and measures of auditors’ performance. Auditing standards assist make sure that audited financial statements are conducted in systematic way and obtain credibility and reliability (Eilifsen et al., 2006, p. 33).
1.7 Disposition

The rest of our research study will be structured as follows:

**Chapter 2 (Methodology):** This chapter represents the methodology choice of this research study. In order to reflect our research interest this chapter will design our research by choosing strategy and method for data collection.

**Chapter 3 (Theoretical Framework):** In this chapter we will review relevant existing and prior literature. Based on the facts got from reviewing prior studies, the theoretical framework will be formulated. Consequently, theoretical formulation will be the backbone for practical findings and draw conclusions for our research question.

**Chapter 4 (Empirical Study and Findings):** This chapter will present the empirical findings from collected data from respondents. The finding will help to draw empirical conclusion and can then reflect our research question.

**Chapter 5 (Analysis and Discussions):** This analysis and discussion chapter will deal with empirical findings as a base and will analyze in order to get vivid results. Discussion section will share knowledge based on the analysis of the empirical outcomes.

**Chapter 6 (Conclusion and Recommendations):** This chapter will respond the research question and draw overall conclusion for this study. Recommendations will be disclosed for further studies related to this subject matter.

**References**

The complete reference list is included in this section.

**Appendix**

The interview guides for SMEs and bankers will be disclosed.
Chapter 2

Chapter 2: Methodology

In this chapter of the thesis, we will explain the research methods we choose for the study and also the reasons behind choosing it. We shall base our attention on the choice of study, preconception, perspective, research approach, research methods, research design, data collection methods, data analysis and finally about the quality criteria and ethical considerations for the thesis.

2.1 Choice of Subject

Choice of subject is most often guided by the previous background, field of the study, backed by interests of the authors. Accounting and auditing being the subjects of specialization, the authors thought to find an issue that is related to their area. In this process authors find audit demand an interesting subject especially in relation to Small and Medium Enterprises (SMEs). More interestingly, the authors try to focus their area of study only in Sweden because of the new legislations of voluntary audit provisions for SMEs in Sweden effective from 1st July, 2010 which is quite new subject at present. Many studies have been found regarding audit demand and exemption of statutory audit for SMEs especially in EU. In Sweden most of the studies were done before 1st July, 2010, i.e. until the proposal of statutory abolition of audit for SMEs came into practice, that is why authors think to choose this subject to explore the audit demand despite statutory audit is exempted for SMEs.

As per the Regeringen, 2010 Swedish Government had predicted that the probability of SMEs keeping their auditors is high, because of the fact that auditing is a quality stamp for banks in their credit rating processes Regeringen, (2010, cited in Ademi & Stigborn, 2010, p. 21). It would be interesting to study this aspect to know the perspectives of SMEs’ for their audited financial statements though they are not statutorily obligated. Moreover, the perspective of other stakeholder like banks can contribute more for broader view about the subject.

2.2 Preconceptions

Writing a thesis is not an easy task. One must have a conception in advance. At most, the authors should remain as objectively as possible, and should possess an adequate knowledge or experience and a high degree of interest in the area of study before going for research on the subject chosen. Because, an author’s background can greatly affect the study, therefore it is important to know who have conducted the study. “Although it is not the authors’ meaning to have their own thoughts to affect the study it is not easy to avoid this” Patel & Davidson, (2003, cited in Franzén 2010, p. 5). Besides, social and cultural differences should also be taken account for removing negative consequences during the study.

Furthermore, one should be clear about the objective of the research. The objective of the study is to find the motives of the small companies for voluntary audit. Despite the fact of statutory audit exemption, studies show that the exempted companies are inclined towards conducting audit. This brings with a question in the authors’ mind why the companies prefer for audit and what are the expected benefits for voluntary audit brings up with the research question to be answered as a matter to fulfill the objective of the study.
Both authors are students of Umeå School of Business with specialization in Accounting and Finance, and have acquired some thorough knowledge in Auditing from the same program here at Umeå University. During the course and case studies, the authors have gained adequate knowledge about the demand of audit especially in relation to SMEs. Hopefully, this will make reading easier and understandable about the related theories that will be discussed later.

2.3 Perspective

In the views of Eriksson and Wiedersheim-Paul (1997, cited in Arey and David 2008, p. 7) perspective can be explained as ‘the point of view chosen to enable one focus on a problem from different dimension’. It is all the individual judgment that makes a difference on making a choice of perspective, as every individual’s way of looking upon reality and perceiving the reality is different due to identical nature of human behavior and socio-economic settings itself. Moreover, one’s perspective varies to others depending upon the discipline of the individual. So, it is desirable to have sound choice of perspective for better understanding of the subject matter for conducting a good research.

The authors want to look upon the Small and Medium Enterprises’ (SMEs’) choice for voluntarily audited financial statements. For addressing this issue, the authors will accumulate the perspectives of SMEs regarding their point of opinions for the financial statements get audited though not required by the law itself. Moreover, authors will also take into account opinions from bankers (banking personnel) for getting broader view of the subject matter. To address all the above perspectives the authors will view from auditing perspective based upon some theories related to auditing. The outcome of this study will hopefully contribute to SMEs and the stakeholders as mentioned earlier, about their perspectives regarding audited financial statements and what factors and aspects affects audit demand in Sweden.

2.4 Research Philosophy

Philosophy is a particular set or system of beliefs resulting from the knowledge and understandings about the world. According to Saunders et al., (2009), “the research philosophy relates to the development of knowledge and the nature of that knowledge”. The philosophy adopted in a dissertation will influence the assumptions on the facts, theories and general implications of the research (Saunders et al., 2009, p. 107-108). In this regard, the choice of philosophy plays an important role in selecting the best and appropriate research design to answer the research questions. Sobh and Perry (2006) argue that having the right research philosophy is crucial since it cuts the unnecessary activities that have no bearing to the research work.

The literature on business research methods considers two general philosophies. They are: the epistemological philosophy and the ontological philosophy. Epistemology relates with how it is possible to know about the world and reality, and what is regarded as acceptable knowledge (Saunders, 2009, p. 112). It addresses to the question of whether or not the social world can and should be studied according to the same principles, procedures, and ethos as the natural science (Bryman & Bell, 2007, p. 16). Epistemology can be further divided into two parts: Positivism and Interpretivism. Positivism is the position that advocates the application of the methods of the natural sciences to the study of social reality and beyond (Bryman & Bell, 2007, p. 16).
Positivism refers to the use of theory and tests that theory providing material for development of laws, the objective analysis of observable facts and a development of hypotheses which will end in a law-like generalization of these facts (Bryman & Bell, 2007, p. 16). The research outcome under this position to generalize requires samples of sufficient quantitative data out of the population and the sample size should also be representing the whole population. The next epistemological philosophy is interpretivism, just a contrast to positivism. Interpretivism shares a view that the subject matter of the social sciences – people and their institutions- is fundamentally different from that of the natural sciences (Bryman & Bell, 2007, p. 17). In this philosophy the researchers are allowed to understand the research problem from social actors’ subjective perspectives. Sometimes, when natural sciences method fails to answer the research question, the researcher may need to change his approach and methods, and adopt interpretative epistemological position so as to gain a new perspective on the subject in order to find the answer to the research question. So this approach has the capacity to come up with surprising findings when positivism approach becomes unable to find the answer.

On the other hand, the ontological philosophy refers to the subject of existence. It concerns the nature of the world and human being in social contexts (Bryman & Bell, 2007, p. 22). It deals with nature of the world and what we can know about it. The ontological philosophy can further be divided into two parts: Objectivism and Constructionism. Objectivism is an ontological position that asserts that social phenomena and their meanings have an existence that is independent of social actors (Bryman & Bell, 2007, p. 23). While constructionism is an ontological position which asserts that social phenomena and their meanings are continually accomplished by social actors (Bryman & Bell, 2007, p. 23). Objectivism gives an objective view of what reality is, while constructionism implies a subjective view to reality.

In our research, for the epistemological assumption we take the interpretivist position to interpret the approach of SMEs beliefs and expected benefits from audited financial information and for the ontological stance, we choose the constructionist view point. The constructionist view point will lead the authors in accomplishing their conclusive result as per the analysis of the knowledge acquired. Since the respondents are going to express their individual viewpoints based on their subjective judgment, this will be in support of the interpretive and constructional viewpoints.

2.5 Research Approach

Research approach is concerned with the way in which the researchers will collect data to answer their research questions (Saunders et al., 2009, p. 110). Basically, there are three different research approaches described in the literature; they are deductive, inductive and abductive approaches (Bryman & Bell, 2007, p. 11-14). Deductive approach is the commonest view of the nature of relationship between theory and research (Bryman & Bell, 2007, p. 11). In this approach, existing theories are used to base the study and the empirical observations are tested; use the hypothesis testing to derive its outcome. However, depending upon the findings, the hypothesis is either confirmed or rejected on the basis of which a new theory is formed or developed. The strong point of deductive is that, it tries to explain causal relationships between variables (Saunders et al., 2009, p. 125). Generally, in deductive approach a large sample size is required to enable the researchers to generalize their conclusions, and the nature of data collected are often quantitative.

On the other hand, in the inductive approach, theory is developed from the observations and findings of the research which are connected with certain enquiry that what reality is (Bryman
&Bell, 2007, p. 14). According to Bryman and Bell, the inductive approach relates more to the subjective research and qualitative strategy; it deals with collection of qualitative data for e.g. by conducting interviews. The collected data are analyzed and a theory is generated.

Deduction involves a process in which:
Theory → Observations/Findings

With induction the connection is reversed:
Observations/Findings → Theory

(Adapted from Bryman & Bell, 2007, p. 14)

As per Bryman & Bell, “it is useful also to think of relationship between theory and research in terms of deductive and inductive strategies as the issues are not as clear-cut as they are sometimes presented” (Bryman & Bell, 2007, p. 15). This brings forth an approach called abduction which is a combination of both the deductive and inductive approach. More simply it can be defined as:

Observations/Findings → Theory OR Theory → Observations/Findings

In this research, the authors shall use the inductive approach to answer the research question. This is because the authors think it is the best approach that has a link on research methods to answer our research question. The authors have aimed to understand the motives behind SMEs’ choice of voluntary audits, as well as studying the stakeholder’s perspectives like banks, in this regard. The motive here indicates the expected benefits SMEs get from voluntarily audited financial statements. Before answering the research question, firstly the relevant theories related to the audit demand, Small and Medium Enterprises (SMEs), and legislative provisions for SMEs will be discussed. On the basis of the theoretical framework related to the research, the interview guide will be prepared to collect the information from the interviewees that will facilitate in drawing conclusions. The research is based on understanding and explaining motives of voluntary auditing in SMEs, rather than describing and testing a theory, which is why an inductive approach is more suitable for this research.

2.6 Research Design

Research design can be described as logical framework of research and data relate to the criteria that are employed when evaluating the research. There are five different kinds of research designs: experimental design, cross-sectional or social survey design, longitudinal design, case study design and comparative design (Bryman & Bell, 2007, p. 44). Experimental design is implemented in true experiment findings which have strong internal validity and mainly use in quantitative research. Cross-sectional design is used when data collection for more than one case at the same time with two or more variables (Bryman & Bell, 2007, p. 54-55). The extension of cross-sectional design is longitudinal design and mainly applied in case study. (Bryman & Bell, 2007, p. 63) The comparative design deals with the study using similar two or more cases and attempts to make logic comparisons between them (Bryman & Bell, 2007, p. 66).

This research paper will conduct cross-sectional design. In this design our research questions will be responded through semi-structured interviews. This research study attempts to collect
data by face to face semi-structured interview with respondents from different areas and perspectives. Interview guide will be formulated based on prior and current literatures and will conduct interview with representatives from SMEs and banks. As per data collection method of cross-sectional research design, this study will collect data from different cases which mean the different perspective of respondents from SMEs and bankers from banking sector. More than one variable can describe as in our interview guides the interview question will be based on several variables what are found out from prior studies. So that we define different cases mean different opinion of voluntary audit from SMEs and bankers and more than one variable as several factors which are included in our interview guides. The main reason why conducting qualitative interview design for this research study is to understand the open interpretation from different perspectives why SMEs demand for auditing rather than what the significant figures could tell. Cross-sectional design helps us to analyze research finding more than one variable from different perspectives.

2.7 Research Strategy

There are two main strategies when conducting business research; quantitative and qualitative methods. Quantitative research can be described as a distinctive strategy dealing with collection of numerical data and finding the relationship between theory and research from deductive approach (Bryman & Bell, 2007, p. 154). Qualitative strategy focuses on words rather than quantification in data collection and analysis. It is an inductive approach of finding relationship between theory and research (Bryman & Bell, 2007, p. 402). Mixing quantitative and qualitative in the same research findings is called triangulation. It is aimed for convergence between those two methodologies and attempt to attain strong validity than using one methodology (Jick, 1979, p. 603). Another strategy is comparative research method which is looked for diversity among cases. The main intuition is to identify similarities and differences between cases and then attempt to advance new theory. The following table shows the fundamental differences between quantitative and qualitative research strategies:

<table>
<thead>
<tr>
<th>Fundamental differing facts</th>
<th>Quantitative</th>
<th>Qualitative</th>
</tr>
</thead>
<tbody>
<tr>
<td>Principal orientation to the role of theory related with research</td>
<td>Deductive; testing of theory</td>
<td>Inductive; generation of theory</td>
</tr>
<tr>
<td>Epistemological orientation</td>
<td>Positivism</td>
<td>Interpretivism</td>
</tr>
<tr>
<td>Ontological orientation</td>
<td>Objectivism</td>
<td>Constructionism</td>
</tr>
<tr>
<td>Data collecting and analysis</td>
<td>Structured, standardized, data condenser and data analysis through diagrams and statistics</td>
<td>Less structured, flexible and data enhancer and analysis through use of conceptualization</td>
</tr>
</tbody>
</table>

Source: adapted from (Bryman & Bell, 2007, p. 28, 426,482)

This research study has subjective view toward differences between people and objects of natural sciences. Qualitative strategy is chosen in order to align with ontological consideration of external realities. Since the formulation of research question, it is better to give feedback by words rather than what numerical data could. Regarding the strategy chosen, this research study will then conduct interviews with owners/managers from SMEs and authorized personnel from banks. The main reason for interviewing is to get better understanding related with subject matter. Moreover researcher can get closer learning from respondents that could help us to give better explanation for research question. By contrast the
research study has to be aware of not being too much subjective manner since qualitatively data collection greatly injected subjective human behavior.

2.8 Data Collection

Generally there are two kinds of data source; primary data and secondary data when collecting data for business research. The data that have already been collected, processed, stored for both descriptive and explanatory purposes are called secondary data. Secondary data can then be categorized into documentary secondary data, survey-based secondary data and multiple-source secondary data. The collecting modes of documentary data are journals, interview transcript, media account, voice recording etc. Questionnaire survey is mostly used to collect survey-based secondary data. And multiple-source secondary data is collected through by using documentary or survey-based or both of them for example financial times report of documentary mode or survey-based time series data (Saunders et al., 2009, p. 256-262).

The primary data can be described as first hand information collected by researchers for specific purpose. In order to give feedback for research question and align with the purpose of study, primary data is collected through observations, interviews and questionnaires. Observation can then be categorized into participant observation which is used in qualitative strategy and structured observation for quantitative data analysis. Qualitative matter of interviewing can be classified as semi-structured interviews, in-depth and focus group interviews, telephone and electronic interviews. Primary data collected through questionnaires are applied in both descriptive in order to describe variability in different phenomena and explanatory research for relationship explanation between variables. Questionnaire types can be divided into two categories; self-administered and interview-administered. In self-administered data are collected by designing questionnaires and send them to respondents. The collected data are normally analyzed by computer. Structured or standardized interviews are mostly used in this questionnaire data collection. It is different from semi-structured interviews and in-depth interviews in terms of defined schedule of questions of which interviewers could not deviate. Structured interviews are typically used in social survey research (Saunders et al., 2009, p. 360-365).

Data collecting for this study uses both primary and secondary data sources. When it comes to formulate interview guide, documentary secondary data source is used. Besides, research question motivation idea is somewhat based on prior literatures from journals, books, articles, e-forum in accounting and auditing field and other relevant electronic sources. Secondary data source is mainly collected from Umeå University library database. E-journal, articles, conference papers, publications and student papers are collected through Google scholar advanced (searching by keywords), EBSCO host (Business Source Premier, Emerald, etc.), and DiVA (research publication and student papers) from library database. In fact, using secondary data for this research is a matter of detective work. The main intuition using secondary data is to ensure overall suitability and data coverage for this study.

In addition, primary data source is also applied in order to answer our research question. Semi-structured interview is employed for primary data collection. This interview focuses on the response of experienced personnel banks and SMEs. Qualitative interview methods enhance greater flexibility, rich and detail answer from interviewee’s opinions. Since authors prepare semi-structured interview questions the study can generalize main findings and there is also a chance to get respondents’ free opinions. Moreover, interview questions will be formulated into completely open-ended questions when it comes to interview with
representative from SMEs in order that interviewees feel free to discuss the topic. Consequently, the researcher also get closer look on the research topic and attempts to get conformability of the findings. Besides, questions in the semi-structured interview do not need to follow exactly in the way outlined in the guide. Even interviewer can ask questions which are not in the interview guide. Those are the distinct characteristics that differ between structured and semi-structured interviews (Bryman & Bell, 2007, p. 472-475).

When it comes to respond research question authors use both secondary and primary data sources. Interview questions will be formulated at least 20 questions and interview time duration would be at least 30 minutes per each respondent. Interview guide will be sent to each respondent a week in advance. Face to face interviews will be carried out if the respondents are in Umeå. Authors will conduct interview by telephone conversation when respondents are outside of Umeå. Both face to face and telephonic interviews responses will be noted down and recorded in order to avoid missing data. Face to face interview rather has advantages than other interviewing methods for example can capture interviewee’ non-verbal gestures, can maintain rapport with respondents. The interview guide will be enclosed under appendix of this research study.

**Data Collection Method for SMEs’ Interview**

As the researchers have mentioned above, the primary data for the research would be collected through interviews with the companies and the bankers to get their opinions and perspectives for voluntary audit despite not required by law. The companies which fulfil at least two out of the three following criteria: maximum of 3 employees, maximum of 3 million Swedish Kronor in turnover, and/or 1.5 million Swedish kronor in balance sheet total assets are eligible for interviews. The next important condition is that, the exempted companies should be conducting audit at present to be finally qualified for interviews.

The websites www.eniro.se and www.rating.se are used to get the details of companies. The authors also contacted by phone to the responsible person at the head office (Stockholm) of the website ‘www.eniro.se’ to confirm whether the information provided in the site is reliable. The reply was that the information is reliable and is up-dated daily as provided by the companies. Besides, www.rating.se is used to confirm whether the information provided in www.eniro.se are correct or not, and also for getting furthermore information in case required. Only the companies within the Västerbotten (Umeå) is chosen for the study because of time and cost constraints for collecting the primary data. Companies with different business type will be chosen for more diversity in the companies and to get the collective perspectives from different business backgrounds. In the www.eniro.se the companies are categorized as per its business type. The authors went through most of the companies located in Umeå and checked their financial details, number of employees, their contact numbers and emails address.

The researchers selected 62 companies that meet the research criterion as mentioned above. The gathered information, especially related to the threshold criterion will be confirmed later at the time of interviews to avoid errors in data collected. In regard to this, the companies will be emailed with a request for the interview mentioning brief details about the purpose of research and time requirements. The interview guide will also be attached along the email for letting the prospective interviewees know about the questions in interviews. Besides, telephone call, door-to-door request also will be done to the companies requesting to participate in the research for timely and positive responses. The data collection would be stopped when 20 respondents’ interviews from the companies are conducted, due to time and cost constraints.
2.9 Sample Selection

Sampling and sampling methods depend on the feasibility and sensibility of collecting data to answer research question and align with the research purpose. “Population is a universe of units from which the sample is to be selected” (Bryman & Bell, 2007, p. 182). Sample units or co-domain of population can describe as representative of the population which can then reflect the characteristic of whole population and can draw conclusion on behalf of the population. Because of time and cost constraints, researchers do research on selected sample which can represent the entire population. There are two sampling techniques; probability or representative sampling and non-probability or judgmental sampling. Probability sampling is related with survey-based strategies and mostly used in quantitative studies. Non-probability sampling is aimed for in depth study for example case study and pilot survey. Under this sampling samples are selected based on researchers’ subjective judgment (Saunders et al., 2009, p. 213-243).

Probability sampling has to comprise specific sampling frame and sampling techniques can then categorize into random sampling, systematic sampling, stratified random sampling, cluster sampling and multi-stage sampling. When it is not possible to construct a sampling frame non-probability sampling technique can apply. This technique has five different sampling methods; quota sampling, purposive or judgmental sampling, snowball sampling, self-selection sampling and convenience sampling (Saunders et al., 2009, p. 213-243). This research study is relevant with non-probability sampling technique since the research purpose to select sample purposively and to get deeper understanding of respondents sample. Furthermore authors intent to conduct interview with 20 representatives from SMEs and 10 bankers. This can say as sample size is rather small with the intention that non-probability sampling would be suitable technique in sample selecting.

This study will employ purposive sampling and convenience sampling when selecting samples. The reason behind choosing purposive sampling is that there are pre-defined heterogeneous and homogeneous sample groups in authors mind. Authors want to get different explanations regarding research question from different opinion of respondents. That is heterogeneous nature of purposive sampling technique (Saunders et al., 2009). Besides, authors already pre-defined the sample group from different backgrounds. That means respondents from banks and SMEs. Bankers from banking sector and CEO or CFO, managers and/or accountants from SMEs are the pre-defined sub-group of sampling. It is a homogeneous nature of sampling which focuses on specific sub-group among different sample backgrounds (Saunders et al., 2009, p. 237-240).

Convenience sampling for this study means that regarding with geographical location. Authors are studying in Umeå School of Business, in order that authors intent to select sample particularly in Umeå. Perhaps this kind of sampling injects difficulty in terms of generalization the findings. There are four sources of errors have to aware when we do business research namely sampling error, sampling-related error, data collection error and data processing error. Since this study has subject judgment when choosing research strategy and because of convenient sampling, generalization and external validity of findings difficulty do exist. Besides, sampling-related error is of great concerned than other errors stated above for this qualitative study. Whereas, since this study is qualitative research findings as long as there has a greater extent of conformability criteria generalization problem might not be a great deal. And regard with the sample size of at least 25 respondents can generalize of our findings for master thesis 30 credits.
2.10 Data Analysis

When it comes to analyzing data qualitative strategy has a difficulty in finding analytic paths among richness of collected data. While quantitative data analyses have relatively clear rules for its collected data stream. Generally there are two approaches for analyzing qualitative data; analytic induction and grounded theory. Analytic induction is used when researchers want to give universal explanation of phenomena by pursing collected data until no deviation from hypothetical explanation already found (Bryman & Bell, 2007, p. 583). Grounded theory can be defined as “a theory derived from systematically gathered data and analyzed through the research process.” Developing theory out of data and iterative approach are two distinct features of grounded theory. Iterative approach is obtained by data collection and analysis repeatedly referring each other (Bryman & Bell, 2007, p. 585).

Data analysis for this study will conduct grounded theory approach. Concepts, categories, properties, hypothesis and theory are the product of grounded theory approach of data analysis. This research study is finding for the concrete concepts of why SMEs willing to have audited financial statement. Concepts can then analyze through coding processes in grounded theory. There are three coding; open coding, axial coding and selective coding within the approach. When it comes to answer our research question this study will apply open coding which can break down, examine, compare, conceptualize and categorize collected data from respondent samples.

2.11 Quality Criteria

Reliability, replication, validity are main criteria when the research is examined by quantitative method and the criteria related with trustworthiness and authenticity are greatly examined by qualitative study (Bryman & Bell, 2007, p. 39). Since this research study will be carried out by qualitative strategy, trustworthiness and authenticity are of great concern. Trustworthiness consists of four criteria; credibility, transferability, dependability and conformability which qualitative researchers have to aware. Each criterion can be defined as;

Credibility: Is a criterion which identifies the researchers’ findings is relevant with social world and can be acceptable to others. The respondent validation can say as a measurement criteria as to attain relevance and acceptance of our findings from others. When conducting interviews, authors have to ask same questions to all respondents and analyzing the data have to be the same procedure. In this regard respondents’ validation can then provide an indication of credibility to our study. This criterion is paralleled with internal validity of quantitative research (Bryman & Bell, 2007, p. 411).

In order to attain credible results, we will ask the same questions to the interviewees as per our interview guide.

Transferability: Is a criterion that judges the how much extend of researcher findings can transfer to other. This criterion is equivalent with external validity in quantitative studies (Bryman & Bell, 2007, p. 412).

In this study, research area is limited in Sweden so that our findings can obtain strong transferability in Sweden but it can be weak in other countries which have different rules, regulations and backgrounds.
Audit from audit exempted SMEs in Sweden

**Dependability:** This criterion is matching with reliability of quantitative studies. Reliability for qualitative studies means that researchers have to disclose the complete records throughout the research phases (Bryman & Bell, 2007, p. 414).

In this study, we will disclose the interview guides, list of respondents and their responses, the detail analysis process in order to get reliability of our research findings.

**Conformability:** This criterion is concerned with to make sure researchers’ personal values are not injected into research findings (Bryman & Bell, 2007, p. 414). Regarding with sample selection this study already has subjective nature so that when conducting we have to aware not to leading the interview flow by our own beliefs. When it comes to analyzing collected data we have to aware that not to inject subjective conclusion which could differ from the real findings.

With regard of intuition from interviewing, authors will use separate interview guides when interview with representatives from SMEs and bankers. First authors will interview with SMEs and then will list it down their responses. Thereafter what authors attempt to conduct interview with banker is to get confirm whether or not responses from SMEs are relevance with bankers’ perspective of audit demand for SMEs. By this attempt conformability of research findings could be have high extent.

In addition to the above four criteria qualitative researchers have to pay attention on authenticity criteria which is concerning the wider political impact of research. This criterion indicates that research findings are fairly represented or not, can help other people to get better understanding of social setting or not, can educate people or not and how extend researchers can contribute into society (Bryman & Bell, 2007, p. 414). When this research paper is finished, it will be accessed in Umeå University database so that it could be of help to interested users. The concluded findings will be sent to all interview respondents that could say as a little contribution into the society.

2.12 Ethical Considerations

Ethics is a vital issue in conducting a research. Ethics are norms or standards of behaviour that guide moral choices. The main goal of ethics in research is to ensure that no one is harmed from the research activities. Bryman & Bell, (2007) argue that ethical issues cannot be ignored, because they relate directly to the integrity of a piece of research and of the disciplines that are involved. So, when ethics are discussed in research, we often think about protecting the rights of participants, respondents or subject.

In this qualitative research, the authors collect primary data through interviews, and secondary data are collected from the literature related to the study. In regards to this, all the ethical issues will be considered during the research. During the research, the four main areas of ethical principles classified by Diener and Grandall (1978, cited in Bryman & Bell 2007, p. 132) such as: harm to participants, lack of informed consent, invasion of privacy and deception are well considered during the study. The secondary data used for the study are also well cited and referenced to avoid plagiarism. After all, the authors hope that the ethical issues are fully considered.

The following chapter will present the literature review of prior studies and based on its finding the theoretical framework of this research paper will be structured.
Chapter 3

Chapter 3: Review of Literature

The review of prior literature is presented in this chapter. The chapter begins with a short introduction about accounting and auditing aspects like provisions for accounting records, auditing, advantages and disadvantages of auditing. On the next part, overview of small and medium-sized enterprises will be provided. And then review of banking sector and its relation of audit demand for SMEs will be presented. After that, Stakeholder theory and each stakeholder’s role and their view of auditing will be discussed. Furthermore, agency theory and its framework for internal and external audit demand will be discussed. Thereafter internal and external audit demand will be given followed by statutory audits and voluntary audits aspects. At last, prior research related to the subject matter will be looked at to find the research gap and theoretical framework will then be structured for empirical findings of this research subject.

3.1 Accounting and Auditing

Generally, as a company comes into existence, it has to consider both accounting and auditing aspects. Accounting plays a role of maintaining all the accounts of business transactions in systematized way, whereas auditing plays a role of validating those accounted information. So, to know the real picture of a company, its business activities need to be well accounted and audited. In Sweden, companies are regulated by different Acts like, Accounting Act 1999, Auditing Act 1999, and the Company Act etc. A company is established under the Company Act. The Accounting Act talks about accounting issues, for example, provisions regarding maintaining book of accounts, and the Auditing Act is all about audit regulations for the companies. For auditing, the firms that are liable to close the accounting records by publishing an annual report should also engage an auditor. The audit implies that the auditor reviews the firm’s annual reports among other aspects (Giertz & Hemstrom, 2004).

3.1.1 Provisions for Accounting Records and Standards

According per Swedish Accounting Standards Board (BFN) website, Swedish accounting practices are mainly governed by the mandatory Annual Accounts Act (AAA) and the Accounting Act, supplemented by specific requirements for unlisted, listed and financial companies. The AAA incorporates with the European Commission’s Fourth, Seventh and Eleventh Directives.

The Accounting Act, 1999, the Second Chapter’s First Section affirms that all legal entities and individuals performing business activities are obligated to maintain accounting records where the value of their assets, calculated as per section four, exceeds 1.5 million Swedish Kronor (Norstedts Juridik, 2009, p. 8). The Fourth Chapter of the Act explains regarding the contents of the obligation to maintain accounting records; the First Section states that, an undertaking must maintain regular accounts of all business transactions in accordance with the provisions mentioned therein (Norstedts Juridik, 2009, p. 11).

According to the Sixth Chapter’s First Section of the Accounting Act, firms need to close their annual accounts with an annual report and publish them in accordance to Section Two.
The annual report consists of a profit and loss account and a balance sheet, as mentioned in the Sixth Chapter’s Fourth Section of the Accounting Act. Such firms must satisfy one or more of the following conditions: a) the average number of employees exceeds 50; b) the firm’s reported balance sheet total exceeds 25 million SEK; and c) the firm’s with net turnover exceeds 50 million SEK (Norstedts Juridik, 2009, p. 14). However, firms other than referred in Section One of Chapter Six shall, where an annual report is not prepared, close the current accounting with annual accounts, and with annual turnover not exceeding 3 million Swedish Kronor are not obligated to prepare annual reports pursuant to Section One (Norstedts Juridik, 2009, p. 15). Such firms may prepare simplified annual accounts pursuant to Section Ten of Chapter Six (SFS 2006: 874, cited in Norstedts Juridik, 2009, p. 15). As per Chapter Six’s Section Ten, a simplified annual account consists of a profit and loss account and a balance sheet, and it is prepared pursuant to GAAP. Chapter Two, Section Seven of the Annual Reports Act (SFS 1995:1554) shall apply in pertinent parts to the issue of signing of annual accounts (SFS 2008:90, cited in Norstedts Juridik, 2009, p. 17).

As per the Annual Report Act, the annual report should be prepared in a clear manner and in accordance with generally accepted accounting principles. It is the responsibility of the Swedish Accounting Standards Board (in Swedish BFN) for the development of generally accepted accounting principles and guidelines. EU has made mandatory to adopt full-IFRS for all listed companies in Sweden, however for unlisted companies including SMEs, they have to follow the Swedish GAAP. The International Accounting Standard Board (IASB) has also developed and issued separate International and Financial Reporting Standards (IFRS) for SMEs in July 2009. The IFRS for SMEs is a simplified, self-contained set of accounting principles that are appropriate for smaller, unlisted companies and is based on the full range of IFRSs (ISAB: IFRS for SMEs, 2009). This standard is for intended use in general purpose financial statements and reporting by small and medium-sizes entities, private firms and non-publicly accountable enterprises. The main reason for IFRS for SMEs is to improve the quality and comparability of SMEs financial statements all over the world and would be helpful for SMEs in gaining access to finance (Neag, Masca & Pascan, 2009, p. 1).

3.1.2 Auditing and It’s Role and Purpose

The Auditing Act (Sweden) is applicable on the firms that are obligated to close the accounts with an annual report according to Chapter Six, Section One of the Accounting Act (SFS 1999:1078, cited in Norstedts Juridik, 2009, p. 21). The regulation about auditing is also found in the Tenth Chapter of the Swedish Companies Act, as well as the tasks the auditor has to perform (The Swedish Companies Act, 1975: 1385, cited in Norstedts Juridik, 2009). Auditing implies examining firm’s annual reports and accounts as well as the management’s operations, done by the auditor (Section Five, the Auditing Act, cited in Norstedts Juridik, 2009, p. 21). The firms should have at least one auditor (Section Three, the Auditing Act, cited in Norstedts Juridik, 2009, p. 21). However, after the new legislation of exempting the SMEs of Sweden from statutory audit, this Act no longer applies to the firms.

Auditing, according to Eilifsen et al., 2006, p.11, “is defined as a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicating the results to interested users”. It is designed to demonstrate ‘the completeness, accuracy and validity of transactions which, when aggregated, make up the financial statements’ (Power, 1997, p. 24).
Generally, the purpose of auditing is to increase the credibility of firm’s accounts and reports. The audited financial information adds credibility to the report and reduces information risk, benefiting both the owner and the manager. It creates assurance about the reliability of information for managers, investors, creditors, and regulatory bodies in making decisions. It has been argued that auditing aims at fulfilling the public interest of verifying information (FAR SRS, 2006; Bruzelius & Skarvad, 2004; Baker, 2005). Power (1997, p. 5) states that: ‘Audit is a risk reduction practice’. An independent audit of internal controls can reduce information risk, inherent risk (the likelihood of a material misstatement arising) and control risk (the likelihood of the accounting control detecting any material misstatement), thereby reducing agency costs (Hossain et al., 1995; Watson et al., 2002; Prencipe, 2004).

3.1.3 Advantages of Auditing

Numerous literatures can be found that emphasize the advantages of auditing in a business. As pointed above, auditing can have significant effect on information risk. The reduction of information risk can have a significant effect on the borrower’s ability to obtain capital at a reasonable cost. In this regard, Brannstrom (2005) also argues that the auditing reduces risks for investors and facilitates firms to obtain capital. He further mentions that auditing reduces the possibility of crime, conscious errors. Auditing is a way for the Tax agency to ensure that the correct amount of tax is paid (FAR, 2005). Andersson & Paulsson (2005, cited in Ademi & Stigborn 2010, p. 21) explains why auditing makes it fairer for firms. He states that auditing is a tool to ensure solvency, and the ability to convey and confirm a firm’s financial status. He furthermore states that stakeholders like suppliers, creditors and customers need to feel sure with the firm and also being informed of potential financial crises in time. In this case, auditing is more useful for stakeholders such as banks, suppliers, tax authority, despite that the cost of auditing is only the firm’s expense (Thorell & Norberg, 2005b). Axenborg (2005) states that auditing also gives a better competitive advantage and increase standard of the accounting Axenborg, (2005, cited in Kaur, J. & Kurt, N. 2008, p. 40)

Adams, Bedard & Johnstone (1995) discusses that audited financial statements are needed to decrease the information asymmetry between managers and the owners. This is also studied by Moore & Ronen (1990); they discussed the usage of financial statements by potential investors. Their findings state that the benefit of an audit is greater if the company is in need for external funds. Guntert, (2000) argues that the small company audit gives the directors ‘increased confidence in the reported figures, the general financial position of the business, the financial basis for making decisions, the reliability of the accounting system and the information it produces and the early identification of trends that could lead to failure’. (Guntert 2000, p. 75-76) These views are also supported by empirical evidence from the UK (Collis et al., 2004).

3.1.4 Disadvantages of Auditing

In the literature, we can also find arguments against the auditing, mostly related to the cost and benefit issues of auditing. In this stance, Thorell and Norberg (2005b) argue that the costs of auditing exceed the benefits of it, in small firms. They state that benefits are hard to appreciate, while it is less complicated to calculate the cost of auditing. They also find out that auditing exists due to owners’ aspiration for an independent review of their firm. Furthermore, small firms’ owners are the one who runs the business. In this respect, auditing is mainly useful for stakeholders such as banks, suppliers, tax authority, despite that the cost of auditing is only on the firm (Thorell & Norberg, 2005b).
3.2 Small and Medium Entities (SMEs)

3.2.1 Definitions of SMEs

The definition of SMEs is different between countries and regions. Generally, indicators like capital, earnings, turnover, balance sheet total, numbers of employees etc. are used to define SMEs. As per OECD, SMEs are defined as non-subsidiary, independent firms which employ less than a given number of employees; and this number differs across national statistical systems (OECD, 2000).

The definition for SMEs has been changing since years ago in EU. “The new SME definition – user guide and model declaration” and the directive (2003/361/EC; EU, 2005) have been issued by the EU for clear and broader definition of SMEs. In its way, European Commission defines SMEs as companies with less than 250 employees and which have turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million (European Commission, 2005, p. 5). Furthermore, EU has also considered independence issue as one of the basic criterions for an enterprise to become a SME. A SME can be said as independent, if it is not more than 25% owned or controlled by another enterprise or jointly by several enterprises which are not themselves SMEs. EU further defines SMEs into three categories such as: Micro-, Small-, and Medium-sized enterprises which are explained below:

- **Micro Enterprises**: The firms with less than 10 employees, annual turnover not more than 2 million EUR, and/or balance sheet assets total not exceeding 2 million EUR.

- **Small Enterprises**: The firms with employees less than 50 persons, annual turnover not more than 10 million EUR, and/or balance sheet assets total not exceeding 10 million EUR.

- **Medium Enterprises**: The firms with less than 250 employees, annual turnover not more than 50 million EUR, and/or annual balance sheet assets total not exceeding 43 million EUR.

### Table 3: Classification of Enterprise in EU

<table>
<thead>
<tr>
<th>Enterprise Category</th>
<th>No. of Employees</th>
<th>Turnover or</th>
<th>Balance Sheet</th>
</tr>
</thead>
<tbody>
<tr>
<td>Medium-sized</td>
<td>&lt; 250</td>
<td>≤ € 50 million</td>
<td>≤ € 43 million</td>
</tr>
<tr>
<td>Small-sized</td>
<td>&lt; 50</td>
<td>≤ € 10 million</td>
<td>≤ € 10 million</td>
</tr>
<tr>
<td>Micro-sized</td>
<td>&lt; 10</td>
<td>≤ € 2 million</td>
<td>≤ € 2 million</td>
</tr>
</tbody>
</table>

*Source: European Commission, 2005.*

As per the International Accounting Standard Board (IASB, 2009), *‘the Small and Medium Entities (SMEs) are those enterprises which are not publicly accountable and thus publish financial statements with general purpose for its external users’. These external users can be the non-managerial owners, current and prospective creditors and credit-rating agencies that are directly as well as indirectly related to the enterprise. A non-publicly accountable entity is defined by IASB as an entity: whose shares are not publicly traded, that is not a financial institution or an essential public service, and that is not economically significant in its own country. IASB quotes ‘general purpose financial statements are those intended to meet the needs of users who are not in a position to demand reports tailored to meet their particular*
information needs’. IASB has categorized SMEs into three types, such as micro, small and medium-size enterprises with following basic requirements:

- Companies without public accountability, and
- Prepare general purpose financial statements for external users (IASB, 2009).

3.2.2 Significance of SMEs

SMEs are generally regarded as one of the most important sector of a nation’s economy. Hillary (2000) states that, SMEs are the main players in an economy to provide and create jobs, especially during recessions; SMEs are also seen as a source of innovation and entrepreneurial spirit with better future of the business in the competitive (Hillary, 2000, p. 11).

According to data from Eurostat, SMEs constitute 99.8% of the total amount of enterprises in the non-financial sector, employing 67.4% of the European workforce employment. These figures indicate how significant SMEs in the EU are. An increasing body of literature indicates that small and medium-sized enterprises (SMEs) are of major importance for macro-economic growth. (European Commission, 2009, p. 8) SMEs are often referred to as the backbone of the European economy, providing a potential source for jobs and economic growth. The 20 million SMEs in the EU represent 99% businesses, and are a key driver for economic growth, innovation, employment and social integration (European Commission, 2009).

In regard to Sweden, SMEs constitute 96% of the total amount of enterprises, employing around 60% of workforce in Sweden (SOU 2008, p. 32). According to the data from (Economifakta, 2010) there were 981349 companies registered in Sweden. After a number of clear ups done in terms of deducting form of ownership, legal form and traditionally public sectors there were 914043 companies registered in 2010.

3.2.3 SMEs financing methods and problems

SMEs take an important role in today’s entrepreneurial economy likewise Swedish SMEs can say as a backbone of future development of the Baltic regions. SMEs most often encounter limited financial as well as non-financial resources. They do have less access to the public funds, which restricts them in obtaining capital or credit, particularly in the early start-up phase which ultimately results in less access to new technologies and innovation. Due to this, financing can have direct impact on the long turn survival of SMEs. According to Abouzeedan (2003), SMEs’ financing sources are from internal sources, informal external sources, financial intermediaries (debt financing and equity financing), public markets and government agencies. Internal sources mean financing come from owners’ saving, business retained earnings and depreciation. Informal external financing is from friends and business associates. Financial intermediaries mean the financing from banks and finance companies. To be detail debt financing is using banks as financial intermediaries and equity financing venture capital funds as their capital provider.

The following table shows the financing sources of Swedish SMEs and their financial cost level and long-term survivability.
Table 4: Swedish SMEs financing methods, sources, costs and their affect on survival index value level of the firm

<table>
<thead>
<tr>
<th>Financing methods</th>
<th>Financing sources</th>
<th>Financial cost level</th>
<th>Expected survival index value (SIV) level</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal financing</td>
<td>Owner savings</td>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td></td>
<td>Business returned earnings</td>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td></td>
<td>Depreciation</td>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td>External informal financing</td>
<td>Friends</td>
<td>Medium</td>
<td>Medium</td>
</tr>
<tr>
<td></td>
<td>Informal business associates</td>
<td>Medium</td>
<td>Medium</td>
</tr>
<tr>
<td>Financial intermediaries (debt financing)</td>
<td>Commercial banks</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td></td>
<td>Non-commercial banks</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td>Financial intermediaries (equity financing)</td>
<td>Venture capitalist</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td></td>
<td>Financial companies</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td>Public markets</td>
<td>Factoring</td>
<td>Medium</td>
<td>Medium</td>
</tr>
<tr>
<td></td>
<td>Disintermediation</td>
<td>Medium</td>
<td>Medium</td>
</tr>
<tr>
<td></td>
<td>Stock markets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government agencies</td>
<td>NUTEK (The Swedish business development agency)</td>
<td>Medium</td>
<td>Medium</td>
</tr>
</tbody>
</table>

Source: Adapted from Abouzeedan (2003, p. 13)

Swedish SMEs major sources of financing are from bank loans and future retained earnings. But these sources cannot fulfill the SMEs requirement thus why started using alternative ways of financing for example venture capital funds and factoring. The lender especially the banks intend to lend short-term loans with high interest rates because of security reasons. Compared with large corporations SMEs are in risky zone with higher default risk case. The major financing problems of Swedish SMEs are limited self-financed capital, difficulties to get bank loans for weaker group, banks intend to lend larger loans than smaller loans under 100,000 Swedish Kronor and greater security requirements. Limited self-financed capital is mainly because of double taxation effects; personal tax and corporation tax. Because of limited information provided from SMEs, banks prefer to lend to other firms which have better information sharing and publicly available disclosure. Even when banks lend loans to SMEs the interest rate will be higher in terms of security reasons (Abouzeedan 2003, p. 12).

3.2.4 Auditing for SMEs: Benefits or Cost burden

Blackwell et al., (1998) investigate that the value of auditing to private firms by examining cross relation of voluntary purchase of audit and interest rate they pay. They find that auditing reduces the lenders’ monitoring cost, increasing voluntary audit that can attain lower audit fees in terms of competitiveness, and improves the creditability of financial information for external capital providers. Auditing has a long tradition when it comes to discuss the internal controlling by supporting client management using unbiased advice (Carey, 2008). Since SMEs are smaller in terms of sizes, concentrated ownership structure and fewer employees
than large firms, the quality and adequacy of internal control system can bring great benefits to the firm.

According to Carey (2008), there is a significant positive relation between firm’s owners not involved in management and external audit demand. In this regard Carey states that auditing as a valued monitoring mechanism of the firm. But related with lower interest rate pay to lender, Carey studies Australian SMEs and banks that their relations do not give the significant result. Moreover, the study also mentions that Australian banks do not vary their loan pricing, when Australian SMEs whether go for voluntary audit or not (Carey, 2008, p. 37). However, Kaur et al. (2007) find that auditing has been used to limit frauds and illegal acts, to get better granting loans and longer loan duration and loyalty. They also discuss that benefits for SMEs regardless of the abolishment of audit is to uphold credible and attempts to build good image with investors and users. The approximate annual cost of audit fees in Sweden for SMEs as 10,000 Swedish Kronor. When the firm’s financial statement is reliable and lack of material misstatements, the benefits attained will outweigh its cost incurred (Kaur et al., 2007).

3.3 Banking

In this literature review section authors will present the prior studies which are related with the relationship between banks’ lending techniques and SMEs. Numerous academic papers argue that large and foreign banks are not interested to deal business with SMEs while only small and niche banks have intention to serve SMEs because they believe that to overcome SMEs opaqueness by using relationship banking technique. This opaqueness means that it is difficult to ensure if the firms have capacity to pay and/or willingness to pay back their obligations. Regarding this argument, Torre et al. (2010) show that banks (small, large, domestic and foreign) perceive SMEs as a core and strategic business in today’s business world. Consequently the SMEs’ market is increasingly competitive. Not only small and niche banks intend to serve SMEs, large and foreign banks are also willing to do business with SMEs by using new technologies, business models and risk management systems when it comes to track SMEs’ financial and non-financial data. Moreover, the reason behind why large and foreign banks intend to invest or grant loan to SMEs is to diversify their business portfolios by means of lending credit to new types of firms and deriving incomes from non-lending activities (Torre et al., 2010, p. 2285).

Financial intermediaries (banks) need reliable and accurate information about the borrowers when it comes to decide whether to lend or not. Reliable information is not always publicly available. Especially for small firms which have fewer stakeholders than large firm, information sharing of SMEs could say as weak. According to Ashton & Keasey (2005), lending decision making is important to the operation of SME banking services and it relies on the different lending techniques used by banks. Bass & Schrooten (2006) also mention that the choice of lending technique is important for cost function of the bank. These costs could describe as monitoring cost to borrowers, cost of refinancing credit and bad loans which mean that the cost of lending to borrowers who cannot pay back their credit (Bass & Schrooten, 2006, p. 128).

3.3.1 Lending techniques of bank

According to Bass & Schrooten (2006); Ashton & Keasey (2005) lending techniques of banks can be categorized into four different categories. These are relationship lending, financial statement lending, asset based lending (credit collateral) and credit scoring. Relationship
lending is a method of lending decision making based on the relationship between banks and SMEs. The other three lending methods namely financial statement lending, asset based lending and credit scoring can be termed as transactional lending technologies. These lending methods are based on firm’s audited financial statements, firm’s collateral assets and accurate and reliable information of the firm and the owners.

**Transactional lending techniques**

Financial statement lending decisions are made from the strength of firm’s balance sheet total and income statements. This lending technique requires transparent information of the firm and its financial statements are independently audited. Bass & Schrooten (2006) term this information requirement as hard information of borrowers’ firm. This type of lending technique is mostly applied to larger firms which have long histories and their default risk occurrence seems quite low. And from the cost perspective, this technique might be costly for small firms.

Asset based lending decision is based on the quality of collateral for a loan, such as firms’ inventory, account receivable and for SMEs collateral could also be owners’ personal wealth such as land, building, etc. High level of collateral has to be pledged for this lending technique. This collateral lending technique is suitable for all types of firms but from the banks’ point of view, this could be an expensive technique when it comes to monitor the ongoing value of the collateral (Ashton & Keasey, 2005, p. 479).

Credit scoring method is applied by using statistical techniques to analyze the firm’s data. Under this lending method banks require lots of information from firms regarding audited income statement and balance sheet total, and soft information for example: history of firms, reputation, and prior lending experience of the firm. In this regard authors could say as credit scoring methods require both soft and hard information of borrower firms. This lending technique is widely used for consumers lending and its intensive data requirement nature comes to match for listed large firms with long history and large extent of publicly available information. Because of cost, intensive data requirement and high level of collateral have to be pledged. Besides that, Ashton & Keasey, (2005) argue that transactional lending techniques are probably not suitable for SMEs which are new in the market and default risky nature of its firm (Ashton & Keasey, 2005, p. 479).

**Relationship lending decision making**

The relationship lending decision making is employed for small firms in order to overcome the difficulties arise from transaction lending methods and risky nature of SMEs when it comes to finance them. This lending technique is also beneficial for banks when it attempts to overcome the problems arising from banking activities including adverse selection, information asymmetry, potential costs occurrence from transaction lending methods, monitoring of debtors and intermediation risks (Ashton & Keasey, 2005). Relationship lending technique is built by repeatedly communicating and contracting between banks and firm. The longer the relationship, the greater incentives of banks will be attained to make investing and lending for developing SMEs. Because of longer communication aspect banks get the exclusive access of the firm’s financial data and intensive soft data or the owner’s personal data and the firm’s position in the market.

Another aspect of lending method under relationship lending is the cross subsidizing, which flows from deposit from firm and then credit provision will be obtained from banks. The longer relationship between bank and firm grant cheap core deposit for the firm and in return,
the firm can get the credit provision from the bank (Ashton & Keasey, 2005, p. 479). According to Torre et al., (2010), in developed countries which have better institutional environment relationship lending seems less favorable. Banks intend to finance SMEs by using other financing methods like factoring, leasing and credit scoring. Banks would like to count on well-functioning formal contract than collecting intensive soft information by closer look from longer informal communication (Torre et al., 2010, p. 2292).

Table 5: Lending techniques of banks

<table>
<thead>
<tr>
<th>Lending techniques</th>
<th>Efficiency</th>
<th>Requirement</th>
<th>Costs and benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial statement lending</td>
<td>Depends on the quality of available information and accuracy of financial statements audited.</td>
<td>Audited financial statements (Hard information)</td>
<td>Costly lending technique but reliable and accurate information can attain</td>
</tr>
<tr>
<td>Assets based lending</td>
<td>Depends on the reliability of collateral assets</td>
<td>High level of collateral assets have to pledge</td>
<td>No credit lost for lenders when borrowers fail to fulfill the obligation</td>
</tr>
<tr>
<td>Credit scoring</td>
<td>Depends on quality of information disclosure provided from firms and credible financial statement.</td>
<td>Audited financial statements and intensive soft information related with firm</td>
<td>Borrower firm’s credit rating will be high when they have reliable financial statements audited and transparent information</td>
</tr>
<tr>
<td>Relationship lending</td>
<td>Depends on the relationship tightness of banks and borrower firm</td>
<td>Closer review of borrower firm financial position and firm’s non-financial performance</td>
<td>Decreasing monitoring costs from banks. Investment opportunities, deposit and provision of credit, lower loan interest rate can obtain from banks</td>
</tr>
</tbody>
</table>

Source: Authors

3.3.2 The Swedish financial market

The Swedish financial market is made up of three major groups of companies namely banks, mortgage institutions and insurance companies. As per the following figure 1, banks take a significant role in financial market. In this regard, this study will review banking sector of Swedish financial market. The function of banks could describe as to accept deposit and provide credit, to set interest rates, to provide means of payment (e.g. mediation of payments the bank giro) and to diversify business portfolio (e.g. offering trading in futures and options) (Swedish Bankers’ Association, 2010).

The following figure shows the players on Swedish financial market and their percentage composition in that financial market.
There are four main categories of banks on financial market namely Swedish commercial banks, foreign banks, saving banks and co-operative banks. In December 2009, 117 numbers of banks are in Swedish financial market. The types and numbers of banks in Sweden will be presented in following table:

**Table 6: Type and number of banks in Sweden**

<table>
<thead>
<tr>
<th>Type of bank</th>
<th>No. of banks (2000 Dec)</th>
<th>No. of banks (2009 Dec)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Swedish Commercial Banks:</td>
<td>22</td>
<td>32</td>
</tr>
<tr>
<td>- Big four banks</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>- Former saving banks</td>
<td>9</td>
<td>13</td>
</tr>
<tr>
<td>- Other commercial banks</td>
<td>9</td>
<td>15</td>
</tr>
<tr>
<td>Foreign banks:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Subsidiaries</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>- Branches</td>
<td>19</td>
<td>27</td>
</tr>
<tr>
<td>Saving banks</td>
<td>79</td>
<td>53</td>
</tr>
<tr>
<td>Co-operative banks</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>124</td>
<td>117</td>
</tr>
</tbody>
</table>

As per the above table, big four banks could describe as Sweden’s leading banks in financial market namely Nordea, Skandinaviska Enskilda Banken (SEB), Svenska Handelsbanken (SHB) and Swedbank (Swedish Bankers’ Association 2010, p. 4).
3.4 Stakeholder Theory

Stakeholder theory states value maximization of the firm. Value maximization means that every single decision made from managers have to seek for long-term market value maximization of the firm. Stakeholder theory also implies that managers have to make decisions which are aligned with all stakeholders’ interest of the firm (Jensen, 2002). The role of auditing under stakeholder theory is to get true and fair view of the companies’ performance and financial position not only for owners but it means for all stakeholders of the firms.

Freeman et al. (2004) mention five arguments regarding primary value creating of stakeholders. The arguments are listed as follow:

1) The goal of maximizing shareholder value is pro-shareholder.
2) Creating value for stakeholders generate the apt incentives for managers to assume entrepreneurial risks.
3) If a single goal setting is difficult or impossible to attain that will bring governance and management failure.
4) It is easier to make stakeholder out of shareholder than vice versa.
5) Stakeholders have remedies in the presence of breach of contract or trust while shareholders do not have (Freeman et al, 2004, p. 366).

Stakeholders of a firm include owner, manager, investors, shareholders, creditors, customers, suppliers, government, etc. (EC, 2010). The following figure shows the firm and its stakeholders.

![Stakeholder model](source)

Source: Adapted from (FAR 2006, cited in Kaur et al, 2007)

**Figure2: Stakeholder model**

The stakeholder theory describes the relationship between a firm and its stakeholders. The managers of the firm have to be aware with stakeholders’ interests to maximize the market value of the firm. In order to get sound governance practice and transparent information for all stakeholders and other interested users, auditing can perceive as a governance mechanism (FAR SRS, 2006). Different stakeholders have different needs and demands from the firm. In this regard, it is important to observe what their interests and how do they think about the role...
of audit. Since this study is an attempt to get the expected benefits of SMEs when they go for voluntary audited financial statement, various stakeholders’ needs and their view of voluntary audit is of concerned. This study will explain the role of eight stakeholders mentioned above in the stakeholder model figure, their demands from firm and how do they perceive the audit.

Owner, shareholders and managers’ perspective:

The owner and shareholders who contribute the invested capital of the firm have a risk of losing it or else can get higher return than invested capital. In this regard the role of managing the whole organization takes a major role. If an organization has a sound management system and the agent (managers) who act on behalf of the owner and shareholders and seek for their best interest, there might not be risk for losing capital contribution. But if the manager just aims for personal interest and minds for personal wealth maximization, the owner and shareholder of the firm might not obtain the good result from it. In this regard, owners and shareholders view the audited financial information of the company as a monitoring and controlling mechanism. Since SMEs has less employees employed, small in terms of size and there is less separation of ownership and control, there is less problems than diffuse ownership structure of large corporation. But, the owner and shareholders view the voluntary audit as an assurance of business (Kaur et al., 2007).

Government perspective:

The government perceives auditing as a backbone of tax assessment. Since SMEs play dynamic role in an economy, the government might pay attention on generating and monitoring more information on SMEs for public good. This information could be used not only to get financing source for SMEs that can also help to improve taxation for nation wealth (Torre et al., 2010). The firm has to pay tax regard with audited financial statement income. In Sweden there are government associations which funded for SMEs in the early development stage. In order that can say as an opportunity to do business and taxation might not be a big deal. Moreover, government agencies believe that auditing as a monitoring tool and can eliminate the illegal act and fraud occurrence (Strömberg, 2005 cited in Kaur et al., 2007).

Creditors’ perspective:

If the company is not financed by owner the alternative way of funding the firm is from creditors (Ademi & Stigborn, 2010). In return, creditors expect the interest from the firm. Generally, the interest rate on loan depends on the loan amounts and the term structure. Since creditors take significant role in organization, their need and demand are of great concern. Moreover, creditors have to bare the default risk of the firm when it comes to lending. In this regard, the firm has to secure their financial position and trustworthiness when they attempt to borrow from financial institutions. In this respect, auditing takes the role of secure intermediary between lenders and borrowers relationship. This could say as creditors’ view of auditing (Kaur et al., 2007).

Customers and suppliers’ perspective:

The customer contributes the firm by buying products or services. The reliable information provided from the firm, quality, on time delivery and warranty services are of vital to the firms’ customers (Ademi & Stigborn, 2010). The suppliers who provide products or services to the firm, in turn want to get back assurance from the firm. In this regard, audited statements can say as a controlling statement for on time payment from customers to suppliers Bruzelius & Skärvad, (2004, cited in Kaur et al., 2007). Authors can say as audited statements are not
directly used by customers but when it comes to build concrete relation of suppliers and customers, audited statements can attain visibility and information transparency. The reliable and accurate information disclosure is more or less important when it attempts to get customers’ satisfaction.

**Employees’ perspective:**

The employees who look for salaries and other compensations from the firm that is in return of their performance contribution to the firm. If their compensation scheme is formed by financial performance of the firm, auditing can be a reliable mechanism for their performance contribution to the firm.

These are the role of stakeholders and their view of auditing.

3.5 **Agency theory**

The agency arguments do exist when there is a situation of separation of ownership and control. Separation of ownership and control means “ownership is vested in one group shareholders or owners but the controlling the day to day operation of firms is vested in a separate group that is management or managers who are hired by shareholders/owners in order to act on behalf of them”. (Ogden et al., 2003, p. 75) The agents (managers) do have more information than the principals about the firms. By using better information of the firms, managers attempt to behave for their personal interests than instead of shareholders’ wealth. That is called information asymmetry between managers (agents) and shareholders (principals) (Ogden et al., 2003).

Jensen & Mecking (1976) state that the cost of agency problem can be categorized into two main costs categories. First is the agency cost of managerial discretion because of separation of ownership and control. The cost is incurred when owners attempt to align managers’ interest and their interests. The second agency cost does exist between firm’s creditors and owners when the firm’s financing is supported by issuing additional debt capital. The owners of the firm attempt to choose the risky investment and that potential operational risk have to bear by creditors. Because of this conflict of interest between creditors and owners, agency cost of debt is exposing to the firm. Increasing the firm’s leverage and high probability of bankruptcy are the consequences of agency problem between the firm’s creditors and owners.

In order to align interests and close the gap of asymmetric information, shareholders used strategic incentives schemes for example financial or non-financial performance based compensation, bonuses, share compensation etc. Moreover, some owners/shareholders conduct contracting to managers and others monitoring devices. Auditing can be said as an independent monitoring tool for these agency problems. Regarding with those conflicts of interests, shareholders/owners bear agency cost in order to align interests and to get accurate information of the firms. One of those agency cost can be described as cost of audit for monitoring and control purpose. Independent auditing takes the role of monitoring firm’s financial performance, attaining credibility and solving the agency problem (Seow, 2001).

According to Jensen & Mecking (1976) agency cost can be defined as the sum of: 1) monitoring expenditure by the principal 2) bounding expenditure by the agent and 3) the residual loss. The principals incur monitoring costs when it attempts to align interests. For example owners establish the appropriate incentives to managers in order to act behalf of owners and their wealth maximization. Bonding expenditure of agent means that the contracting costs have to compensate to owners when agents fail to fulfill the contract.
requirements. The residual loss of agency cost means that the opportunity loss of owners/shareholders occurs because of agency conflict of interests. Watt & Zimmerman (1990) describe contracting costs as information costs, renegotiation costs and bankruptcy costs (Watt & Zimmerman, 1990, p. 135). As to mention in the momentary issue this residual loss from dysfunctional decision means the equivalent reduction in monetary value occurs because of agents fail to maximize the firm value and its shareholders wealth (Jensen & Mecking, 1976, p. 308).

Agency theory suggests that the demand for auditing is to signal the quality of firms for both existing and future owners and lenders. Numerous literature debates about differences between small firms and large firms in terms of reasons for audit and its consequences. There also have a limited credibility when it comes to audit the small firms, mainly because of the closeness of auditors-clients relationship. Seow (2001) describes the potential factors affecting the independence auditing of small firms that are frequent rotation of auditors, audit fees, audit service and non-audit service (e.g., consulting) to the same client and unqualified audit report which means that auditors fail to report the actual conditions of the firm mainly because of bounding between auditors and clients in the small content.

Regardless of the size of the company and even in the absence of mandatory requirement of audit, auditing can be seen as an assurance and tool for solving the agency theory for small firms (Chow, 1982). When small companies are financed by other financing sources instead of capital contribution from owners, auditing can be described as a security requirement from lenders (banks, bondholders, debt holders, etc.). Since lending or issuing loans to SMEs can be said as more risky in terms of higher potential default risk than large corporations. The intuition why SMEs go for independent audit is for security reason of their firm. When small firms have their accounts audited and have transparent information, the lenders, investors and shareholders might have better attitude toward the firms. This not only solves agency problems but also better credit rating from lenders and better investments from investors (Chow, 1982).

The following figure shows the relationship between agent and principal in relation to demand for audit.
Figure 3: Overview of the Principal-Agent Relationship Leading to the Demand for Auditing

Source: Adapted from Eilifsen et al. 2006, p. 8

3.5.1 Agency framework of external audit demand

Regarding with agency conflict, the demand of audit can be categorized into internal demand and external demand. These two types of demand will be discussed in detail in the next section. This section will review about the relationship of agency conflict mainly because of information asymmetry and separation of ownership and control, and how does it relate to the two types of audit demand. Chow (1982) findings indicate that the external demand happens when is to help control conflict of interests among firm managers, shareholders and bondholders. Firm characteristic is the significant criterion when it comes to demand for external audit. Agency cost consideration takes an important role when deciding to have external audit, and among agency cost factors, managerial cost is the most influencing factor for external audit demand (Chow, 1982, p. 287).

Moreover, Chow (1982) finds that the effects of leverage and accounting-based debt covenants and firm size are influencing factors for firms’ voluntarily demand for external audit. In regards of Carey et al., (2000) findings, external auditing even does exist in the family businesses. In terms of size consideration and owner managed firms, agency problems seem not serious than big size firms with diffuse ownership structure. The reason why this small size firms go for voluntary external audit is to have appropriate monitoring mechanism. In order that firms believe that they might get economic benefits of lower interest rate than non-audited firms when it comes to funding capital from non-family members Carey et al., (2000).
3.5.2 Agency framework of internal audit demand
The internal auditing can also act like external audit help to maintain cost-efficient mechanism for contracting between owners and managers (Adams 1994; Carey et al 2000; Watt & Zimmerman, 1990). Agency theory implies that if there is information asymmetry, internal audit can help to take controlling action between owners and managers. Regarding this, the internal employments of in-house auditors have better knowledge than outsiders so that cost-efficient and effective monitoring could enhance. But demand for internal audit is less likely occurred in firms which have complicated business operation and complex organizational structure. This kind of firms demand audit mainly because of external complexities and conflict of interests in principal agent relationship (Adams, 1994, p. 11).

According to Carey et al., (2000), both internal and external auditing serve as a monitoring mechanism for agency problems occurrence when audit is voluntary and costs and benefits of different approach can be taken. For listed companies, internal audit can say as a complement for external audit; in this regard, cost of external audit is less than other companies which only have external auditing. If the audit is voluntary and firm size is small, internal audit can say as a substitute in two ways. First, is because of audit fees perspective when internal auditors can give the similar service as external auditors when it comes to financial account audit. The fees of this internal auditor must be lower than the amount paid for external auditors so that firms can get cost savings. Second, since the firm size is relatively small and agency problems so to be lower than listed firms internal audit could be reasonable for monitoring and controlling function within firms.

The following section will present the demand for auditing and detail explanation of internal and external demand of auditing.

3.6 The Demand for auditing
There are a number of complementary explanations as to sources of demand for auditing (Chow et al, 1988). Eilifsen et al., (2006) explains that audits are often utilized in situations where they are not required by law, and audits were in demand long before laws required them (Eilifsen et al., 2006, p. 8). In fact, evidence shows that some forms of accounting and auditing existed in Greece as early as 500 B.C. (Costouros, 1978). This elicits that statutory audit requirements cannot only be accounted for audit demand.

Agency theory is seen as the base for explaining the demand for external auditing. Auditing is demanded because it plays a valuable role in monitoring the contractual relationships between the entity and its stockholders, managers, employees, and debt holders (Eilifsen et al., 2006, p. 7). Hay and Knechel (2004) argue that the demand for auditing is a function of the set of risks faced by individual stakeholders in an organization (management, shareholders, creditors, etc.) and the set of control mechanisms available for mitigating those risks. This implies that demand for the audited financial statements arise both from outside and inside the firm. While talking about audit, this dissertation will focus on the external auditing because the new legislation is about exemption of external auditing requirement for SMEs. Further discussions on demand for audit will be made both from external and internal perspectives.

3.6.1 External demand
Demand for audited financial statements can arise from parties outside of the company. They can be owners/shareholders, suppliers, investors, creditors, banks, government bodies etc. Principal-agent problem can be one of the reasons for the external demand of audit. These interested parties demand audit because it plays a valuable role in monitoring the contractual
relationships between them. As mentioned above by Hay and Knechel (2004), external parties like creditors, banks, suppliers, investors, etc. demand audit to reduce the risk involved with the company. In this regards, audited financial information is generally regarded as only the way for external parties to know and get informed about the company. In other words, it is only one way for additional monitoring; thereof extensive presence of auditing in such circumstances can be a cost-effective monitoring device.

3.6.1.1 Demand from owners / shareholders
Generally, there arises a conflict of interest between the managers and the owners of the company due to information asymmetry and different personal objectives as a result of principal-agent problem in the company. Managers serve as agents for the owners/shareholders (referred to as principal). In regard to this, Collis et al., (2004) found that demand for an audit appears where there is an agency relationship between the owners and managers of the company. Similar conclusions were also drawn by Senkow et al., (2001) mentioning that audit demand as the key reason in such circumstance. A study by Chow (1982) also shows a greater demand for audit in firms with agent relationships. Moreover, his finding indicates that in owner-managed companies there is a smaller demand for conducting an audit.

3.6.1.2 Demand from investors/banks
Literature also shows audit demand in relation to investors/banks. Investors like banks want to be sure that their investments are safe and the borrower is financially sound to pay back the loan with interest. Since ensuring that the business continues as a going concern is also important to lenders (Collins & Jarvis, 2002). For this, investors use audited financial information assuming that it is reasonably complete, accurate, and unbiased. Collis et al., (2004) also studied the demand for audit from the banks/investors. They find that companies go for their financial statements audited to satisfy their lenders like banks.

According to Haley and Palepu, 2001, p. 415, banks generally demand audited financial statements for granting loans to private companies. Similar result is also drawn from a study by Seow (2001) in small companies in the UK. Carey et al., (2000) also studied regarding the demand from lenders. Their findings show that demand for audit increases with the degree of debt in the company; the more debt the higher the demand for audit of the company. This result is also consistent with a study by Chow (1982).

3.6.2 Internal demand
Demand for audit can also arise from inside the company. Internal demand for audit generally arises as a matter of internal control. The main users of financial information within the company are managers and employees of the company. In companies with large organizational structure and level, there can be more information gap and conflict of interests which replicates weaker internal control mechanism. In regards to this, there occurs a need of internal demand for audit as tool kit for better internal control system. These factors are elaborated below:

3.6.2.1 Demand from managers
A study by Collis et al. (2004) based in the UK found that 63% of the managers in small companies opinioned that the audited accounts is beneficial for the company and will continue to do so. Their argument was that audit gives a review of the internal control systems of the company. An audit assures the management that the financial statement is correct (Carberg et al., 1985). A study by Abdel-khalik (1993) about audit demand shows that the demand for audit increases with the number of employees, increasing the loss of control due to hierarchy.
Similar results were drawn by Senkow et al. (2001) from a study relating to the relationship between employees and the managers.

**3.6.2.2 Voluntary reporting and internal control**

It is the responsibility of management for establishing and maintaining the entity’s internal control. Theoretical literature shows that company management voluntarily adopts monitoring mechanisms in the presence of potential agency problems. Based on survey data, Hermanson (2000) observes that the stakeholders feel that internal control aids decision making and voluntary reporting motivates management to improve internal control. In a study by Deumes & Knechel (2008), found a positive relation between the willingness of conducting voluntary reporting and the existence of agency problems and information asymmetry. A study by Knechel & Willekens (2006) also shows that internal control increases the demand for audit. Collis et al. (2004) have also been studying the relationship between the audit and internal control, if auditing can be used as a check on the internal control. Their findings show a positive relationship between these two factors, the respondents in their study agrees that the audit gives a check on the internal control.

**3.6.2.3 Lower cost of capital**

Generally, market risk is adjusted in the cost of capital. Information asymmetry is also regarded as a form of risk. Reduction in information asymmetry can reduce the information risk. Because of the reduced information risk associated with audited financial information, creditors/banks may offer loans with lower interest rates. In other words, the borrowers can obtain capital at reasonable cost and this is an internal benefit for the company. In regard to this, a study by Blackwell et al. (1998) found that small private firms derived an economic benefit from auditing through significantly lower interest rate than that paid by non-audited firms. However, he further mentioned that to make this an internal benefit, the cost of capital i.e. interest rate should be more than the cost for audit. Brannström (2005) also argues that the auditing reduces risks for investors and facilitates firms to obtain capital.

**3.6.2.4 Attitude towards audit**

The demand for audit can also be related with of the users’ attitude towards it. There can be both positive and negative attitudes towards audit. Positive attitude towards audit comes when the clients/users are satisfied with the audit service. Satisfaction is more related to behavior science and it relates to cost-benefit aspect, quality issues etc. Some users are cost-benefits driven and others may think quality is the first criteria which determine their attitude. If a client is satisfied with the audit, s/he is more likely to buy it, or demand it as long as it meets the expectation. A study by Behn et al.,(1999, cited in Franzén 2010, p. 14), related with audit fees and satisfaction of audit, found that the satisfied clients with audit are more willing to pay, which replicates that quality is more important than just a cost issue.

**3.7 Statutory Audit**

Statutory audit means it is mandatory for certain companies to have an auditor who inspects their accounting and administration (FAR SRS, 2006). It can also be defined as an external audit that involves ‘an independent examination of and the subsequent expression of opinion on, the financial statements of an organization’ (Owen et al., 2005, p. 34). The main objective of statutory audit is to provide certified financial reports for the stakeholders of the companies (FAR SRS, 2007). As per the European Economic Community (EEC) Fourth Directive, Article 51, the member countries in the European Union should use statutory audit. The article mentions that: the companies must have their accounts audited by one or more persons authorized by national law to audit accounts (78/660/EEC, p. 15). However, the same
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directive (article 11) also mentions that the member states can exempt small companies from the statutory audit (78/660/EEC, p. 37-38). In regard of this provision, the majority of the member countries have statutorily exempted the SMEs from doing audit. Sweden have also exempted statutory audit requirement for SMEs that came into practice since 1st July, 2010.

The statutory audit in Sweden was introduced in 1983 and every limited company should have the financial statements audited from a certified auditor. In Sweden, as per the Auditing Act, 1999, Section 5, there is a requirement of both financial and administrative audit, and it should be detailed as per the generally accepted auditing principles (GAAP) (Norstedts Juridik, 2009, p. 21). As per European Commission, companies with 50 employees and more, with turnover more than 83 million Swedish Kronor, and/or a balance sheet asset total exceeding 41.5 million Swedish Kronor need statutory audit requirement. In case of Sweden, as per the new legislation, firms with more than 3 employees, turnover of 3 million Swedish Kronor, and/or a balance sheet asset total of 1.5 million Swedish Kronor require statutory audits (SOU, 2008; FAR press release, 2010).

The following table shows the statutory audit exemption published by European commission and Swedish new legislation of audit exemption for SMEs.

### Table 7: Criteria for Statutory Audit Exemption

<table>
<thead>
<tr>
<th>Criteria established by nations</th>
<th>Turnover (SEK)</th>
<th>Number of Employees</th>
<th>Balance Sheet Total (SEK)</th>
</tr>
</thead>
<tbody>
<tr>
<td>European Commission</td>
<td>83000000</td>
<td>50</td>
<td>41500000</td>
</tr>
<tr>
<td>First Proposal (Sweden)</td>
<td>83000000</td>
<td>50</td>
<td>41500000</td>
</tr>
<tr>
<td>Sweden (by Nov. 2010)</td>
<td>3000000</td>
<td>3</td>
<td>1500000</td>
</tr>
</tbody>
</table>

Source: SOU 2008:32; FAR press release: 1st Nov, 2010

A study by Lindholm & Sagefors (2006) on ‘Statutory audit, the opinion of small business owners’ shows that 27% of the respondents opinioned significant benefits of auditing as a tool of controlling mechanism. They argued that auditing helps to control accounting and economic situations, while 27% appreciate that laws and regulations are followed. 24% of the respondents believed that auditing helps to raise the credibility of the financial reports. 8% of the respondents stated that audit provides opportunities for consultation. Furthermore, 38% considered that abolishment of statutory audit would bring greater errors in the annual accounts and 22% argued that this will increase the frauds and illegal acts. Nearly 79% stated that they are most likely to consult their accountants to get an audit of their business despite statutorily not required (Lindholm & Sagefors, 2006, p. 48).

### 3.8 Voluntary Audit

As mentioned above there can be numerous reasons for doing audits. External auditing is mostly seen as statutory requirements for the companies. But after removal of statutory audit requirements for SMEs in EU including Sweden, new horizons have been created with lots of debates for and against this provision, and still a hot topic of discussion at present.

Number of studies can be found in the literature investigating the factors related with voluntary demand for external auditing. A study by Seow (2001) states that users of audited financial statements identify and make use of the benefits as a matter of assurance that auditing brings, resulting the demand for voluntary audit, even it is not required by law. In addition, he also mentions that a firm may be more likely to have voluntary audit from their existing auditors, if the auditors also offers other essential and useful services.
A study by Chow (1982) in relation to the impact of agency costs, firm size and debt found a support for firm size on voluntary demand for auditing. He used an agency framework to investigate the impact of agency, firm size and debt related to voluntary audits. Similarly, Carey et al. (2000) also indicates that demand for voluntary audits is positively related with the level of the firm’s debts. This implies that as the debt size of the firm increases, there is more willingness of getting an audit.

A study by Tauriingana & Clarke (2000) related with the demand for external auditing in relations with managerial share ownership, size, gearing and liquidity of small firms exempted from statutory audit in the UK, found out that conflicts between managers, shareholders and outside creditors, firm size and size of the firm’s debt are the main reasons for external audit demand. The authors also explain that auditing is to get help to control stakeholders’ conflict of interests. In addition, they also state that the willingness to obtain voluntary audits tend to increase as the size of the firm increases. Their reasoning to this statement was that, as a firm grows, the number of transaction also increases with higher probabilities of inaccuracies and this leads for obtaining voluntary audit. The next influencing factor for demand of audit as per Tauriingana and Clarke (2000) is that the debt size in a firm. They argued that it would be of great risk for creditors to use the non-audited financial information. Since the creditors don’t have legal right to assess a firm’s books of accounts, auditing would be the best way for them to confirm about the firm’s financial information (Tauriingana & Clarke, 2000, p. 160-166).

A study by Abdel-khalik (1993) based on “structure of organization approach” found a correlation between voluntary demand for auditing and the extent of hierarchy. Blackwell et al. (1998) found that small private firms derived an economic benefit from voluntary auditing through significantly lower interest rate than that paid by non- audited firms. In small enterprises, mostly owners have direct control. When the firm grows in size, it becomes necessary to delegate responsibilities and authorities resulting less supervisions. This may increase the risk of suspicion among owners. As a matter of this, Hay & Davis (2004) mentioned that owners seek voluntary audits as a tool to compensate control system for organizational loss of control (Hay & Davis, 2004, p. 52).

Besides above, one of the interesting benefits of voluntary audit is mentioned by C Lennox, (2009) i.e. the signaling benefits. Going for voluntary auditing can create positive signal about the company’s credit risk (C Lennox, 2009, p. 9). According to (Melumad & Thomas, 2009), Companies would have incentives to appoint auditors voluntarily due to the positive signal that rational lenders would refer. The authors show that the decision to hire an auditor conveys useful information about the company’s type when auditing becomes voluntary. In other words, they argue that there is a signaling benefit from voluntary audit since the company’s decision on whether to be audited conveys valuable information to stakeholders, shareholders and other interested users (Melumad & Thomas, 1990, p. 77-79).

3.9 Corporate Social Responsibility

Numerous literature and researches on Corporate Social Responsibility (CSR) have been found on large companies (Sweeny, 2007). Williams (2005) mentions that CSR is important for both large companies and small companies. The European Union (EU) in regard to CSR stated that, “...its wider application in SMEs including micro-businesses is of central importance, given that they are the greatest contributors to the economy and employment” (Commission of the European Communities, 2001, p. 7). Similarly, a study by Roberts et al.
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(2006) states small and medium-sized enterprises have positive economic and social impacts in the society, which are not often recognized in CR terms (Roberts et al., 2006, p. 280).

CSR are defined in different ways and perspectives. CSR can be said as an obligation that is beyond the law, for a firm to pursue long term goals that are good for society. Being a responsible part of a society, CSR is way of managing business activities to generate an overall positive impact on the society. In other words, it can be said as way of responding positively to emerging priorities and expectations of the society. According to The European Union (EU), Corporate Social Responsibility (CSR) is “a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on voluntary basis” (Commission of the European Communities, 2001, p. 6).

According to EC and Observatory of European SMEs, (2002), stakeholders are identified as follows: a) Internal Stakeholders: employees, shareholders and owners, and b) External stakeholders: local communities, suppliers and other organizations.

A study by Gelb & Strawser (2001) regarding CSR and Financial Disclosure, show a positive relationship between disclosure level and Corporate Social Responsibility. They found that socially responsive firms provide more informative and extensive disclosure than companies that are less focused on advancing social goals. The findings suggest that firms may provide more informative disclosures because of a sense of responsibility to their stakeholders (Gelb & Strawser, 2001, p. 10-11). Better disclosure in other words, can be regarded as better transparency by conducting audit of the financial information of the company.

3.10 Previous Research

Numerous researches can be found in the literature regarding audit demand, especially after the European Union’s decision to abolish statutory audit requirements for the small and medium-sized enterprises. The main reason often argued for exempting SMEs from statutory audit was the high audit costs than the benefits it derived. But studies show that SMEs still prefer and go for their financial statements get audited despite not required by law to do so. A recent study by R.L. (2010, cited in Franzén 2010) in Danish context, mentioned that about 78% of SMEs in Denmark has continued to conduct an audit of financial information, despite the SMEs are statutorily not required to audit since 2006 (R.L., 2010, cited in Franzén 2010, p. 9). In regard to Sweden, a study by Svanström (2008) found that 68% of the respondents (SMEs) would continue with audit (Svanström, 2008, p. 287). Furthermore, he found that 84% of the subsidiaries and 57% of the non-subsidiaries would continue their accounts audited despite statutorily not required (Svanström, 2008, p. 112). He also mentioned that the demand for auditing is positively related with firm size, use of a Big 4 auditing firm and the geographical location of companies in Småland (Svanström, 2008, p. 287).

Above studies offer statistics on the proportion of firms that are positive towards voluntary audits. Going through the previous literature, we found less research in the areas why SMEs go for voluntary audit. The present study aims to contribute to identify reasons behind for voluntary audit. This research will be probably first of its kind and will help to fill the gap in the literature by exploring the expected benefits of SMEs for voluntary audited financial statements, especially after the formal implementation of the new rule effective from 1st July, 2010 i.e. exemption of statutory audit requirements for SMEs in Sweden.

Next section will present the theoretical framework for this research study.
3.11 Our Theoretical framework
The theoretical framework is structured based on previous literature review findings. Authors will then apply these theoretical findings when it comes to formulate interview guide for the research study. The empirical findings will be collected through interviewing. Thereafter, in order to answer our research question authors will analyze empirical results by using grounded theory approach.

Auditing takes a significant role when it comes to track credible and accurate financial information of firms. The mandatory statutory audit requirement differs between different countries. In case of Sweden, the requirement of statutory audit applies only to companies with more than 3 employees, 3 million Swedish Kronor in turnover, and/or 1.5 million Swedish Kronor in balance sheet total assets (FAR Press Release, 2010-11-01). This new proposition came into effect after 1st of November 2010, as per the Swedish government’s decision dated 25th March, 2010. The new proposition of Sweden in relation to statutory audit exemption is much smaller than the EC’s criterion for audit exemption. Previous studies have shown that exempted firms are inclined towards conducting audit despite not required by law. This study wants to find reasons for SMEs choice of conducting their financial statements audited despite not required by the law and their expected benefits from voluntary audit.

When SMEs need external financing there has difficulties in terms of risky nature of SMEs, credit rating requirement and poor publicly available information. According to Abouzeedan (2003), there are seven types of financing methods for SMEs namely internal financing, external informal financing, debt financing, equity financing, public market financing and financing from government agencies. Except internal financing and external informal financing, the other financing methods call for detailed financial and non-financial information of companies. Some prior studies argue that SMEs willing to go for voluntary auditing because of the difficulties when it attempts to get loan from external financing source. Abouzeedan (2003) mentions that major source of Swedish SMEs’ financing come from bank loans and futures retain earnings. With this regard, when it comes to collect empirical findings for this study bankers’ perspective of audit demand for SMEs will be presented.

Based on studies discussed about banking perspective for SMEs, banks use several lending methods when it comes to grant loans. According to (Torre et al., 2010; Bass & Schrooten 2006; Ashton & Keasey 2005), these lending methods could be categorized as relationship lending, financial statement lending, asset based lending (credit collateral) and credit scoring. Besides that, there can be different opinions between large banks and small banks when it comes to choose lending methods for SMEs. However, (Torre et al., 2010) find that all types of banks are willing to deal with SMEs by using new technologies, business models and risk management systems attempt to track client firm’s financial and non-financial performance.

Related with the cost and benefits of voluntary audit for SMEs, Blackwell et al., (1998) finds that auditing can reduce the lenders’ monitoring cost for their client firms; credibility of financial information can enhance better investing opportunities from investors and lending decision from financial institutions. The increasing demand of audit can reduce audit fees because of competitive environment. Besides that, C Lennox, (2009) finds that SMEs’ demand for voluntary audit provide signaling benefits. Having their financial statements audited could attain a positive signal to overcome the credit risk. However, SMEs have concentrated ownership structure and less conflict of interests among its stakeholders. So, external auditing might be a cost burden for SMEs. In this regard, voluntary audit for SMEs is
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A cost burden or beneficial mechanism that is still debating issue. This study attempts to get relevant explanation for that cost and benefit arguments when SMEs go for voluntary audit.

Regarding with literature review of stakeholder theory, demands for auditing is viewed differently by different stakeholders of companies. The major intuition of stakeholder theory is that to get value maximizing of the firm. In order to attain value maximizing of a firm, managers have to take account all stakeholders’ interest of the firm and then try to maximize the market value of the firm. From stakeholders’ perspective, auditing is viewed as governance mechanism when it attempts to get sound governance practices and transparent information for all stakeholders and other interested users (FAR SRS, 2006).

When companies have separation of ownership and control, agency problem will be mostly injected. Information asymmetry between manager (agent) and owner or shareholders (principal) of the firm call for internal and external monitoring mechanism requirement in order to get transparent information. In order to align principal and agent’s interests, firms demand for auditing as monitoring and controlling purpose. Besides that voluntary audit has an impact on CSR. A study by Gelb & Strawser (2001), show a positive relationship between financial disclosure and CSR. Socially responsive firms provide more informative and extensive disclosures to their stakeholders.

Regarding with literature review of this study, the reasons behinds why SMEs go for voluntary audit and their expected benefits could summarize as follow. SMEs’ willing to have audited financial statement is to overcome agency problem and attempts to maximize value of the firms. Moreover, SMEs believe financial statements when audited can enhance better signaling of the firm in terms of credibility and transparent information disclosure. As a consequence, they can get better credit scoring when they seek to find for external financing. Banks might grant loans to SMEs with acceptable interest rate because of credible audited figures. In Sweden, auditing is used to limit illegal act and fraud and even for taxation purpose (Blackwell et al., 1998; Tauringana & Clarke 2000; Kaur et al., 2007).

The research gap could be described as after the legislation (since 1st July, 2010) of audit exemption in Sweden for SMEs, there are few literatures regarding SMEs going for voluntary audit. Numerous studies have done research on statutory audit and its benefits. This study will answer the research question by conducting interviews with Swedish SMEs who are statutorily exempted from audit but still continuing their accounts audited. Our motive would be to find the reasons behind conducting audits besides studies argue that the audit cost for SMEs is more than the benefit it derived. Moreover, this study will also discuss bankers’ perspective of auditing for SMEs, whether banks grant loan to SMEs with lower interest rate when they have audited financial statement. Besides that, this study intends to give explanation regarding whether banks will demand their SMEs client to have audited statements.
Chapter 4

Chapter 4: Empirical study and Findings

The empirical findings are based on the interviews conducted for the study. Since our research is to find the perspectives of representatives from small companies and bankers, 20 interviews of small firms and 7 interviews with bankers were conducted with the aim to get their opinions regarding the audit demand by small companies despite statutory audit not required by law and bankers’ opinion of financing to companies who have not their financial information audited. The interviews were conducted face-to-face in order to get responses of interviewees.

When it comes to collect data from SMEs, we defined the small and medium-sized companies within two out of three following criteria; 1.5 million Swedish Kronor turnover, 3 million Swedish Kronor balance sheet total and up to 3 employees. When companies meet two out of three criteria we defined those companies as our target sample group and attempt to conduct interviews with their representative. In order to get bankers’ opinion of audit demands for SMEs authors conduct interview with bankers.

Since there are five main banking institutions namely Nordea, Skandinaviska Enskilda Banken (SEB), Svenska Handelsbanken (SHB), Denske bank and Swedbank in Northern Sweden, authors conducted interview with bankers from those five major banks. Besides, authors also conducted interview with bankers from Forex bank in order to get bankers’ opinion from a small and niche bank.

This empirical findings chapter is divided mainly into two sections. Brief introduction of the respondents/interviewees’ profile will be given in the first section. The second section will provide the collected opinions of respondents/interviewees regarding the research findings. This section will be further divided into two sub-sections; first would be related to the opinions of small companies and the next will be the bankers’ perspectives regarding the topic.

4.1 Profile of interviewees

4.1.1 Interviewees profile of SMEs

1. Mehrdad Naurbakhsh is the manager of Un Po D'italia. Mr. Naurbakhsh is working in the company for more than five years, in managing and controlling the business. This 60 year person is engaged in the pizza making profession since 19 years. Un Po D'italia was established in 2002 as a pizza restaurant. There are 3 employees working in Un Po D'italia. The annual turnover of the company is 1.70 million Swedish Kronor with balance sheet asset total of 0.36 million Swedish Kronor in 2010.

2. Eva Lindh-Holmgren is the owner of Lilla Galleriet i Umeå AB. The company was incorporated in 2006, engaged in art galleries and trading arts with two employees. Before Eva started her art business, she was herself an art teacher. There are 2 employees working in Lilla Galleriet i Umeå AB. The annual turnover of the company is 1.9 million Swedish Kronor with balance sheet asset total of 1.48 million Swedish Kronor in 2010.
3. Anders Olf Rydfjäll is the owner of Rydfjäll Byggkonsult AB with two employees. Anders by profession is an engineer. Rydfjäll Byggkonsult AB was established in 2005 engaged with civil engineering, architecture and planning activities. There are 3 employees working in Rydfjäll Byggkonsult AB. The annual turnover of the company is 2.41 million Swedish Kronor with balance sheet asset total of 1.44 million Swedish Kronor in 2010.

4. Eva Brändström is one of the representatives of E L G E Ekonomikonsult AB. Eva by profession is an authorised accountant. E L G E Ekonomikonsult AB provides accounting and consulting services. The company was established in 1986 with equity capital of 100000 Swedish Kronor. There is 1 employee working in E L G E Ekonomikonsult AB. The annual turnover of the company is 0.63 million Swedish Kronor with balance sheet asset total of 0.50 million Swedish Kronor in 2009. The annual turnover of the company is less than 3.0 million Swedish Kronor with balance sheet asset total of 1.5 million Swedish Kronor in 2010.

5. Orjan Magnusson is the owner Örjan Magnusson Psykologkonsult AB. He is a registered psychotherapist. His company provides psychology, psychotherapy and Cognitive Behaviour Therapy. The Company was established in 2008 with equity capital of 100000 SEK. There is no employee working in Örjan Magnusson Psykologkonsult AB. The annual turnover of the company is 1.0 million Swedish Kronor with balance sheet asset total of 0.80 million Swedish Kronor in 2010.

6. Hans Hällström is one of the co-owners of I4m AB. I4m AB provides healthcare and massage services specially related to the treatments Tuina and Ayurveda. He also owns a separate company called ERALIX AB. There is 1 employee working in I4m AB. The annual turnover of the company is less than 3 million Swedish Kronor with balance sheet asset total of 1.5 million Swedish Kronor in 2010.

7. M Ann-Charlotte Widmark Ludvigsson is one of the co-owners Lintottens Hårfixeri i Umeå AB. The company’s business is relates with hairdressers and hair-care. The company was established in 1986 with equity capital of 102000 Swedish Kronor. Besides, as a partner, Ann-Charlotte also works as a hairdresser in the company. There is employee working in Lintottens Hårfixeri i Umeå AB, all three co-owners work in the company. The annual turnover of the company is 2.1 million Swedish Kronor with balance sheet asset total of 0.71 million Swedish Kronor in 2010.

8. Anna-Marta Hillorn is the owner of a company called Sofiehems Sjukgymnastik AB. Professionally, Anna-Marta is a physiotherapist since 1982 and her company provides physiotherapy. The company was established in 2002 with capital of 100000 Swedish Kronor. The company has special contract with the Västerbotten County Council, each patient is charged 100 Swedish Kronor and rest fee is paid by the Council on their behalf. There is no employee working in Sofiehems Sjukgymnastik AB. The annual turnover of the company is 0.75 million Swedish Kronor with balance sheet asset total of 0.30 million Swedish Kronor in 2010.

9. Jan Hardell is the owner of his company called Magazin du Nord. Magazin du Nord’s business relates with clothing-retailing and others. The company was established in 1985. There are 2 employees working in Magazin du Nord. The annual turnover of the company is less than 3 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.
10. Åsa Westin is the owner of Handelsgården. The company deals with the local handicraft products. Handelsgården is popular for Skafferiet, with local food specialities. The company is a part of Sagagallerian which is formed of many women doing handicraft business. However, each person has separate business working combined. There is 1 employee working in Handelsgården. The annual turnover of the company is less than 3 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.

11. Leif Stefan Nilsson is the owner/director of his company Burmans Musik AB which was established in 1998. The company business relates to music records. There is 1 employee working in Burmans Musik AB. The annual turnover of the company is 2.40 million Swedish Kronor with balance sheet asset total of 1.30 million Swedish Kronor in 2010.

12. Rezza Dehad is one of the owners of Cafeteria Pronto i Umeå AB. The company’s business is related to sightseeing cruises and restaurant. The company was established in 1985. There are 2 employees working in Cafeteria Pronto i Umeå AB. The annual turnover of the company is 1.80 million Swedish Kronor with balance sheet asset total of 0.12 million Swedish Kronor in 2010.

13. Frida Palm is the owner of her company called Frida Palm. The company was established in 2007. The company’s business is about nail care. Frida Palm is engaged in this profession since 5 years. There is no employee working in Frida Palm. The annual turnover of the company is less than 3.0 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.

14. Hans Vilgot Sjöberg is the owner and director of his company Printstore Personal Signs Sweden AB. The company’s business relates to printing related products. The company was established in 2008. There is no employee working in Printstore Personal Signs Sweden AB. The annual turnover of the company is 1.15 million Swedish Kronor with balance sheet asset total of 0.67 million Swedish Kronor in 2009. The annual turnover of the company is less than 3.0 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.

15. Vivianne Lindström is the owner and director of Atelje Koppehatten. The company manufactures and sells wearing apparel like hats and other accessories. The company was established in 2008. There is no employee working in Atelje Koppehatten. The annual turnover of the company is less than 3.0 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.

16. Susanne Loven is the manager of Annaleffe AB. The company is involved in trading gift items, decorative, antiques and other related business. The company was established in 2010. There is 1 employee working in Annaleffe AB. The annual turnover of the company is less than 3.0 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.

17. Synnöre Andersson is the director and co-owner of the company Lloyd Mattsson Konst och Ram AB. The company was established in 2009 and it involves in trade with art, framing art, art web design. There is 1 employee working in Lloyd Mattsson Konst och Ram AB. The annual turnover of the company is 2.54 million Swedish Kronor with balance sheet asset total of 0.23 million Swedish Kronor in 2010.
18. Inga Maria Fransson is owner of the company name Optique i Umeå AB. The company deals with selling of optical goods. The company was established in 1988. There are 2 employees working in Optique i Umeå AB. The annual turnover of the company is 2.40 million Swedish Kronor with balance sheet asset total of 1.91 million Swedish Kronor in 2009. The annual turnover of the company is less than 3.0 million Swedish Kronor with balance sheet asset total of less than 1.5 million Swedish Kronor in 2010.

19. Monica is a representative of Dahlgrens Ur & Optik AB. The company was established in 1971. Dahlgrens Ur & Optik AB’s business is related with selling spectacles and other optical devices, and watches. There is 1 employee working in Dahlgrens Ur & Optik AB. The annual turnover of the company is 1.21 million Swedish Kronor with balance sheet asset total of 0.48 million Swedish Kronor in 2010.

20. Roger Mikaelsson is the owner and director of a company named Datacenter i Umeå AB. The company engages in the sale and brokerage of new and used computers, service and repair, sales and installations of software and related services. The company was established in 1994. There are 2 employees working in Datacenter i Umeå AB. The annual turnover of the company is 2.0 million Swedish Kronor with balance sheet asset total of 0.68 million Swedish Kronor in 2010.

4.1.2 Interviewees profile of Bankers

1. Alexander Bagrov is a Head of corporate branch at Handelsbanken, regional bank Northern Sweden, Umeå. He has been working as a head of corporate branch over a month. Before that he has been working in banking profession as a credit analyst and branch manager.

2. Annika Holmlund is a sale support of corporate department at Nordea bank in Umeå.

3. Fredrik Lundberg is a branch manager at Denske bank, Västerbotten province bank in Umeå. He has been working in banking profession for over 20 years.

4. Maria is a banker at Forex bank in Umeå. She has been working in accounting and banking professional over 4 years.

5. Marie Johansson is a head of Swedbank in Umeå. Marie has been working in banking profession for over 20 years.

6. Martin is a banker at Forex bank in Umeå. He has been working at Forex bank almost 3 years.

7. Mikael Stålfjäll is a Head of corporate branch at Swedbank in Umeå. Mikael has been working as a Head of corporate department at Swedbank in Umeå for 3 years and he has been working in this banking profession for 15 years.

The following table shows the lists of interviewees from SMEs and banks.
### Table 8: Group and Lists of interviewees

<table>
<thead>
<tr>
<th>SMEs</th>
<th>Business Type</th>
<th>Interviewees</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Un Po D’italia</td>
<td>Pizza Restuarant</td>
<td>Mehrdad Naurbakhsh</td>
</tr>
<tr>
<td>2. Lilla Galleriet i Umeå AB</td>
<td>Arts and Framing</td>
<td>Eva lindh-Holmgren</td>
</tr>
<tr>
<td>3. Rydflåj Byggkonsult AB</td>
<td>Civil Engineering</td>
<td>Anders Olf Rydflåj</td>
</tr>
<tr>
<td>4. ELGE Ekonomikonsult AB</td>
<td>Accounting Consulting</td>
<td>Eva Brändström</td>
</tr>
<tr>
<td>5. Örjan Magnusson Psykologkonsult AB</td>
<td>Psychology</td>
<td>Orjan Magnusson</td>
</tr>
<tr>
<td>6. I4m AB</td>
<td>Massage and fitness</td>
<td>Hans Hållström</td>
</tr>
<tr>
<td>7. Lintottens Hårfixeri i Umeå AB</td>
<td>Hair care</td>
<td>Ann Widmark Ludvigsson</td>
</tr>
<tr>
<td>8. Sofiehems Sjukgymnastik AB</td>
<td>Physiotherapy</td>
<td>Anna-Marta Hillorn</td>
</tr>
<tr>
<td>9. Magazin du Nord</td>
<td>Clothing and retailing</td>
<td>Jan Hardell</td>
</tr>
<tr>
<td>10. Handelsgården</td>
<td>Handicrafts</td>
<td>Åsa Westin</td>
</tr>
<tr>
<td>11. Burmans Musik AB</td>
<td>Music and records</td>
<td>Leif Stefan Nilsson</td>
</tr>
<tr>
<td>12. Cafeteria Pronto i Umeå AB</td>
<td>Resturants</td>
<td>Rezza Dehad</td>
</tr>
<tr>
<td>13. Frida Palm</td>
<td>Nail care</td>
<td>Frida Palm</td>
</tr>
<tr>
<td>15. Atelje Koppaehatten</td>
<td>Hat making and selling</td>
<td>Vivianne Lindström</td>
</tr>
<tr>
<td>16. Annaleffe AB</td>
<td>Decorative &amp; Glossaries</td>
<td>Susanne Loven</td>
</tr>
<tr>
<td>17. Lloyd Mattsson Konst och Ram AB</td>
<td>Arts and framing</td>
<td>Synnöre Andersson</td>
</tr>
<tr>
<td>18. Optique i Umeå AB</td>
<td>Optical</td>
<td>Inga Maria Fransson</td>
</tr>
<tr>
<td>19. Dahlgrens Ur &amp; Optik AB</td>
<td>Optical and watches</td>
<td>Monica</td>
</tr>
<tr>
<td>20. Datacenter i Umeå AB</td>
<td>Computers and Services</td>
<td>Roger Mikaelsson</td>
</tr>
</tbody>
</table>

#### Banks

<table>
<thead>
<tr>
<th>Banks</th>
<th>Bankers</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Handelsbanken</td>
<td>Alexander Bagrov</td>
</tr>
<tr>
<td>2. Nordea</td>
<td>Annika Holmlund</td>
</tr>
<tr>
<td>3. Denske Bank</td>
<td>Fredrik Lundberg</td>
</tr>
<tr>
<td>4. Forex bank</td>
<td>Maria</td>
</tr>
<tr>
<td>5. Swedbank</td>
<td>Marie Johansson</td>
</tr>
<tr>
<td>6. Forex bank</td>
<td>Martin</td>
</tr>
<tr>
<td>7. Swedbank</td>
<td>Mikael Stålfjäll</td>
</tr>
</tbody>
</table>

**Source:** Authors

The 20 small companies interviewed operate in diverse business areas and have dissimilar core businesses such as, restaurants, health, glossaries and decorative, handicrafts, optical, music records, hairdressing, nail care, printings, engineering, accounting consultant, arts and framing, clothing and retailing, computers and services. Thereby, they operate in different markets with diverse customers and they have also been in the market for different periods of time, which can represent whole Sweden with similar demographic interests and diverse business in different part of the country. Out of the total 27 interview, 12 interviewees were male and the remaining 15 were female. This represents 44% of male respondents and the rest 56% female respondents of sample population. As for banks, there are 5 big banks in Umeå, we conducted interviews with 4 banks out of 5; with this regard we can say that the sample bankers’ opinion represent the whole banking in Umeå.

### 4.2 Opinion of SMEs

Authors attempt to collect SMEs’ opinions for audit demand based upon the interview guide developed from the theoretical framework in the previous chapter. The opinions from the companies are reported as under:
4.2.1 Audit Legislation

It is the fact that the new Swedish legislation has exempted the companies with less or equal to 3 employees, less or equal to 3 million SEK, and /or less or equal to 1.5 million balance sheet asset total from doing statutory audit anymore effective from 1st November, 2010. If a company that fulfills at least two out of three criteria mentioned above, there is no any mandatory obligation of doing external audit. However, such company has still an option to go for voluntary audit.

When the respondents were asked if they have ideas about this new rule as mentioned above regarding the statutory audit exemption for the small companies, most of the respondents knew about this change in the legislation except few respondents. Out of 20 respondents, 15 respondents had idea about the change in legislation for audit to small companies whereas the rest 5 respondents were unknown about the new rule. In other words, 75 percent of the companies had the information about the non-requirements of statutory audit if the companies fulfill at least two out of three conditions for being exempted from statutory audit exemption. The respondents knew about the new rule mainly through the newspapers and their auditors. The respondents who did not know about this rule were Westin, Stefan Nilsson, Susanne Loven, Synnöre Andersson, and Maria Fransson. In regard to Synnöre Andersson, the respondent had idea about the new rule but did not know when this new rule came into force.

4.2.2 Is Audit Important?

In reply to the question why the company conducts audit, despite it is not required by law, Naurbakhsh stated that it is important to the company. According to Holmgren, first of all this is the new law and at the moment the company likes it to have because conducting audit is good approach to the company as it is important to the owners. Rydfjäll stated that it is important to the company due to its several benefits. More importantly, it is helpful tool to have control of the company. Eva Brändström also stated similar opinion that the audit is important to the company. Magnusson stated that audit is important because the owners are secured doing it. Hans Hällström stated that audit is important to the owners and also during taxation. Ludvigsson also stated audit it is important to the company and the owners. The company wants to continue it because owners are not sure what is going to be later on; as the rules are changing, it is good to have audit for some couple of years and see how it goes. According to Hillorn, audit is important for the owners as well as for tax office for instance as if they need verification. According to Hardell, audit is important to the company. He further added that the rules are changing frequently and it is difficult to know updates of new rule every time, it is also wastage of time reading newspapers every time. It is good to have the company’s audit as it is the best way to take care of the papers and the company.

According to Westin, it is important to the company; especially to the company with unique and complex organisational structure for better transparency of information in the company besides it is not required by law for doing audit. Stefan Nilsson stated that audit is important to owners and other interested parties. Rezza Dehad stated that owners want best financial information and it is the audit that provides the best financial information of the company. Frida Palm stated that audit is important to know the right and correct information of the company. According to Sjöberg, it is good to have audit so that other companies and other interested parties can see how the company is going. Lindström stated that, being the owner the audit is important to the company, to know the company better. Susanne Loven stated that the audit makes feel comfortable and secured to the owners of the company.
Synnöre Andersson stated that the audit is important to a company not having skilled manpower in handling the books of accounts well. If a company / owners have good educational background in accounting / finance it is not really important to the company. The main reason doing audit is that the company thought it is required by law. Maria Fransson stated that audit is important to the company as it provides lots of support to the company. Monica stated that audit is important to the company; besides the company had planned not to conduct audit after the new rule came into effect, but due to time limitations the company decided to continue it. Mikaelsson also stated that audit is important to the company and the owners as feel secured doing it.

4.2.3 Factors for Audit Demand

Different factors are accounted when the respondents are asked about the factors that determine the audit demand for their company. The respondents were asked about the internal and external factors for the audit demand despite not required by law to do it. The factors pinpointed by the respondents are discussed by distinguishing them into internal and external factors:

4.2.3.1 Internal factors

In response to the question regarding the internal factors for the audit demand, Mehrdad Naubakhsh stated that the owners are the first and main factor that demand audit. According to him, the owners want to feel secured with the company’s financial information, and audit can make this possible. According to Eva Lind Holmgren, the demand for audit first comes from the owners. Eva Lind Holmgren added that the audit is more important to the owners than the employees because they are the ultimate users of the audited financial statements. And it is obvious to conduct audit by the owners for to know the company’s state of business and feel more secured. Furthermore, Eva Lind Holmgren also stated that it is the new rule and the owners also want to keep it for more years and see later whether to demand or not.

Regarding the internal demand of audit, Anders Olf opinion that it is the owner first in hand to demand audit for easy controlling about the economy of the company. Anders Olf added that the main reason for audit demand by the owners is due to the feeling of security and control that gives by conducting audit. Eva Brändström also added that it is the owner for audit demand. Respondents like Hans Hällström, Anna-Martä Hillorn, Jan Hardell, åsa Westin, Stefan Nilsson & Anton Olsson, Rezza Dehad, Inga Maria Fransson, and Roger Mikaelsson were also stated similar opinions that it is the owners who demand audit for the security reason for themselves.

As per Orjan Magnusson, owners always want to know what the company is doing and how is the company doing at the end of the year; so wants to know all things are well managed and under control. For this reason, Orjan stated audit can only make the financial information verified and make owners feel secure. He further added that audit demand is not only important to owners but also employees in the company where employees have also some interests.

According to Vivianne Lindström, audit demand arises from the owners itself. Because owners want to have correct and transparent information of the company which is also well accounted and reported. He further added that every owner want to feel secure regarding their company so audit demand is the main reason for assurance they get from conducting audit. Similar opinion was also given by Susanne Loven. Susanne Loven added that when the company has more than one owner, there is higher demand for audit with increasing need of assurance regarding the financial information about the company with more transparency.
Ann-Charlotte Widmark Ludvigsson also stated that in the companies with co-owners, there is more need for audit to make all the partners assured and satisfied with the company’s overall affairs from the externals like auditors.

Synnöre Andersson stated that it is the owners that demand for the audit as for safety reason. Educational background of the owners can also affect for audit demand internally. The educated managers and owner especially in the field of accounting, finance and economics believe audit is a quality stamp for the company, beside they really do not think it is only the main aspect of security reasons. There is more audit demand from the owners without good education background in related field as they have no choice, besides calling an external auditor to fix their annual reports verified and make more reliable. Similar opinions were also given by Hardell, Holmgren.

Monica said that owners want the correct numbers of their company and audit is the only way to get the correct numbers of all the accounting records and reports when audited. Frida Palm stated that in an owner-managed company, it is most probably the owners who demand the audit as they want everything correct regarding the financial information of the company. However, if the companies are bigger and have more employees it can also be demanded by the employees.

Furthermore, the owners devote most of their time in managing the company’s business, rather than more focus on the handling books of accounts properly. However, owners want up-to-date correct information of the company’s financial situation that can be assured. So, owners demand audit despite not required by law. Similar views were also stated by Mehrdad Naurbakhsh, and Monica.

4.2.3.2 External Factors
In regard to the external factors for audit demand, according to Mehrdad Naurbakhsh, there is a demand for audit due to the taxation. He stated that the when accounts are audited it is easy to claim the right amount of tax to be paid to the tax authority. Furthermore, he added that banks also demand the audited statements before granting loans to the company for their own security reasons. Eva Lindh-Holmgren stated that the demand for audited financial information can also arise from the creditors like banks and suppliers to see the credibility of the company before giving loans and credits. The taxation authority can also demand the audit reports to make sure that the company pay right amount of tax or not.

In the words of Rydfjäll besides the owners, the outsiders can see whether the company’s financial position is good or not, they want assurance of good book-keeping and sound financial position that is certified by an external person. Also, he mentioned that it is also the bank who demands the audited financial information before granting the loans to the company.

Eva Brändström stated the audited financials are also demanded for taxation and banking purposes i.e. bank loan. Banks generally ask for the company audited annual reports for banking loan process. According to Magnusson banks never provide the loans without presenting the audited financial statements, as it is only the papers the banks can rely on. Banks think the audited papers show the real picture of the company. He further added that, it is also too important for the taxation, for paying the right amount of tax to the government. Magnusson stated that creditors and suppliers also want the audited information to check whether the company’s financial position is good enough or not.
According to Hans Hällström it is the tax authority who demands the audited financial information of the company to be sure that the company is paying the right amount of tax or not. The tax authority relies that it is the audited reports that confirm the actual amount of tax the company needs to pay. The respondents like Ludvigsson, and Hardell also stated that there is audit demand from outside the company like banks, in case of banking loans; tax authority during the tax assessment. Frida Palm stated that it would be the banks who will demand the audit financial information when companies approach for loans from the banks. The customers can also demand for the audited financial information if the companies are bigger.

Westin stated that the audited financial information is demanded by the creditors for some cases, also the tax authority during tax assessment. Banks also do demand the financial information that is audited when the companies go for loan. Susanne Loven stated that the audit is demanded by the tax authority and also the banks if they have loans. Rezza Dehad, and Maria Fransson also believe that the external demand for audit arise for the taxation and banks in case of banking loans. According to Westin, audit is demanded from the external parties like bank for instance, if the company has loan with the bank. The tax authority also demands the audited report during tax assessment. Similar views were also of Stefen Nilson for the audit demand from outside the company.

Sjöberg believes that audited financial statements are more demanded for taxation purpose than bank loan. He believes that banks can have other crediting rating mechanisms than just the audited financial statements to look after for granting the loan. According to Lindström, the audited financial statements are more demanded by the outsiders like banks and tax authority, especially in regard to new companies and new owners.

Synnöre Andersson and Monica think audited financial statements are demanded by the tax authority. Audited annual report helps in easy and correct tax declaration, and the owners do not want to take any risk with this matter. Furthermore, Synnöre Andersson adds, it is also the banks that demand the audited financial information when approaching loans from them. The investors would also demand the audited report for their assurance to see the company’s actual situation and guarantee their investments. Mikaelsson mentions that the audited financial information is demanded by the investors to see the creditworthiness of the company and also for the taxation purpose for paying right amount of tax.

4.2.4 Favourableness of Audit exemption for the small companies

Regarding the new rule, most of the respondents were positive. They think it is really good decision by the government by removing the compulsory requirements of audit for small companies. Besides, according to Holmgren, it is also good with an option to do for those who want to do audit. No doubt, there is involvement of cost in doing audit, the respondents’ opinion that the cost can be minimised if option of not doing is choses. Most of the respondents argue that audit cost is generally expensive and think the new rule for small companies is economically favourable.

However, Ludvigsson stated that it can be economically favourable at present by using this facility, but in long run it can be costly to the companies i.e. by discontinuing audit; it takes time to see the real impact of it. According to Hardell, besides small companies can save money by not doing audit, he thinks that many small companies need help in maintaining and verifying the financial information as they lack proper knowledge and manpower. He further adds companies grow as time passes and they need some professional help in this regard, for making themselves sure that their financial information is correct. However, the option to use or not in the right way should be motivated thinking about the benefits the company itself.
Audit from audit exempted SMEs in Sweden

Frida Palm also stated and appreciated the new provisions for small companies regarding audit rule, besides she stated that it is also more worthy the money in spending in audit too.

4.2.5 Doing business with companies without audit

Despite the fact that most of the respondents believe it is economically favourable for small companies by not doing audit, they prefer to do business with companies with audited financial statements rather than with those companies without the audited financial information. The respondents stated that it is the audited financial information the outsiders can know how the company really is, whether it is good or bad, and whether the company is creditworthy and good image to do business with. A company without audited financial information is difficult to trust and might cost extra cost when it needs to track their history.

But some respondents like Ludvigsson, Stefan Nilsson, Sjöberg were different regarding this aspect. In this regard, Sjöberg stated that the trust and relation matter more than just the audited financial statements. If the companies can create good trust and relation with each other, unaudited companies can be a good partner in doing business. He believes that, business does not work only with paper, the trustworthiness; truthfulness and sincerity in business are more important aspects than the financial information being audited. In real world, business especially in small companies, market is also small and the people we need to deal with is also limited, so the company cannot be concerned only with the audited financial statements, more importantly it is also the social relations and networks that help to promote the business in an easy way. Synnöre Andersson opinions that, there are also other ways to analyze whether the company is good or bad, credit ratings agencies, and also from the taxation authority, and important websites where we can get crucial information about the company about the company details, which can be a support.

4.2.6 Bank Loans Aspect

In response to the question whether the company has bank loan at present or not, the table below shows that 9 out of 20 companies do have loans from banks, whereas remaining 11 companies are using their own money / finance to run the company with their own capital only. This accounts 45% companies with bank loans and 55% companies without bank loans.

<table>
<thead>
<tr>
<th>Companies with Bank Loans</th>
<th>Companies without Bank Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>Un Po D’italia AB</td>
<td>Lilla Galleriet i Umeå AB</td>
</tr>
<tr>
<td>Rydfjäll Byggkonsult AB</td>
<td>E L G E Ekonomikonsult AB</td>
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<td>I4m / ERALIX AB</td>
<td>Örjan Magnusson Psykologkonsult AB</td>
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<td>Magazin Du Nord</td>
<td>Lintottens Hårfixeri i Umeå AB</td>
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<td>Handelsgården</td>
<td>Sofiehems Sjukgymnastik AB</td>
</tr>
<tr>
<td>Cafeteria Pronto i Umeå AB</td>
<td>Burmans Musik AB</td>
</tr>
<tr>
<td>Printstore Personal Signs Sweden AB</td>
<td>Frida Palm</td>
</tr>
<tr>
<td>Annaleffe AB</td>
<td>Atelje Koppahettan</td>
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<td></td>
<td>Optique</td>
</tr>
<tr>
<td></td>
<td>Datacenter i Umeå AB</td>
</tr>
</tbody>
</table>

Source: Authors

In reply to the question whether the banks ask for the audited financial statements of the company before granting loans, Naurbakhsh responded that banks generally ask to submit the audited financial report for the company along with other related documents. According to
Audit from audit exempted SMEs in Sweden

Rydfjäll, if a company wants loans from banks, banks are more likely to demand the audit report to know the company’s actual position as the banks think it is important to have it before granting loan. Similar views were also given by Eva Brändström and Westin in case if company wants to approach for bank loans. Magnusson stated that bank ask the audit report, otherwise, they will not grant the loan. Ludvigsson, Hillorn and Hardell stated that banks generally want the audited financial information of the company, as they think it is the quality stamp for the company. According to Stefan Nilsson, banks may ask the audit report if in case they have doubt with financial information provided by the company for loans.

According to Holmgren, it is the trust that is more important than the audited financial information and image of the company. If the company has good relation and trust with the bank, the company can get loan without audited financial reports. Besides, banks do also consider the collaterals and security before granting loans to the company. Synnöre Andersson stated that size and type of the business also do matters when banks decide to grant loans to the company besides considering the audited financial information. Hans Hällström, Lindström, Susanne Loven, Maria Fransson, Monica, and Mikaelsson also stated that bank feels secured with the audited financial information while granting loans to the companies.

4.2.7 The impact of audited financial statements on bank loan interest

In reply to the question of whether the interest rate on loan is lower or higher to companies with unaudited financial information, Naurbakhsh replied yes. Naurbakhsh stated that there is more risk to the banks providing loans to the companies without audited financial statements. This ultimately will charge higher interest on the loans granted, as compare to the companies with audited financial statements. Holmgren stated that it should be the lower interest rate on loan to the companies with audited financial statements. However, the collateral and securities of the company also matters in determining the interest rate on bank loans.

According to Rydfjäll the company needs to pay higher interest rates on the loans from the banks if they do not have audited financial statements. Banks want to feel secure when providing loans to the companies and the audited financial statements can reduce their risk involved that can support for charging less interest rate. Eva Brändström, Hans Hällström, Hillorn, Stefan Nilsson, and Mikaelsson believe that the interest rate on the loan is lower to the companies with audited financial information than the companies with the unaudited financial information. They stated that the interest rate is actually the cost for time value and risk of the banks on the loans. They think that audited information can reduce the risk (information risk) which can help to reduce the interest rate itself.

Magnusson stated that audited financial statements can reduce the interest rate on the loan, but it is up to the banks to decide the interest rate on the loans they provide. According to Ludvigsson, the interest rate on the loan can be negotiable with the banks if the company has the audited financial statements. But the audited financial information is not only the main aspect for lowering the interest rate. Lots of other aspects are involved in the loan process. The financial position and the company’s business also have equal role in determining the interest rate on loan. Hardell stated that the good relation with the banks and other financial institutions also is needed. He thinks that unaudited financial statements do not make huge difference in the interest rate, if the company has good relation with the bank. Westin stated banks will charge higher interest rate on loans to does who do not have audited financial statements. He thinks that the company can demand loan with lower interest if the company has audited financial statements, if not there are other banks and financial institutions to provide loans with cheaper interest rates. Rezza Dehad said that banks will definitely charge higher interest to their clients with unaudited financial statement, because there is more risk to
lend money to such company. Furthermore, banks will charge and expect more for more risky investments. Frida Palm and Sjöberg replied that they have no idea about matter and not sure whether audited statements really matters in determining the interest rate.

According to Lindström, first of all banks will not provide loan without the presenting the audited financial statements. Because it is hard and also too risky providing loans without knowing the correct and credible financial information of the company. For instance, when banks think about providing loans to such companies they have to use other financial measurement parameter and other ways of assessing the company’s creditworthiness. This is time consuming for the banks and at the end banks might increase the interest rate on loans.

Susanne Loven replied that banks will not determine different interest rates on loans to different clients. Loven thinks that the interest rates are generally same for their customers no matter whether the financial information is audited or not. However, there can be personal negotiations and discussions with the banks and the companies regarding this matter. If the banks are satisfied they can rethink.

According to Synnöre Andersson, the interest rate on loans does not depend on the audited financial information. Actually, it depends more on the banks’ rules and regulation regarding the granted loans. If the company meets the banking requirements they can get the loans any time. Audited financial information can also be one of those requirements though. The interest rate also depends up on the best loan the company wants and more importantly the loan depends on the collaterals and securities before taking loans from the bank. Maria Fransson stated that she does not have idea in this regard, as her company is totally owner finance.

According to Monica, audited financial information should matter in the determination of the interest rate on the loans. More important is that the audited financial information is more useful in easy access of loans from the banks.

4.2.8 Auditing as Monitoring and Controlling Mechanism

In the reply of the question whether auditing as a monitoring and controlling mechanism, all the respondents answered yes. Holmgren added that when audit is done by external auditors, the owners can see the real problem of the company for instance the financial transactions are well checked and reviewed and any misstatements are located in time which helps in monitoring and controlling the company. Rydfjäll added that audit benefits a lot more, often to the people (owners) who do not have good knowledge about accounting, and also to those who do not have much time to see by themselves; so rely on the audited financial information as the tool for monitoring and controlling mechanism of the company. Magnusson stated that audit is too crucial for every company, as it certifies the financial information so that the owners can use this in making their business strategies and plan.

According to Hans Hällström, audit is important to all firms, but it is more important for bigger companies than small companies. Large corporations have more business transactions than small companies. However, as for small companies audited figures are also important mechanism for how the owners/managers use this audited information in monitoring and controlling the company’s affairs effectively.

Susanne Loven stated that audit helps to monitor and control the company more effectively and she thinks that it is good to have audited reports. Furthermore, it is the owners who use and conduct audit because audit can locate to do the business in right way.
4.2.9 Owners and creditors relationships

In reply to the question whether audit can improve owners and creditors relationships, Holmgren stated that audited financial information has positive contribution enhancing the relations between the owners and creditors. Holmgren added “it is better for creditors to see how is the company, whether company can be trusted or not”, and the audited financial statements are the only thing creditors can rely on. Naurbakhsh said that creditors prefer to do and continue business with those companies with audited statements. According to Rydfjäll, the audited financial information of the companies has positive benefits to improve the relationship between owners and creditors, because creditors can see the companies’ details about financial position when they like.

Rydfjäll replied creditors are curious to know the companies’ have good financial statements. Besides, creditors are interested whether the companies are sound and solvent. Regarding these issues, only the audited financial statements can make them sure and confirm about the company’s situation. According to Eva Brändström, audited financial statement may improve the relations between the companies and creditors. Magnusson believes that audit has positive influence in the owners and creditors relations. Hans Hällström stated that audit can help in creating good relation between owners and creditors. But, it also depends upon how strong is the financial information of the company. If the company has weak financial position though it is audited, it will not help to improve the relations; instead it will be difficult for the company to improve the relations. Hans Hällström also said that creditors frequently want to do business with those companies having good financial economy and that are also audited, as creditors want to be sure whether the company can pay back their credit amount in time or not. Ludvigsson also responded that the audited financial information can play an important role in improving the owners and creditors relationships. According to Hillorn, audit can improve relation between the creditors and owners because it enhances the trustworthiness of the company. Westin answered that audited financial information are too important to the creditors because it is more trustworthy. The creditors also want to feel secured with the company’s situation. Stefan Nilsson, Rezza Dehad, Sjöberg, Lindström and Susanne Loven also think that financial statements when audited bring more assurance and reliability, increasing the relations between creditors and the company.

According to Synnöre Andersson, yes of course the audit helps to create good relation between the owners and creditors. Besides, personal and social relations are also needed to create favourable atmosphere between the owners and creditors with trust and understanding. Frida Palm, Maria Fransson and Mikaelsson also replied that the audited financial information is a must, for stronger creditors-owners relationships. The companies can get extra benefits from the creditors when companies have good audited financial information. Creditors can extend the credit limits and time in case sometimes when companies are in problems. Monica stated that audited financial information greatly improves the creditors and the company relation as the information is more reliable.

4.2.10 Audit Fees Aspect

To the question that what is the opinion regarding audit fees and whether it is acceptable, Naurbakhsh replied the audit fees is expensive and it is not acceptable for small companies. Holmgren replied that this is hard to comment upon. Holmgren stated that the audit fee is rather high to small companies as compare to other companies. She stated that the audit cost differs depending upon the type and size of company. Despite this, Holmgren stated that the audit fee is acceptable for her company. Furthermore, if the audit fee is not acceptable, it is
worthless to conduct audit despite not required by law. According to Rydfjäll, the audit fee is not so much, and it is acceptable. Eva Brändström stated that it depends upon the auditors too. Some auditors charge more money while others charge less. She added that bigger audit firms charge more as compare to small local audit firms. According to Magnusson, the audit fee is acceptable and is satisfied with the audit service. On the other hand, Hans Hällström stated that the audit fees are generally too high for small companies, despite less paper works. It would be acceptable and good if it is a bit lesser so that more small firms can use and get benefited. Furthermore, the audit fees depend upon the auditors we choose and type of service we want. Both cheaper and expensive auditors can be found in the market. The easy way is to choose the right auditor depending upon the willingness one want to pay for the service. Ludvigsson stated that audit is too costly of the company and it is not acceptable.

According to Hillorn, audit fee is acceptable and it is not expensive. The audit is a professional job/service, and professional service is can be higher than the normal day to day business job. The fees mainly depend on the time and efforts needed for the completion of jobs and also the quality does matter to great extent. Hardell stated that the audit fee, more especially for small companies is expensive. It also depends upon choice of the auditors. Westin stated that the audit cost for small companies is small; it depends on the size of company. According to Stefan Nilsson, the audit fee is not a big deal for the company and it is acceptable. The service is worthy as per the fees for the audit. Rezza Dehad and Frida Palm also stated that the audit fee is satisfactory and acceptable for their company.

According to Sjöberg, the audit fee is expensive for the company and he prefers to pay less cost for audit otherwise audit firm should provide extra audit services in the same cost. Lindström stated that the audit fee is too much cost burden for the company. Susanne Loven thinks that the audit fee is not cheap and they are expensive like lawyers. Synnöre Andersson thought that the fees charged by the auditors for auditing is too high for small companies.

According to Maria Fransson, audit fee is not expensive to the company. The fee is acceptable. Monica stated the company needs to pay higher amount of fees for auditing service, so it is quite expensive to the small companies, as there are no many things to do in small companies. Mikaelsson also stated that the audit fee is high and prefers less cost for hiring the auditing service.

4.2.11 Costs-Benefits Analysis of Audit for SMEs
In reply to the question that how do you think that auditing is a cost burden or beneficial for small and medium sized companies, Naurbaksh replies was that, auditing is cost as well as beneficial to the company. It is a cost burden because it is costly to the company. Though it is cost burden, the company has no other choice besides audit and also no time to do by- self. Despite this, audit has lots of benefits too to the company. The owners feel secured about the company, and it also required by banks when going for loan. The audited financial statements also help in determining the exact amount of tax to be paid to the tax authority.

In reply to the question regarding the expected benefits by conducting audit, Naurbaksh stated that by doing audit, firstly owners/ managers feel secured about the company. The owner can know how the company is going. It is also useful when going for loan. The company can have easy access to finance from banks and financial institutions with the audited financial information, because banks prefer / demand the audited annual reports before granting loans. It is also quite easy during taxation due to audited financial information. The company can easily access the tax amount of the company and pay accordingly.
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According to Holmgren, though audit is costly to small companies, it is good for the company to have their financial information audited. It is not only a matter of money. More important is it the security and satisfaction we get by conducting audit. Audit provides assurance to the owners regarding the company’s financial information. If the company thinks the present audit is costly, the company can hire new auditors with cheaper audit fees. Doing audit by-self is impossible and there is also no other alternative ways for controlling besides hiring for external auditing. The audit has more benefits than the cost it incurs as it is time saving, helps in easy assessment of tax, and besides this society also needs it.

According to Holmgren, the main benefits by conducting audit is that the owner/managers in small companies get the control of their business, feel secured about the company with right and correct information. Most important is that it greatly helps in determining the correct amount of tax to the government; this removes the risk of fines and penalties for paying less tax amount. Audited financial information is also important during the banking loan process as bank rely on the annual reports that are audited by external certified auditors.

According to Rydfjäll, the audit is more beneficial than the cost it incurred. With auditing, companies can see if the business transactions are well organized and checked if there is any material misstatement. It makes feel secure and see how the company is. Besides, the banks can easily grant loans to the company on the basis of audited annual reports of the company. Rydfjäll further stated that the company can easily assess the exact tax amount removing the chances of paying less tax than required.

Eva Brändström stated that audit can be a cost burden for small companies, otherwise it is beneficial. The most important benefits conducting audit goes to the owners/managers and their board members. The owners/managers and other board members are assured about the company’s audited financial information. They can use this audited information in developing news plans and strategies of the company. They are crucial to the company as a whole. The expected benefits the small companies get by conducting audit can be regarding taxation. With the help of audited financial information, the company can easily determine the right amount of tax to be paid to the tax authority. Besides, the company can get benefits in case of banking loans process, because banks generally ask for the company’s audited annual reports before granting loans to the company.

Magnusson stated audit is worthy for the company besides it is small. Its benefit is far more than the cost we pay for it, especially to small companies who have no manpower and also lack sufficient knowledge in handling the annual accounts of the company, so there is a need of second person like auditors to verify our financial transactions as a matter of assurance and credibility. When audit is conducted the financial information are well managed and the owners feel relax about the financial information are error free and reliable. It is also much helpful in determining the correct tax amount that is to be paid to the tax authority. Furthermore, Magnusson added the audit annual reports can be a good source for the creditors to see about the financial positions and performance of the company as they are more reliable and assured. In case, the company needs loans, the audited information can be an important document to the banks to get better picture of the company.

According to Hans Hällström, the audit is more cost burden than the benefits to small companies as there is not more things to do in small company, but the auditors charge for every opening of their mouth. Besides, the audit is cost burden to the company; they do not have other alternative ways instead of auditing that provides similar benefits like that of audit. Though the audit is expensive to the company, it has many benefits the company and the
owners can get from it. The expected benefits that are derived from continuing audits are, security reason, enhance the relations between the partners / co-owners of the company with trustworthy and transparent financial information. Furthermore, audited financial information has of great importance for bank loans and helps in calculating the right amount of tax to the tax authority.

Ludvigsson stated that audit is both cost burden as well as beneficial to the small companies. Audit is cost burden because of the higher audit fees as compare to the size of the company. Actually small companies have less business activities and transaction. But the audit fee is much higher to the company despite fewer things to do. Ludvigsson stated that audit has much more benefits. Firstly it makes the owners get more transparent information of the company and let feel the owners and board members secured with the company’s financial situation whether good or bad. Audited financial information is also too important during the taxation process. The audited annual reports are used as the base in determining the correct amount of tax to the government.

According to Hillorn, audit is cost burden as well as beneficial to the company. But, the benefit of audit is more than the cost for audit. The audited annual reports are mainly important to the owners of the company, because they are the main users who want and need it. The reason behind conducting audit despite not required by law is that owners are more interested with the audited information. It provides them a crucial source of information about their company’s present state of affairs in well manageable way. Besides, the owners feel convenient to declare the tax amount that is required to pay to the tax authority. Besides, if the company needs loans from banks, the banks generally ask the audited financial statements of the company. So, in that case, the audit can be much beneficial tool in getting required finance from banks and fulfil the financial requirements of the company. Furthermore, audited information can also help to improve good relations with creditors / suppliers.

According to Hardell, the audit is more beneficial than cost burden to the company. The benefits from audit could be the correct financial information and helps in controlling the business. The owners feel more secure with the audited financial information because it is more reliable when audited. The auditors are also supportive in fixing the problems in the company related to financial issues which makes easier in solving the problems. More importantly audited financial information is the base in determining the exact amount of tax to be paid to the taxation office.

In reply of the question whether the audit is cost burden or beneficial, according to Westin, it is beneficial tool for the company. The owners and managers of the company feel secured with the financial information and financial situation of the company as all the books of accounts and transactions are checked and are assured regarding the transparency of information. The owners and managers also do not have enough time as well as knowledge to check by-selves. So, conducting audit is the best and convenient solution besides no other easy alternatives instead of audit providing similar results. Furthermore, audit makes easier in tax payment. The owners do not need to see and calculate themselves amount of tax to be paid to the tax authority. Based on the audited financial information, the tax is determined and paid reducing the chances of over-payment and underpayment of tax amount. This removes the chance of fines and penalties due to wrong assessment of tax. Importantly, the tax authorities are more convinced with the audited annual reports than unaudited annual reports. Furthermore, company can easily access to bank loan with the help of audited reports from the bank.
According to Stefan Nilsson, audit is beneficial tool rather than cost burden for the company. The audit is of much importance to the owners of the company as they are end users of the audited information. The audited annual reports provide crucial information to the company with the auditor’s opinions that are valuable to the company in tracing the positive as well as negative sides of the company. In short, it provides summary of the exact situation of the company. The audited information is also helpful in paying the correct tax amount to the government.

Rezza Dehad also stated that the audit is more beneficial rather than cost burden to the company. Rezza Dehad pointed out that it is the security reason for conducting audit by the owners of the company, as it provides assurance of the financial statements and also help in determining the right amount of tax to the tax authority. Audited information is also important to the creditors / suppliers to know about the true figures of the company whom they are dealing with, and of course it is also important for banking loan process besides the collaterals and security. Frida Palm also stated that audit has more benefits than the cost for the service. The benefits conducting audit is that owners feel more secured for the company. It is also easy in bank loan. Besides, audited annual reports also helps in settling the taxation issues.

According to Sjöberg, the audit is more cost burden to the company. Despite its cost burden the company has no other alternative ways for audit. Sjöberg also stated that, the company will continue with audit until it gets other reliable ways like audit. The company would prefer some supportive help instead of audit to reduce the higher audit cost. Sjöberg stated that audit helps in easy access to bank loans. It also helps the company in declaring the right amount of tax to the government. More importantly, the owners feel more secured regarding the company’s business affairs, because it helps in exact valuing the company. Audit also benefits in improving relations with creditors. If new investors are willing to invest in the company / business, the audited financial information can be the catalyst in approaching new investments in the business and grow bigger.

According to Lindström, audit is cost burden to small companies despite little benefits. Small companies have small business activities and the audit is too expensive for them. The audited information is also useful only for limited users. Despite the audit is cost burden, the company is using it as the company have no other alternative right now instead of audit, and the main thing is the owners lack knowledge in the area and are dependent on the audit since long time with handling the financial information and verifying them. Lindström stated that despite the high cost, it is beneficial to the company and the owners to know how the company and how the trend is going. It also helps to pay right tax amount to the tax authority.

According to Susanne Loven, despite the audit is costly to small companies, it is also beneficial to the company. The company also thinks audit is only the option for verifying the books of accounts and making it more reliable and credible for the interested users of the company’s financial information, so the company have not think about any other alternative ways that can substitute audit. Susanne Loven stated that the owner feel more secured with audited annual reports. Especially in a company with more than one owners and partners, audit is the more important to satisfy and create good understandings, trust among all the owners. Besides, audited financial information is quite more important for the taxation purpose. The tax authority do not have to look deeply the company’s financial information when audit; in other words, the audited information are reliable and trustworthy. Audited financial information is also equally important in getting loans from the banks, as banks more often wants the audited papers of the company before granting and processing loans.
In the response of Synnöre Andersson, audit is more cost burden rather than beneficial to the company. The audit fee for small companies is too high. It would be better if the audit fee is less expensive so that most of the companies get benefited with the service despite it is not required by law at present. Despite the audit is costly the company use it, as at moment the company has no other option instead of audit. Furthermore, the company will rethink whether to continue or discontinue in upcoming years.

Synnöre Andersson stated besides huge cost, audit fee do have many benefits to the company as well as other interested parties outside the company. Most importantly, the audited financial information is important and beneficial to the owners and managers of the company as they are more responsible towards the company’s financial matters. The owners want to be assured that the company’s information is correct and transparent and that information can be used productively for the benefits of the company like: in banking loans process and also at the time of payment of tax to the tax authority. Besides, the audited financial information can be the important source of information to the prospective investors of the company.

According to Maria Fransson, audit is more beneficial than the cost burden to the company. The audit has lots more benefits to the company and its owners. Audited financial information provides more assurance and security to the owners. On the basis of audited annual reports, the owners can determine and pay right amount of tax to the government. Also, if the company needs loans from the banks and financial institution, the audited annual reports are demanded by the banks to see how company’s financial details. Besides it can be a useful to the creditors and suppliers to know the company in more detail.

When asked whether audit is cost burden or beneficial to the company, according to Monica, audit is cost burden to the small companies rather than beneficial. Generally, audit fee is too high for small companies. However, the company do not have other ways besides audit at present, and also have no time to do by themselves; small companies have both limited manpower and finance to run the business. The company conducts audit because the owners think it is safe to continue the audit. Audit provides correct figures of the company and there is more transparency regarding the company’s performance. It is also quite important during the taxation purpose, helps to pay right amount of taxes to tax authority. Besides, banks and creditors also like to see the audited financial information of the company before granting loans and credits, as they think it is important. So, if the company has audited annual reports, it is relatively easy to get loans from banks and grant credits from the creditors. The main point to be noted is that the owners do not want any problems in the business, and do not want to take risks and negative impacts by discontinuing the audit just to reduce the cost of it. The company think it would be more costly to the company by discontinuing audit rather than continuing it when it attempts to get external financings, despite not required by law.

According to Mikaelsson, audit is not cost burden; instead it is beneficial to the company. The audit benefits a lot to the owners and also the interested parties of the company. The owners are more benefited with more accurate, reliable and verified financial information when audited. The owners feel more secured with the audited financial information and can use this crucial information in decision making and controlling the company. The audited information is also useful in determining the correct tax amount. The audited information can also benefit the investors and creditors in the deciding about the company’s overall financial position and performance. Furthermore, company can easily access to bank loan with the help of audited reports.
4.2.12 Expected Benefits Vs Actual Benefits
In reply to the question regarding if the expected benefits and the actual benefits do match, Naurbakshah said that the actual benefits from audit is not same as the company expected. The company’s expectation is more than actual benefits. He stated the company also needs freedom to work wants more things from the audit as per the cost for it. Rydfjäll stated that the company is satisfied with audit. Besides checking and verification or annual reports, it would be better if the audit provides other services for example giving advices and suggestions to the company. Eva Brändström stated that the audit benefit is as per the expectation and is satisfied with the service. Magnusson also stated similar opinions. Magnusson is also stated that the benefits from conducting audit are as per expectation mentioned in above section.

Hans Hällström stated a different opinion regarding this issue. The benefits do not match with expectation, but still it is satisfactory. Ludvigsson, Hillorn, and Hardell, stated that the company is benefited with the audit service and it is as per the expectation. Westin, Stefan Nilsson, Rezza Dehad, Frida Palm, and Sjöberg also mentioned that the expected benefits and actual benefits that are derived from audit do match, and the owners are satisfied with the service. Lindström, Susanne Loven, Synnöre Andersson, and Monica are also satisfied with the audit service and it does match with the expected benefits. However, it is good to have supportive role in future in handling the financial matters.

4.2.13 Signaling Benefits and corporate social responsibility (CSR)
In reply to whether voluntary audit has good signalling benefits and corporate social responsibility, Naurbakhsh answered yes. Holmgren stated that voluntary audit provides good signal about the company. Audit report transmits good information about the company, increase goodwill. Doing something which is not really needed is itself is good information to outsiders, as it increase the image of the company. Rydfjäll stated that audited financial information is more reliable, and it is important to the owners and also the society. The information can be helpful for other interested parties. According to Magnusson, audit can give positive signal to outsiders because, it helps in providing verified financial information to outsiders like banks, tax authority, creditors, or suppliers. It is also useful in building goodwill of the company. Hans Hällström stated that conducting audit shows honesty. Audit is itself good thing and an important tool for control system. Cost is not only an important part, transparency and good faith in business is also equally important. Doing audit definitely have positive impact to the company.

Ludvigsson stated that audit can add value to the company. It can work as a tool or catalyst to separate good or bad company providing reliable and verified financial information to outsiders. Hillorn stated that audit report can be a good source of information to the company as well as outsiders. It provides better support during taxation, bank loans process and also to enhance the relations with creditors and suppliers that are good parts we get from conducting audit but that may not with the companies not doing audit. Hardell also stated audit provides signalling benefits to the company. Westin mentioned that as compare to the companies without audited reports, the companies with audited financial information has positive signalling benefits and it also contribute as CRS, by giving right and information to the society. The audit report can also be useful for business but also the researchers and academicians. Rezza Dehad also stated that audit has more advantage and good signalling benefits as it increase goodwill and trustworthiness. It is more important to companies like restaurants where trust is the main thing.
According to Frida Palm, a company with audited financial information has better signalling benefits. Being a part of society it also good to thing about society. Providing right and transparent information to society is also the duty of a company and it fulfils CSR to some extent. Sjöberg and Lindström also stated that audit is beneficial in transmitting positive information of the company. Susanne Loven stated that, besides audit has numerous benefits. It brings better competitive advantages in regards to banks’ loan, easy taxation, and better relation with suppliers than the company without audit reports. According to Synnöre Andersson, audit may help in signalling benefits. It can built good image of the company. Maria Fransson stated that as a corporate person it is good to provide right information to the society; and in this regard, audit can be a good way towards CSR. Monica stated that audit can contribute the company and can play as a signal of a good company. It can also contribute in CSR as the audited information can beneficial to the interested parties like government, tax authority, creditors, suppliers and customers and society as a whole. Mikaelsson also replied that audit has good signalling benefits to the company.

The following section will be presented empirical findings of audit demand for SMEs from bankers’ perspective.

4.3 Bankers’ perspective of audit demand for SMEs

When it attempts to collect bankers’ opinion of audit demand for SMEs, the interview guide is categorized into four categories namely relationship between banks and SMEs, role of auditing for SMEs, the impact of audited financial statements on loan interest rate and bankers’ opinion on new legislation of audit exemption for SMEs.

4.3.1 Relationship between banks and SMEs

Regarding with the relationship between banks and SMEs authors discussed four main areas with bankers. First the involvement between banks and SMEs and are there any separate unit only deal with SMEs clients are discussed. Second authors ask the question related with when banks grant loans to SMEs what are the major criteria have to consider. Third when it comes to ensure the creditworthiness of SMEs clients how do banks assess the risk factor of client firms and for credit rating of SMEs how do bank manage with it. Finally lending techniques of bank when they already decided to grant loan to SMEs is discussed. Authors also ask besides granting loans to SMEs, are there any kind of services bank used to provide their SMEs clients.

The relation of banks and SMEs

According to market analysis of internet banking bankgiro system Marie and Mikael said the market position approximately 38% to 40% of corporations in Umeå are clients of Swedbank. Swedbank used to do business with SMEs that could be described as financing, cash management services, and even investment. Alexander said that the primary financial involvements between Handelsbanken and SMEs is granting loan. And others involvements could say as credit card services, internet services for receiving and payment transactions. Annika also said that granting loan to SMEs is a major involvement of Nordea bank. As per reply of Fredrik, Denske bank used to do business with SMEs which at least have the criteria of turnover ten million Swedish Kronor and the primary involvement is financing to SMEs clients. According to Maria and Martin, Forex bank in Umeå did not directly deal business with corporation but granting private loan to owner of SMEs could say as the indirect way of financing involvement between Forex bank and SMEs clients.
The question related with are there any separate unit within bank which is only communicate with SMEs, Marie and Mikael said that they could not say they have a separate unit. But they do have specific responsibilities for instance in corporate department which is only deal with corporate loan, four out of sixteen people are working for granting corporate loan to SMEs. Fredrik also said that since they are mostly working for corporate loan they do have separate unit within branch who are responsible for SMEs clients. Alexander replied that they do not have separate unit for SMEs, everything is done within the branch. According to Annika, they do not have any special unit for SMEs clients but of course they have different responsibilities for clients. Maria and Martin said that there are no separate unit and specific responsibilities in their bank. Everyone has to ready for all customer services.

Bankers’ opinion of criteria for granting loan

In response to the question regarding the important criteria have to consider when granting loan to SMEs, Alexander replied that the most important is the good credit history of borrowers. When it comes to identity whether the borrower is creditworthy, first they considered borrower firms’ financial reports. They did cash flow analysis and took into consideration the balance sheet figure of equity and earning situation of borrower firms. After analyzing the hard information from financial statement, Alexander said that the soft information of client firms are also important criteria have to track in order to ensure the credit history of clients. Whereas the number of employees employed within the companies is not the important criteria as for bank when they considered financing to client firms.

In the reply of Mikael, the important criteria as for small and medium-sized entities can say as the financial situation and the history of owner. According to Mikael’s opinion this study definition of SMEs criteria 30 million Swedish Kronor turnover, 1.5 million Swedish Kronor balance sheet total and up to 3 employees are rather small and they could say as micro-sized companies. So that owners’ personal profile is also an important criterion have to consider. Non-numerical criteria of owners’ confident, skills, business idea and their business plan are also important facts that banks have to identify. If the companies are bigger than micro-sized, they considered the market position of clients firms and business categories instead of intensive tracking of owners’ personal information. Besides that, client firm financial situations have to analyze even though they are micro-sized companies. Cash flow statement is the most important financial criteria to analyze in order to ensure the credit risk of clients.

Marie in her answers to the question related with important criteria bank has to consider when they grant loan to their client firms is that the probability of payback the loan amount what bank lent could say as the most important criteria. When it comes to consider the probability whether client firms can pay back or not, bank used to use traditional way of cash flow analyzing. After analyzing the cash flow statements, bank made their own internal ranking to client firms. Based on that ranking point, they consider whether clients are creditworthy or not. Another criteria what they consider is that the amount of collateral plagued by clients. The better the collateral, there will be more chances to finance the client firms. They have their own definition of identifying small or medium-sized corporations. As per their own definition of categorizing client firms, if the client firm is rather small banks have to track owners’ and companies’ credit history. They used to consider the data available from (www.uc.se) when it comes to analyze the creditworthiness of client firms.

As per Fredrik replied to the important criteria to consider when granting loan, he said that this study sample companies are relatively small in terms of turnover and balance sheet figures. They are not used to do business with this kind of micro-sized companies and most
of their client firms’ turnover figure at least has over 10 million Swedish Kronor. Most of their client firms have turnover ten million to thirty million Swedish Kronor. The important criteria for financing what they consider are positive cash flow, type of business and specific business plan for the future, the amount of loan clients intend to borrow and credit risk situation of companies. Collateral and deposit are also important criteria when it comes to share the risk SMEs.

Fredrick said that above all criteria what he mentioned is interconnected. When they knew the loan amount the clients intend to borrow, they will look into clients’ business information in order to get better understanding of client firms. For example in which business sector the clients are in and what is the clients’ business plan. If the loan amount is higher, the more detail information bank has to gather. For the ability to pay back bank loans, they will analyze through clients’ financial statements particularly cash flow analysis must be done. They used their internal rating when the client companies are small sized in regards with their own definition of categorizing companies. As for really large corporation they used both internal and external credit rating in order to ensure the credit risk.

Related with the criteria have to consider when it comes to grant loan to SMEs, Annika said that they have to analyze client firms’ financial statement and also take into account the business planning. Regardless of the size of the client firms the most important criteria is the creditworthiness. When it comes to identify whether the client can pay back the loan, they used internal ranking of firms. For internal credit ranking, cash flow analysis is one mechanism when they identify company liquidity position. They have to analyze whether company current liabilities can cover by the cash flow generated from operation. If the client is newly starter, owners’ soft information also has to track.

According to Maria since their bank does not directly grant corporate loan, owners’ personal information is the most important criteria have to consider. When they track owners’ personal information and credit history, since this is a private loan first they have to make sure whether clients have steady income and job. Maria also said that nationality is also an important criterion since they did not grant private loan to foreigners. Moreover, clients have to specify their detail plan of what they planned to do with granted loan. Thereafter they have to track the client credit history. Maritn mentioned that currently their bank only grant private loan to clients so that they need intensive tracking of client personal information. They used data available from Kronofogden that is a government agency handling all debt collection in Sweden. Moreover they also track client credit history by using clients’ Swedish personal number from (www.uc.se). After doing these analyses, they decide whether grant loan or not.

SMEs and risk assessment

Regarding with the question how do bank assess the risk factor of SMEs clients, Fredrik and Alexander replied that they did internal credit rating for small and medium-sized companies based on companies’ current cash flow position and at least two years back financial figures. As for large corporation besides their internal credit rating, they also used credit rating provided from external credit rating agencies for example Standard & Poor’s and Moody’s. Fredrik also mentioned besides those rating they also considered the collateral value when it comes to share the risky nature of newly started companies. In the reply of Annika, they only use their own internal credit ranking regardless of the size of companies. She said that financial reports are the most important tracking tools when they attempt to assess the risk of clients. Besides that if the client companies are newly started, they have to track soft
information of clients. Soft information she mentioned as owners’ credit history that is what they consider when it comes to rank credit risk of clients.

In replies of Marie and Mikael related with how do they assess risk of clients, regardless of the size of client firms they used both internal and external credit rating systems. As for internal rating system, cash flow statement analysis and clients’ payment history are considered. They used the external database of clients’ credit reports and other financial analysis from UC AB (largest credit information agency in Sweden). Thereafter, the collateral value is also take into consider for sharing the potential credit risk. According to Martin, when tracking client credit risk, they also used the database from UC AB. Since they only grant private loan to owner of SMEs, intensive personal information have to collect when they assess the potential credit risk of customers.

**Lending techniques for SMEs**

The question regarding with lending techniques of banks when they grant loan to SMEs, Alexander, Fredrik, Annika, Marie and Mikael replied that credit scoring lending technique is mostly applied for their SMEs clients. Credit scoring technique means that they made ranking of clients based on financial statements and credit history of clients. If the credit score is better, clients will have more chances for getting loans. According to Alexander and Annika, collateral assets are perhaps important but that is not the primary lending technique. Credit rating of companies based on financial statement is the primary criteria when it comes to grant loan.

In the reply of Fredrik as for really large corporation financial statement lending is mostly used. Financial statement lending technique is based on the quality of audited financial statements. Fredrik also mentioned that regardless of the size of companies the primary criteria for lending based on the quality and reliability of financial statements. Based on financial statements they will make ranking if the firm got lower rank no matter how much collateral plagued in, they will not consider for granting loan.

According to Marie, the collateral is perhaps important but they could not grant loan only after looking the amount of collateral assets. If the company is newly started in the market, it would be good when clients will plague more collateral. Besides that, they have to have better understanding of clients’ business. And the question regarding with longer relationship with clients are there any economic favorable clients will have, Marie replied that if they know so well of clients that would be good. But they still have to analyze the clients’ credit record no matter how long the communication between bank and client is. She also mentioned that it is still tricky to say that they will grant loan to this kind of clients without having credible financial statements.

Mikael also replied that regarding with collateral assets as for large corporation they can take real estate as collateral but that is just for better loan principal and favorable interest rate. As for SMEs, owner personal grantee also needed besides inventories and machineries as collateral assets. But collateral lending is not common lending technique when it comes to grant loan regardless of the size of entities. According to Martin and Maria, since they do not have direct relation with companies it is tough to say what type of lending techniques when granting loans. But Martin said that they are not completely using the relationship lending methods of closer look on clients’ financial and non-financial information especially loans what are aim for business. They also do have credit risk analysis and rating creditworthiness of customers based on credit records and database available from UC AB.
Bank as a consultant

The question regarding whether bank can act as a consultant for SMEs, Marie said that they have advisors who could say as a consultant especially for investment decision. She also mentioned that they would like to do more consulting services for clients. Mikael said that they provide consultant services especially in four main areas namely loan services, cash management services, pension and saving. According to Fredrik, they used to give advices to their clients when they demand for instance loan, payment, saving, trade finance and so on.

Annika replied that currently they do not provide any consulting services out of banking service package what they could provide for clients. And she also said that especially for newly started entrepreneurial business, there are government agencies and other special institution used to providing financing and investing advisory services. In the reply of Alexander, they do not have any particular consulting services for clients out of banking services. They used to provide banking services such as internet banking services, pension and so on. He also mentioned that clients used to get financial consulting from auditing firms. According to Maria and Martin, they do not provide consultant services for clients.

4.3.2 Role of auditing for SMEs

When it attempts to collect data regarding bankers’ opinion of role of auditing for SMEs, we interviewed five areas. First bankers’ opinion of SMEs clients with audited financial statements. And second how bankers view on SMEs clients without audited financial statements. Third we discussed whether bank will demand audited financial statement despite that client companies are within the audit exemption criteria. Next authors asked the question regarding are there any alternative way of monitoring client firms’ financial performance besides audited statements. Finally data related with cost and benefits of audited financial statement from bankers’ perspective is collected.

Bankers’ opinion on SMEs with audited financial statement

The question regarding bankers’ opinion on SMEs with audited financial statement, Alexander, Fredrik, Marie and Mikael said that currently they do not have clients without financial statements audited regardless of the size of the companies. Alexander, Fredrik and Marie said that they prefer to grant loan to clients who have financial information audited. Besides that, Alexander and Marie also mentioned that the quality of audit is also very important. When it comes to say the audit quality, Alexander and Marie replied as it would be good the audit is done by reputable auditing firms and/or certified auditors whom they could trust. Annika said that audited financial statements are primary requirement since their bank only used own internal ranking based on reliable and credible financial information. According to Martin and Maria since they do not grant corporate loan, audited statement is not an important matter than owners’ grantee of loan repayment.

In the reply of Fredrik, Mikael and Marie, why bank usually ask for audited financial figures is that in order to ensure the credibility and reliability of financial performance of companies. With this regard, she said that the primary role of audited statements for SMEs as credibility and reliability requirement when SMEs ask for loan. When asked for other role of audited reports for SMEs, Marie and Annika said that since they do have their own internal judgment whether clients are creditworthy or not, audited statements alone could not tell as monitoring device. Besides that, related with information sharing criteria Marie thought that might be primary role for investors, managers and owners of companies. As for bank, credible financial statements requirement is more important than others role of auditing for SMEs. Marie and
Alexander also replied that the role and quality of audited statement also depends on the auditors.

**Bankers’ opinion on SMEs without audited financial statement**

The question related with whether grant loan to clients without financial statements audited Fredrick said that whether granting loan to SMEs clients primarily based on credible and reliable financial statement figures. If client companies could not provide audited financial figures, they do not prefer to grant loan.

Alexander mentioned that if clients do not have audited statements there are many parameters bank have to consider whether finance or not. He said that usually new starter companies do not have their accounts audited. Those kind of clients ask for corporate they will look into clients’ business forecast and plan, and clients have to provide all financial figures for bank internal rating. Besides that financial figures have to be as reliable as audited statement financial figures. Alexander also said that besides financial information they will consider owner’s leadership, management, trustworthy and they require grantee of owner if company will go bankruptcy owner has to take full responsibility.

Marie in her reply, since the legislation of audit exemption for SMEs is still new for them currently all clients are continuing their accounts audited. She also said that if sometime in the future when audit exempted clients will stop financial statements audited as for bank they have to think about other alternative way in order to ensure the default loan repayment. Currently, an audited financial statement is the primary requirement for companies who would like to get bank loans. In Mikael’s opinion if clients do not have accounts audited, there might be subjective judgment when to consider possible default risk of client firm.

According to Annika, if clients could not provide their audited statements it is also possible to consider for financing. But companies have to have income statements, cash flow statements, balance sheet and statement of owner’s equity. Besides that, Annika also mentioned that bank has to make intensive analysis of financial and non-financial information for those kinds of clients without accounts audited. Annika mentioned that for companies without audited accounts first bank has to analyze whether financial statements figure are true and reliable after that have to make credit rating, she would like to say it is time consuming and additional cost incurred for bank. When they decided to grant loan, bank will ask for high level of collateral assets, principal loan amount could not be matched what clients demanded for, owners’ grantee for loan repayment, short-term loan duration and interest rate will be higher than clients with audited statements.

In replies of Marie and Martin, since they do not grant corporate loan to customers audited statements are not primary requirement. Owners’ credit history, income, job, grantee and how clients plan to use bank loan are primary requirements for their bank. In this regard, Martin said that as for private loan, clients do not need to provide companies’ audited financial figures. Whereas, he also replied when they know if clients planned to use private loan for his/ her company bankers have to track both personal credit history and company financial information from UC AB.

**Audit demand from banker**

When asked for the question related with audit demand from bank, Alexander, Annika, Fredrick replied that yes they demand audited statements of companies when they consider for financing. Mikael said that in this present, yes it would be good if clients have audited
accounts. According to Martin and Maria, they do not demand. And Martin also said that if personal loan aimed for business use it would be good company has audited reports. Authors asked for why bankers demand accounts audited, Fredrik said that since they have to know companies’ financial situation audited statements are the primary matter bankers have to analyze.

In replies of Marie, all clients provide accounts audited with this regard currently there is no other way than audited statements of companies when it comes to track financial position and consider for grant loan. Marie also said that especially for clients who have been got loan form bank and those clients are within audited exempted criteria, it is tough to say as because of bank demand companies’ financial statements must have audited. Marie would like to say that it also depends on the trend of clients continuing their financial statements auditing. She said that for example when 9 out 10 clients will stop having audited accounts, bank have to think about other way instead of audit. But for large companies with multiple subsidiaries and complex business structure, bank will still demand for external audit.

**Alternative way for audit exempted SMEs**

Authors asked the question related with is there any alternative way for audit exempted SMEs instead of their financial accounts audited, Fredrik replied that currently there is no other way than audited figure if clients want loan. Alexander replied that since currently no clients without audited statement when asked for loan from bank, he do not think there is other alternative way for SMEs clients.

Annika answered that since decision regarding whether to grant loan or not is greatly depend on audited figures. Besides that in Annika’s reply, their internal credit rating required audited figures so that she could say there is no alternative way. But Annika also mentioned that for current clients who are in the criteria of audit exempted SMEs if bank has better understanding of clients’ business situation and plan, good credit history and clients’ financial statements are as good as audited statements, she could say there is alternative way. This is their internal credit rating and financial analysis way for existing client who want to stop audit. But for new clients regardless of audit exempted Annika said that audited statements have to provide if they want loan from bank.

In Mikael’s opinion, when it comes to grant loan the way of analyzing clients is how bank confident about companies’ financial figures and owners’ skills and history. Marie said that currently she has no exact answer how to react for those audit exempted clients. Mikael and Marie said that might be acceptable alternative if clients could provide annual reports, monthly reports, business model, cash flow and budgeting. Mikael also replied that if bankers have to spend so much time on clients’ financial information even when bank will grant loan there will be differences between clients with and without audited statements.

**Audit is a cost burden or benefits for SMEs from bankers’ perspective**

When asked for bankers’ opinion of cost and benefits of having audited financial statements, Alexander replied that audit fee is also depending on the degree of audit of services what clients needed. If companies willing to have consultant services, financial accounts audited and other kind services, that might be costly for SMEs. But for instance clients only need financial statement audited that will cost approximately 10,000 Swedish Kronor per year. In his opinion this is not a big deal. If clients do not have audited statements, they will face more difficulties when they need bank loan than audit cost. Besides that, less chance to get loan than clients with audited financial statement.
Fredrik replied that if clients did not provide audited figures they will not consider for granting loan. In this regard he thought that without audited statements might be more costly than the audit fee paid. And he also mentioned that not only for financing relation with bank having accounts audited could get advantages for company itself as well. According to Martin, even if clients intended to use private loan in his/ her business and he/ she is not the one who is working for daily operation, having financial statements audited could say as advantage of owner.

In Makael’s opinion for SMEs clients, audit fees will be charged around 10,000 to 20,000 Swedish Kronor. He said that perhaps it a lot of money but clients has to think about because of this audit fee what positive consequences they can get back. Mikael said that clients have to consider for example because of having audited statements they can get loan and can invest and so on. With this regard Mikael said that benefits could outweigh its cost incurred. According to Marie, especially for micro-sized companies audit fee it perhaps a great cost. She said that it is tough to say whether more benefits than cost or not.

4.3.3 The impact of audited financial statements on loan interest rate

When it comes to collect data regarding the impact of audited financial statements on loan interest rate, authors discussed whether bank interest rates are fixed for all clients or it can be flexible. Authors also asked what criteria have to consider grant loan with fixed or flexible rate. And when clients have their financial statements audited whether bank grant loan with lower interest rate.

**Fixed or flexible interest rate**

According to Marie, bank interest rate is flexible. This flexible rate is based on credit rating of clients. The clients who got good rate then considered as reliable and creditworthy clients. She said that for those clients interest rate will be lower than others client who got low ranking. Martin mentioned that private loan interest rate is also flexible. He stated that private loan interest rate varied 3.95% to 12.95%. Within this range, low or high interest rate is based on how trustworthy the client is. When it comes to say reliable client or not, bankers made analysis of clients’ credit history and some other important soft information tracking. Based on the outcome of their analysis, better clients will get lower interest rate.

Alexander replied that mostly flexible interest rates are used for SMEs clients. The determination of flexible rate is based on bank internal credit analysis of clients’ liquidity position and market interest rate and market liquidity condition. The range of flexible interest rate means that depending on credit rating of companies how much lower or higher from official STIBOR (Stockholm interbank offered rate) plus interest rate. He also mentioned that real estate companies turns to choose fixed interest rate. According to Annika, whether fixed or flexible interest rate determination depends on loan amount, purpose of financing and types of industries.

In reply of Mikael, most of SMEs’ interest rates are flexible. But more and more real estate companies want to get fixed interest rate. Mikael mentioned that currently 20% of real estate sector turns to have flexible interest rate. Because large portion of real estate companies’ balance sheet is loan amount and now market interest rate is going up and up. Because of increasing interest rate, real estate companies want to have fixed interest rate in order to secure the interest rate.

According to Fredrik, they have both flexible and fixed interest rate when it comes to grant loan. The flexible interest rate is based on internal and external credit rating of companies and
then internal credit analyst determine the interest rate for clients. The lower or higher flexible rate is calculated on STIBOR from Riksbanken (Sweden’s central bank) rate plus lower or higher margin percentage. For example if client’s credit rating is better, the lower margin will be added on STIBOR%.

**Audited financial statement and interest rate relationship**

When asked for whether clients can get lower interest rate if they have accounts audited, Fredrik said that determination on interest is based on credit rating of audited figures so that audited statements are very important to get better rating. Consequently, clients with good rating will get lower interest rate than poor credit rate clients. According to Annika, lower interest rate could be reasonable for clients who have good internal credit rating. With this regard, she said that, clients’ financial information audited have positive impact on getting lower interest rate. Mikael in his reply, lower flexible interest rate could say as a benefit for clients with good credit rating.

According to Alexander, clients who have good credit rating can get favorable interest rate. But he also mentioned that it is hard to say how they will react when clients will stop their accounts audited. Marie in her reply, it could be lower interest rate for clients with credible audited financial statements. Marie also said that currently she still has no idea yet whether to charge higher interest rate when clients will discontinuous their accounts audited.

**4.3.4 New legislation of audit exemption for SMEs**

Questions related with bankers’ opinion on Swedish new legislation of audit exemption, authors asked three areas. First why Swedish new audit exemption legislation criteria are much lower than criteria of European Commission is asked. Besides that, authors discussed are there any influence of new legislation and banker. Second question is related with when existing clients will discontinue their accounts audited in this regard how bank will react. The last question is related with bankers’ opinion on voluntary auditing of audit exempted SMEs clients.

**Bankers’ opinion on new legislation**

Regarding with the first question, bankers’ view on new legislation, Fredrik said that in Sweden the number of SMEs are much higher than large corporations so that it might be one reason of criteria is lower and most of SMEs have to have audited accounts. Moreover, for example in UK there is other way for financial statement analysis than auditing. But in Sweden bank needs third party (auditor) sign for whether clients’ financial figures are correct. He also mentioned that the criteria of audited exempted companies are just micro-sized companies so that other small and medium sized companies have to go for audit. He does not think that this Swedish new legislation is a barrier of bank and clients relation.

According to Alexander, SMEs are the major players in the market since there is not much large corporation in Sweden. He also mentioned that other EU nations might have other judgments than audit but in Sweden audited statements are important when it comes to consider grant loan. With this regard why audit exemption criteria are low and audit demands could say quite high in Sweden than other EU countries. Alexander said that if Swedish legislation is same with EU, there will be a lot of companies within audit exempted criteria. And if they want to stop counts audited, as a bank they have to think about other judgment than audit. With this regard, he said that for Sweden this legislation is not bad. But he also said that it could be barrier for clients who have good credit history, good business plan and forecast when they want to stop their financial statements audited.
Marie in her opinion, there are so much SMEs because of that the audit demand for SMEs is higher. She also mentioned that there might be because of political reason for instance tax authority want to have transparent financial statements for taxation purpose. Marie also said that for audit exempted SMEs first it could be barrier. And she said that if bank could consider other way than asking for clients’ financial statement audited that might be strengthen bank and client relationship.

Annika replied that approximately 90% of companies in Sweden are SMEs because of that the mandatory audit requirement is high. She said this legislation is a barrier between bank and audit exempted SMEs. In Mikael’s opinion, political dimension could be a reason why there is such a difference between audit exemption criteria of EU and Swedish new legislation. He said that tax authority wants to make sure the companies’ taxable income situation. Mikael said that since numbers of SMEs are much higher than large corporation in Sweden government has to control potential fraud occurrence from those large number of SMEs. He thought that Swedish new legislation is good and could not be a barrier between banks and SMEs clients.

Discontinued audited statements

When asked for if existing clients will stop their accounts audited, Marie said that as for existing clients who have good credit history, budgeting and others financial statements are as good as audited one bank will not stop financing to them. According to Mikael, bank will not stop granting loan to existing clients who want to discontinue their accounts audited. But since bank has to take more times on financial analysis than before, because of that bank might charge high interest rate. Moreover, for new clients if they do not have audited statement, they will have less priority than clients with audited figures.

Annika replied that for existing clients with longer relationship and good credit records, bank will not stop granting loan as long as clients can provide reliable financial statements. But she said that whether higher interest rate or same interest rate is based on internal credit analysis. If companies credit rating without financial accounts audited is same as before, bank will not charge higher interest rate because of lacking audited statements. Annika mentioned that if credit rating is not acceptable they will stop grant loan to them even they will not consider still financing with high interest rate. Annika also mentioned that new client who has audited statements before but not existing client of bank and already discontinued accounts audited, they will demand for audited statements.

According to Fredrik, when clients will stop providing audited financial figures that is hard to say how bank will react. He said that bank might stop financing involved with those clients since audited statements are primary parameter for credit rating of companies. Alexander said that it is a problem for bank how to react with existing clients who want to stop financial accounts audited. He said that if internal credit rating of those clients is still acceptable, they will not stop grant loan.

Bankers’ opinion on voluntary audit

According to Mikael, why audit exempted clients still continuing financial statements audited is mainly because of banks have interest in audited figures. Besides that not only with relationship with bank, as for company having audited statement is good when it comes to communicate with investors, suppliers and creditors. If company’s managing and operating is not done by owner only, audited statement should have it. Marie said that the increasing trend of voluntary audit might also influencing SMEs clients to keep going their financial
statements audited. She also said that in future if there are lots of clients who want to discontinue auditing as a bank they have to think other way. And she does not think that because of bankers’ demand, companies still going for voluntary audit.

In Annika’s opinion, voluntary audit could say as has an impact on banks’ influence. When it comes to analyze whether clients is trustworthy, banks used to demand audited figures. Besides that credit rating for companies and lending decisions also greatly depend on audited statements. However, Annika does not think that SMEs voluntary audit is totally because of banks. For SMEs themselves got some other advantages besides high probability to get loan from bank so that clients still continuing. According to Alexander, perhaps they demand for audited statements when clients want external financing from banks. He said that it could be because of bank demands for audit. Fredrik replied that why client going for voluntary audit is that primary because of requirement from bank when clients want to get loan. Fredrik also said that clients also knew other positive impact of having accounts audited besides bank loans. For example, better communication and information sharing with shareholders and stakeholders, audited figures can ensure the right amount of tax paid, and even for owners because of transparent information they could control and monitor business well.
Chapter 5: Analysis and Discussion

This analysis chapter will be based on empirical findings of chapter 4. The empirical results of this chapter will be directed towards when it comes to answer our research question. Furthermore, bankers’ perspective will also be taken into account for confirming the SMEs’ opinion of expected benefits on continuing audits despite not required by the law.

5.1 Bank loan aspect

The empirical findings in respect to bank loan aspect will be analyzed and discussed from SMEs’ as well as banks’ perspectives. Each perspective will be divided into subheadings depending upon the subject matters for better presentation in regards to the empirical evidence.

SMEs’ perspective on bank loans

According to Brannstrom (2005), the audit facilitates the firms to obtain capital and funds. Moore & Ronen (1990) also state that the audit benefits the company for external funds like bank loans. Their findings also support the idea of Collis et al. (2004) stating that companies go for their financial statements audited to satisfy their lenders like bank for granting loans. Kaur et al. (2007) also state audit helps to get better loans. Moreover, Haley & Palepu (2001) opinion audit as a requirement for granting loans from creditors to the companies.

The present empirical findings show that nearly half of the companies interviewed use bank loans to fulfill their financial requirements. Out of total 20 companies interviewed, 9 companies are financed by banking loans whereas remaining 11 companies are financed with their own capital. In other words, we could say that 45% of the companies are with bank loans and 55% of the companies are without bank loans. The empirical evidence show that SMEs perceive that bank hardly provides loans to the companies with unaudited financial information. When companies want to get bank loan, they should have audited figures otherwise banks will not consider for granting loan. Audited financial statements could be described as a security statement for SMEs when they want external financing. It is also found that besides the audited financial information, companies should also have good collateral, trust and longer communication with bank if they can get bank loan without audited statements.

Bankers’ perspective on bank loans

Criteria for bank loan:

When it comes to grant corporate bank loans to SMEs, banks consider financial information and non-financial information of companies. The financial information banks have to gather are borrower firms’ audited financial reports, credit rating of companies from external credit rating agencies and values of collaterals. Among these requirement criteria, audited financial statements are the most important for banks to consider whether to grant loans to SMEs or not. Especially for micro and small-sized companies, banks also need to collect non-financial information (soft information) of the borrowers. These are credit history of companies and owners, business plan and budget forecast, managerial and leadership skills of companies’ board of directors, market position of companies and business categories of SMEs. When it comes to grant private loan to owners of SMEs, banks require more soft information than
Audit from audit exempted SMEs in Sweden

financial information of the clients. For example, banks have to track clients’ credit history, job, income, nationalities, and reason for demanding loan. The most important criterion for private loan is owners’ repayment grantee.

Risk assessment:

In regards to the risk assessment in Sweden, most of the banks evaluate the credit risk of SMEs by using internal and external credit rating of companies. Banks’ internal credit rating is calculated upon audited financial reports of the companies. As for internal credit rating, banks did cash flow analysis of current cash flow position and at least two years back figures, liquidity analysis in order to ensure the creditworthiness of companies and revenue and residual income analysis in order to get true and fair view of current financial position. Banks also use external credit rating from UC AB (largest credit information agency in Sweden), Standard & Poor’s and Moody’s. When it comes to track owners’ credit history, banks use information provided from Kronofogden (government agency which handling all debt collection in Sweden). Besides that, the value of collateral is also taken into consideration in order to share the potential default risk of SMEs. As for private loan, the most important things to consider are borrowers’ credit record from UC AB, banks’ internal credit history of clients and repayment guarantee of owners.

Lending Techniques:

Our empirical results show that credit scoring lending technique is the one mostly used in Sweden. Besides that in Sweden not only small and niche banks are willing to do business with SMEs, all large commercial banks also have business transactions with SMEs. According to empirical findings, credit scoring method is based on financial statements, value of collateral assets and some other soft information for example credit history, business forecast and planning, managerial and leadership skills, etc. After analyzing this financial and non-financial information, banks will make credit rating of the companies. Based on this credit score, whether to grant loan or not is decided.

Ashton & Keasey, (2005) state that transactional lending techniques are probably not suitable for SMEs which are new in the market and default risky nature of its firm, which mean that banks prefer to use relationship lending technique when granting loans to SMEs.

However, our empirical results do not support the above research. Our empirical findings shows that banks tend to use transactional lending technique than relationship lending technique when granting loan to SMEs. Besides that, among the three transactional lending techniques, the banks use Credit Scoring method as their lending technique. In other words, we find that financial statement lending and asset based lending alone are not common methods for granting loans in Sweden. However, the present empirical results of small banks (Forex bank) show that relationship lending and Credit Scoring techniques are not mostly used when it comes to consider for granting loans.

5.2 Role of audits

SMEs’ opinion on Audit as Controlling Mechanism

The primary role of audited financial information for SMEs could say as monitoring and controlling mechanism for their business. Owners demand companies’ financial transaction audited by external auditors in order to get reliable and accurate current financial situation of their companies. Because of having audited statements, owners could see the real picture of his/her financial position and that could be help to make the right decision and control.
Audit from audit exempted SMEs in Sweden

Besides that, strategic business plans, investments and right decision making could be attainable because of credible financial figures. These are reasons of why SMEs have their financial transactions audited. Carey et al. (2000) state that small sized firms go for voluntary audit is to have appropriate monitoring mechanism. Seow (2001) states that independent auditing takes the role of monitoring firm are financial performance attaining credibility and solving agency problem. Furthermore, Knechel & Willekens (2006) state that there is greater internal control in the presence of audit in the company.

Regarding with above empirical findings, we find the different views of bankers and small companies on role of audit. Bankers view the role of audit as a credibility requirement of financial statements. Kaur et al. (2007) found that audited financial reports act as control mechanisms for banks to ensure that firms have a good solvency. From the small companies’ perspective, audit is a monitoring and controlling mechanism.

SMEs’ opinion on companies without audit

Our empirical findings depict that most of the companies / respondents interviewed preferred to do business with those companies who have their audited financial information. It is the audited financial information that is more trustworthy, reliable and transparent which can be relied with assurance. It is hard to believe the company and also their papers which are not really audited and verified by external experts. There underlie more risk doing business with such companies. Because, the unaudited financial information are not reliable and are often can be manipulated easily. Due to this the outside parties don’t really know the exact picture of the company’s state of business, and solvency issue is of big question. So companies generally prefer to work and deal with the companies who have audited financial information as they are more reliable. However, issues like understanding; trust is also crucial aspects in the corporate world. Information from credit rating agencies and other trustful sources can also be a crucial source to assess, evaluate and analyse whether the company’s financial situation is sound enough or not.

Bankers’ opinions on SMEs with audit

In the regard of bankers’ opinion on SMEs with audited financial statement, our empirical findings show that most of the SMEs have their financial statements audited when they go to banks for loans. Besides, banks prefer granting loan to SMEs who have credible financial statement audited. Since most of the banks use credit scoring method when granting loan, credible audited figures are important in order to get reliable credit rate and right decision. From bankers’ perspective, the primary role of auditing for SMEs is to ensure credibility of clients’ financial figures. The role and quality of audit also depend on the auditors’ attitude. In other words, banks view auditing as a guarantee for the quality of information disclosed in the companies as well as a foundation for their credit rating process. Andersson & Paulsson (2005) state that banks believe credit rating would be unsure without audit which supports the findings. As for investors, owners, suppliers and customers of SMEs, the role of auditing could be monitoring and controlling mechanism, information sharing tool and for secure reason.

Bankers’ opinions on SMEs without audit

The empirical findings show that most of the bankers are not willing to finance SMEs if they cannot provide audited financial statements. Since audited accounts are primary requirements for banks when deciding to grant loan or not. Whereas, there is also possible to grant loan SMEs clients without accounts audited as long as clients will provide income statements, cash
flow statements, balance sheet and statement of owner’s equity and other information required by banks. All financial statements must be done in the same way as auditors and have to be credible. As for these clients, banks have to spend extra time in analyzing financial figures and after that make internal rating. There might also be a subjective judgment of clients’ financial and non-financial condition.

Besides that, since external credit agencies based on audited financial figures, clients without audited statements cannot get points from external rating. With this regard, the overall credit ratings of the companies will be lower than that of the clients with audited financial statements. If the credit score is low, the probability of getting loans is also low. Even clients could get loan there will not be same opportunities as clients with higher credit score. For instance banks might ask for more collateral assets, lower principal loan amount, short-term loan duration with higher interest rate and owner of SMEs has to take full responsible if companies go default payment or bankruptcy.

Furthermore, for the companies who have discontinued audit, bankers will not stop granting loan to such clients if they still have good credit score, budgeting and others financial statements are as good as audited one. But, higher or lower interest rate on loans depends on the credit score of the clients. If the clients still keep same credit score despite with unaudited figures, banks will not charge higher interest rate than before. But for new clients who have audited statement before but now already stopped auditing and no credit record with bank, banks will not consider to grant loan or else grant loan with higher interest rate and more collateral assets.

5.3 Interest rate aspect

SMEs’ Opinion

Carey et al. (2000) state that firms believe getting economic benefits of lower interest rate than non-audited firms when it comes to funding capital from external sources like banks and financial institutions. Their findings are consistent with the idea of Blackwell et al. (1998). Blackwell et al. (1998) state that small private firms derived an economic benefit from auditing through significantly lower interest rate than that paid by non-audited firms. Regarding with bank loan interest and audited financial statements, our empirical findings show that if companies have audited financial reports they will get lower interest rate on bank loans than SMEs without audited figures. The lower or higher interest rate determination is based on cost for time value of money and risk level of company. Banks could only secure for SMEs’ potential credit risk through analyzing audited financial statements of SMEs. If companies are less risky, the lower interest rate will be charged by banks.

The following empirical results are new knowledge what we find out when conducting interviews with small companies. The respondents from small companies mentioned that the bank interest rate should also be negotiable as a benefit for companies have credible audited financial reports. Companies also believed interest rate determination is not only based on audited statements, it also relied on having high amount of collaterals and securities, good business plan and good communication with banks.

Bankers’ Opinions

The fixed or flexible interest rate determination depends on loan amount, purpose of financing and types of industries. When granting loans to SMEs, banks mostly used flexible interest rate. The determination of flexible rate is based on internal credit rating score of company, analysis of clients’ liquidity position, current market interest rate and liquidity situation in the
Audit from audit exempted SMEs in Sweden

market. When clients have high credit scores and good liquidity level, they are considered as good customers and will be granted loan with lower flexible interest rate. Banks also have to pay attention on current interest rate and official interbank exchange rate declared from Riksbanken (Sweden’s Central bank). In Sweden, banks’ flexible interest rates range from official STIBOR (Stockholm interbank offered rate) plus how much lower or higher interest rate percentage.

The real estate companies are willing to have flexible interest rate. Currently 20% of the real estate companies in Sweden are granted banks loans by flexible interest rate. The reason is that large portion of company’s balance sheet is loan amount and if interest rate is higher that will be expense of company. And current market interest rate is upward trend so that in order to secure the interest rate level real estate companies turn to have fixed interest rate.

Private loans are also granted by flexible interest rate. As for private loan, lower or higher interest rates depend on trustworthiness of the borrowers. Whether the borrower is trustworthy or not bankers consider credit history, steady income, job and other information which can ensure repayment ability of the borrowers. Based on these facts, banker will identify good clients. Private loan interest rates are ranged from 3.95% to 12.95%. Within this interest rate range, lower interest rate will be granted to more reliable borrowers.

When asked for the relation between interest rate and audited statements, the interest rate determination is primarily based on credit rating of audited financial information. So, credible audited figures are important to get good rating. Clients who have good credit score will be granted lower interest rate. In this regard, audited financial statements have positive influence to get bank loans with favorable interest rate. As for existing SMEs clients who decided to stop their accounts audited and credit rating score turns lower, banks might charge higher interest rate than before in order to share the risk to such clients. But banks will not stop financing to audit exempted existing clients who want to discontinue financial accounts audited as long as they still have same credit score as before.

5.4 Audit demand

SMEs’ perspective

Regarding with internal audit demand of SMEs, the present empirical results show that almost all the small companies in Sweden argue that the demand for audit first of all comes from the owner/owners of the company. Owners are the first and main users of the audited financial information of the company. Actually owners demand and conduct audit for their own safety reasons. Owners feel more secured and comfortable about the financial information and the company’s present state of affairs when they are audited. Especially, when there is more than one owner and partners, there is more demand for the audited financial information because there is greater need of assurance, reliability and transparency in regard to financial issues in the company. So, there is more demand of audit, as the owners think it is important for creating and maintaining better understandings among the co-owners and partners. Besides, the companies believe audit as the monitoring and controlling tool which provide more factual information of the company’s position in making the decisions and future plans. Audit is considered as the quality stamps enhancing the credibility and reliability.

According to Kaur et al. (2007), the owners and shareholders of the company view audit as an assurance of their business. Carberg et al. (1985) also state that audit assures management and the board of directors that the financial statement is correct which let them feel more secured and comfortable about the financial position and solvency of the company. Besides, there is also demand for audited financial information as a matter of assurance and better and
Audit from audit exempted SMEs in Sweden

transient information, where the employees have some interests in the company. This is more found in the companies with more employees where employees have also some influence in the company’s affairs.

A study by Abdel-khalik (1993) about audit demand and state that demand for audit increases with the number of employees, increasing the loss of control due to hierarchy. Furthermore, similar results were also drawn by Senkow et al. (2001) from a study relating to the relationship between employees and the managers.

With regard to external demand for audit, the findings from previous studies like Collis et al., (2004) and Haley & Palepu (2001) stated the demand for audit arise from the external stakeholders like banks/investors. They find that companies go for their financial statements audited to satisfy their lenders like banks. Similarly, Hey & Knechel (2004) state that the demand for auditing arises from the stakeholders like creditors, investors, suppliers, government bodies, tax agency etc., as it is the set of control mechanism for mitigating the risks involved with the firms. Also, Andersson (2005) lists suppliers, creditors and customers as a firm’s essential stakeholders and want to feel secure with the firm.

Our empirical findings show that all of the respondents termed that it is the tax authority that mainly demand for the audited financial information of the company. The tax authority want to be assured that the tax amount is well and correctly assessed and right amount of tax has been paid to the government depending upon the income and profits of the company. FAR (2005) states that auditing is a way for the Tax Agency to ensure that the correct amount of tax is paid. Andersson (2005) states that taxation become fairer for firms by doing auditing. In regard to this, the tax authority demand the tax declaration based upon the audited financial statements of the company is accurate and more reliable, so there is no much need for further investigation in the financial details submitted by the company’s with audited financial information, therefore the companies want audit done for easiness and conformity in taxation.

Apart from above prior knowledge, Collis (2010) also states that there is a significant relationship between voluntary audit and granting loan decision of bank. The present empirical evidences show that the companies believe and argue audit is also demanded by the banks and financial institutions at the time of granting loans. Banks prefer to have the audited financial information of the company besides the collateral, as it is the quality stamps for credibility of the company’s financial position. The creditors, suppliers and the investors are the next users of the audited financial information of the company for closer and better look in the figures so they demand audit as a matter of security in their business affairs. Audited financial information serves as an authentic and most reliable documents the investors, creditor, and suppliers about the company. It is also the customers and researchers and academicians as the interested parties who are interested on the audited financial information.

Bankers’ perspective

Andersson & Paulsson (2005) state that banks believe credit rating would be unsure without audit which supports the findings. Haley & Palepu (2001) opinion that audit is a requirement for granting loans from creditors to the companies. Our empirical findings show that most of the bankers demand audited statements of companies when it considers for granting loan to SMEs. The main reason is to ensure the credibility of financial statements. If SMEs do not have audited statements and want to get loan, banks have to look through every details of their financial figures whether credible or not and then make credit rating based on financial figures and other soft information of clients. Bankers think that this is costly, time consuming
Audit from audit exempted SMEs in Sweden

and subjective judgment. With this regard, banks call for third party (auditors) grantee of accurate and credible financial figures of companies.

The other reason of banks demand for audited statement is that the trend of clients having their accounts audited. In this regard, most of the companies have their accounts audited regardless of the size of companies. Even some companies within the audit exemption criteria, still continuing financial statements audited. In this regard, banks could say as there is no alternative way better than demand for audited statements for tracking clients’ financial positions. Bankers thought that increasing voluntary auditing is not only because of bank requirement, SMEs themselves might think that having audited financial reports is worth when communicate with investors, customers, creditors, suppliers, government and even for owners.

5.5 Cost Vs Benefits of audit

SMEs’ Opinion

Audit Fees Aspect:

Regarding with audit fees, companies have different opinions. Among 20 companies, 11 companies thought that audit fee is too much cost burden especially for those who are exempted from statutory audit. Whereas, remaining 9 out of 20 companies said audit fee is acceptable and that is profession job. If they do not want to hire external auditors, companies could not do by themselves because of limited time and accounting knowledge. Besides that, continuing financial statements audited is worthy for companies despite they are exempted from statutory audit.

Companies expect that if the audit fee would be lower especially for micro-sized companies, there will be more and more companies willing to have audited accounts and get benefited from audited reports. And companies already had audited reports would not discontinue auditing their financial statement. Audit fee also depends on the auditing firm and type services the companies want. Audit fees from big auditing firms turn to have higher amount than small and local auditing firms. Generally, companies choose auditors based on their financial situation and audit fees asked from auditors. However, regardless of the size of companies and audit fees amount all companies knew that having financial statement audited could get positive impact on them.

Signalling Benefits:

C Lennox (2009) states that SMEs’ demand for voluntary audit provide signaling benefits. Having their financial statements audited could attain a positive signal to overcome the credit risk. It has been observed from our empirical findings that almost all the respondents agree with the view that the voluntary audit has signalling benefits to the company as compare to the companies without audited financial information. The empirical evidence demonstrates that though the audit is a cost to the company, it does provide positive signal to the company in different ways and perspectives. Doing auditing is adding value to the company; it is like creating good image and increasing goodwill of the company. The audited financial information are more reliable, credible, and transparent, provides the company as well as outside interested parties like tax authority, banks, creditors, investors, customers and others an valuable source of reliable information. This brings the competitive advantages to the companies with audited financial information in regard to: easy taxation purpose, easy bank loans process, and with better relation with the creditors and suppliers as compare the
companies without audited financial information. Axenborg (2005) states that auditing give a better competitive advantage and increase standard of the accounting.

Costs-Benefits Analysis:

A study by Seow (2001) states that users of audited financial statements identify and make use of the benefits as a matter of assurance that auditing brings, resulting the demand for voluntary audit, even it is not required by law. Kaur et al. 2007 also state that audit is an assurance of business, and act as a control mechanism ensuring the solvency of the company. According to Carey et al. 2000, audit assures the management and board that the financial information is correct. Hay & David (2004) state audit benefits as controlling mechanism that compensates control systems.

Our empirical findings show that all companies in this study believed that having audited financial statement is beneficial for them. In fact audit fee is a lot of cost but companies keep going their accounts audited. However, companies could not manage to prepare all financial statements by-self. Because this is time consuming, lack of manpower and accounting knowledge requirement. Deakins et al. (2001) state that a majority of small firm manager-owners lack formal qualifications, financial skills and knowledge about financial control systems. Companies also believed that when they get benefits of having audited that will be outweigh the audit fees they paid.

Because of having financial accounts audited, companies feel secure and confident about their financial figures. Owners/manager of the company can easily solve the problems based on the audited figures. Brannstrom (2005) states that audit facilitate the firms to obtain capital and funds. Moore & Ronenstrom (1990) also state that the audit benefits the company for external funds like bank loans. Collis et al. (2004) also state that companies go for their financial statements audited to satisfy their lenders like bank for granting loans. Kaur et al. (2007) also state audit helps to get better loans. Moreover, Haley & Palepu (2001) opinion audit as a requirement for granting loans from creditors to the companies. Collis (2010) also states that there is a significant relationship between voluntary audit and granting loan decision of bank. The present findings show that if companies need external financing, audited financial reports could help to get loans from banks. The companies can easily fulfil their capital and fund requirements if they have audited financial reports. Companies also believed that they have better chance to get bank loan than companies without audited statements. When it comes to declare company tax, audited figure could help to pay right amount to tax. Moreover, tax authorities are more convinced with audited reports than without audited figures. In regard to this, FAR (2005) state that auditing is a way for the Tax Agency to ensure that the correct amount of tax is paid.

Andersson (2005) lists suppliers, creditors and customers as a firm’s essential stakeholders and want to feel secure with the firm. A study by Hey & Knechel (2004) state that the demand for auditing arises from the stakeholders like creditors, investors, suppliers, government bodies, tax agency etc. Moreover, Kaur et al. 2007 state auditing helps to uphold credibility and attempts to build good image with creditors, investors and users. The present findings depicts that companies’ audited financial information can also help to improve communication with shareholders (i.e. co-owners / partners) and stakeholders. Regarding on this transparent audited reports, investors would secure about companies current situation and if companies need further investments there will be much easier to get finance. Owners could also do better decision making, business forecast and planning based on audited financial figures. As for owners, the expected benefit of having audited financial statements could say
Audit from audit exempted SMEs in Sweden

as for better controlling and managing the business. The empirical results of respondents from small companies do not say that there is relation between voluntary audits and agency problem within companies. C Lennox (2009) states that SMEs’ voluntary audit provide signaling benefits. Having their financial statements audited could attain a positive signal to overcome the credit risk. The findings also show that the companies believe that voluntary audit also brings signaling benefits and better competitive advantages in the business than the companies without audit.

Based on the empirical findings mentioned above, the expected benefits of SMEs continuing audited financial statements could summarize as security and confident about financial information, problem solving, easy to get bank loan, right amount of tax payment to tax authority, better communication and relation with investors, creditors, suppliers and customers, and for owners of companies could attain better controlling and monitoring the companies. We find out that in relation to the expected and actual benefits, most of the companies’ expected benefits from continuing audits and the actual benefits derived are matched. But some other companies’ expecting is higher than actual benefits that could describe as companies want to get other services along with financial statements audited from the auditors.

**Bankers’ Opinion**

The audit fees will be charged around 10,000 to 20,000 Swedish Kronor depending on the degree of service clients willing to have. If company only need financial statements audited, that will cost approximately 10,000 Swedish Kronor per year. According to empirical findings, some bankers thought that audit fees 10,000 Swedish Kronor is not a big deal when SMEs want to get corporate loan from banks. Some other bankers thought that especially for SMEs this is a great cost.

Bankers have different opinions on this audit fees for SMEs. But when considering about having accounts audited there are benefits for SMEs for instance, easy to get bank loan, can make investment, if company’s credit rating is good can get economic favorable from banks, because of good rating companies could get good image and better communication with shareholders/ stakeholders. In this regard, audit fees could not be a problem for SMEs. However, companies have to think by themselves whether audit fees are acceptable and beneficial or cost burden.

When asked for alternative way for SMEs instead of audit, most of the bankers thought that there is no other alternative way for analyzing companies’ financial figures than audited financial statements. Bank’s internal credit analysis could do financial figures analysis but companies have to provide all financial statements done in right way and as credible as audited statements from auditing firms. Since credible financial statements are most important requirement, the value collateral assets and longer communication between banks and clients could not say as alternative way to get corporate loan from banks. According to these empirical findings, preparing financial statements by companies themselves as good as what auditors could do is only an alternative way for clients who want corporate loan without audited accounts.
5.6 Opinion on new legislation of audit exemption for SMEs

SMEs' opinions

The empirical findings show that most of the small companies in Sweden are aware of the new legislation about audit exemption for the companies with maximum of 3 employees, maximum annual turnover of 3 million Swedish Kronor, and / or maximum of 1.5 million Swedish Kronor of balance sheet assets total. However, fewer numbers of respondents were unaware till the interview about this new rule, due to the lack of information.

In regard to the statutory audit exemption, majority of the companies (i.e. 75%) were aware about this change in legislation. However, 25% of the respondents interviewed were unaware about this rule. The respondents came to know about this change in legislation through the newspapers, media and also through their auditors. Taking this into mind, we can say that the majority of the small companies are aware of the legislation in regard the companies’ that are exempted from statutory audit. Sweden being one of the developed countries with huge information network, the findings show that there is still information gap between the rule-makers and its final beneficiaries i.e., the targeted companies (in case of this study). It could be better if there is more publicity and information sharing so that all the companies know about the updates and changes in rules and regulations related to the companies through proper means and channels of communication so that the targeted companies can be benefited with the new rule.

As explained before, the previous studies show that the audit is important to the companies in many ways. Also, the empirical findings show that almost all the small companies in Sweden think audit is too important and crucial to them. The companies perceive audit is most important to the owners as they are the main users of the audited financial information and, it is also important to other interested parties like tax authority i.e. for taxation purpose, banks for loans, and other interested users etc. Audit is important to the owners and the company as it ensures and provides the right and correct financial information of the company, besides it also derives lots more benefits. The companies want transparent information verified by the external persons like auditors as a matter of safety. The owners feel more secured and comfortable conducting audit.

From the empirical findings, it shows that the educational background of the owners and the time issues also matter greatly for making auditing a vital tool of assurance to the companies in Sweden. We can analyse that the less educated owners with less time perceive audit is more important as compare to the owners with better educational backgrounds. The banks also think audited financial information is more credible and reliable source of information before granting loans to their clients. Besides, it is also important to the suppliers and investors with better information about the company’s financial position and solvency.

Furthermore, the results from our empirical findings show that almost all the respondents believe it is economically favourable for those companies with maximum of 3 employees, maximum annual turnover of 3 million Swedish Kronor, and / or maximum of 1.5 million Swedish Kronor of balance sheet assets total are statutorily exempted from audit. The argument for welcoming the new legislation in regard to audit exemption is that the audit service or audit fee is expensive to the companies with small business activities and limited market. Audit is regarded a costly service to those companies who have fewer things to do and less financial information to be checked and verified. However, besides a costly service, audit has also lots more benefits which cannot be under-mined. The companies should also think them-selves what can be the consequences it can have to the companies by
discontinuing it without any preparations and alternatives instead. The option to do or not to do is also a better option, companies who prefers audit can still go for voluntary audit depending upon their desires and expectations.

Bankers’ opinion

Table 10: Different criteria of audit exemption for SMEs

<table>
<thead>
<tr>
<th>Criteria established by nations</th>
<th>Turnover (SEK)</th>
<th>Number of Employees</th>
<th>And / or</th>
<th>Balance Sheet Total (SEK)</th>
</tr>
</thead>
<tbody>
<tr>
<td>European Commission</td>
<td>83000000</td>
<td>50</td>
<td></td>
<td>41500000</td>
</tr>
<tr>
<td>Sweden (by Nov. 2010)</td>
<td>3000000</td>
<td>3</td>
<td></td>
<td>1500000</td>
</tr>
</tbody>
</table>

(Source: Adapted from SOU 2008:32; FAR press release: 1st Nov, 2010)

According to above the table no.10, audit exemption criteria for SMEs in Sweden are much lower than European Commission’s figures. In bankers’ opinion, in Sweden approximately 90% listed companies are SMEs so that for political, economic and taxation purposes Swedish audit exemption for SMEs are much lower than that of EC. Bankers believe that new legislation is appropriate for their country’s economic and political dimensions. Most of the bankers do not think that new legislation is a barrier between SMEs and bank relationship. Whereas, for audit exempted SMEs currently banks do not have other alternative way better than asking for audited figures when SMEs want bank loans. This new legislation could be a barrier between audits exempted SMEs and bank relationship.

In addition, regarding with audit exempted SMEs voluntarily going for financial statement audited the main reason is that having audited report will easy when they want external financing from banks. Bankers also think that voluntary audit is not only because of bankers’ demand; companies also knew benefits of continuing financial statement audited. For instance, owner could monitor and control business well, better communication and information sharing with shareholders and stakeholders and right amount of tax paid to tax authority.

5.7 Relationship between SMEs and creditors

Relationship between banks and SMEs

In Sweden the primary relation between banks and SMEs is financing (grant loan to SMEs). Besides that, banks used to provide cash management services, credit card services, internet banking for receiving and payment transactions. Some banks also provide investment capital for SMEs and consultancy services.

Owners and creditors relationship

Kaur et al. 2007 state that creditors have expectations on the stability and solvency which is evaluated from the audited financial information. They further state that auditing helps to uphold credibility and attempts to build good image with creditors, investors and users. Our empirical evidence shows that audited financial statements have positive contribution of improving owners and creditors’ relationship. Creditors would like to do business with companies who have audited financial information. Most of the creditors are curious to see the company’s audited reports when they make decision whether to do business or not. Audited figures could describe as the companies’ probability of repaying the credit amount. The advantages of having audited financial statements are that creditors could extend the
credit loan amount and loan term duration. Besides audited statements, mutual understanding and trust are also important in building sound and trustworthy relationship between owners and creditors. For companies who do not have audited reports, there is difficulty for creditors when they want to know companies’ financial condition. When it comes to say companies have audited financial statements but figures are not good enough from creditors’ view, there might be difficulties for owners. For those companies, audited figures could say as a barrier for owner and creditors relationship. We find out that the audited financial information can improve relationships between the company and the creditors. Besides, the audited financial reports with sound figures can enhance better relations between the owners and the creditors.

5.8 Corporate social responsibility
Gelb & Strawser (2001) show a positive relationship between financial disclosure and CSR. Socially responsive firms provide more informative and extensive disclosures to their stakeholders. Our empirical findings show that SMEs in Sweden state that conducting audit despite not required by the law can be regarded also be as CSR. Since, CSR is a way of responding positively to emerging priorities and expectations of the society; and it is also a concept of interacting with the stakeholders on voluntary basis. In this regards, conducting audit by the exempted companies, is a positive contribution towards CSR, as a socially responsible entity. Voluntary audit is motivated towards providing the true and verified financial information to the owners as well as the concerned stakeholders like tax authorities, government, banks, suppliers, customers, researchers, academicians and the society as a whole.
Chapter 6: Conclusion and Recommendations

This chapter will summarize the entire study as well as answer our research question and conclude the research findings according to empirical data results analysis mentioned in chapter 5. Since our research is made with an inductive approach, when it comes to answer our research question we will use empirical results analysis. And then new knowledge will be built, based on empirical findings from bankers and respondents of SMEs. Besides that, recommendations regarding audit from audited exempted micro and small-sized companies in Sweden will be given. Moreover, as a contribution, suggestions for further research will be given to who are interested to do research in voluntary audit subject matter.

6.1 Conclusion

The Swedish first proposal for legislation of statutory audit exemption came into effect on 1st July, 2010 that is same as the European Commission’s criteria. On 25th March, 2010 the government decided to reduce the audit exemption criteria that would be applicable by 1st November, 2010. In accordance with this new legislation, SMEs within two out of three criteria; turnovers 3 million Swedish Kronor, balance sheet total 1.5 million Swedish Kronor and 3 total numbers of employees are exempted from statutory audit requirement. Despite the fact, prior studies show that the audit exempted SMEs in Sweden are still inclined towards continuing audit.

This study finds the expected benefits of audit exempted SMEs in Sweden when they go for voluntary audited financial statements. When it comes to answer our research question, we collect the empirical data by interviews with respondents from 20 SMEs. These 20 SMEs are within audit exemption criteria and continuing their financial statements audit despite not required by the law.

According to our empirical results, the expected benefits for audit exempted SMEs in Sweden voluntarily conducting their financial statements audit are as follow:

- Security with the audited financial information
- Right amount of tax paid to tax authorities
- Easy to get bank loan
- Better relation with creditors, investors and suppliers.

The explanation regarding each of the above expected benefits from voluntary audit could describe as follows.

We find that the owners firstly would like to get secured financial information of the company. Owners feel secured and confident with the audited reports. Although audit fee is costly especially for small companies, owners believe that conducting audit could have more benefits than audit cost incurred. For instance, having audited figures could bring security benefits on their financial situation. Based on the secured financial information owners/managers can get better controlling and monitoring of the business. With this regard, owners demand for voluntary audit expected to get security benefits.

The next expected benefit is related with corporate tax. Companies believe that audited financial figures are of great help in paying the right amount of tax to the tax authorities.
Companies also think that tax authorities are also more convinced with audited figures to declare company’s tax amount than unaudited figures. In this regard, we could say that voluntary audit is related with taxes purpose.

When companies require external financing, audited financial statements could help to get easy loans. Banks usually ask for the audited financial reports when granting loans. Companies believe that if they have audited financial reports, banks will grant loan more easily. Moreover, companies expect that having audited financial reports could help to lower interest rate on the loan.

The next expected benefit is related with companies’ relation with investors, creditors and suppliers. Audited financial reports could help to improve communication with investors, creditors and suppliers. Since credible audited financial information presents the true picture of companies’ financial situation, investors, creditors and suppliers of the companies would like to do business with companies who have financial statements audited. Doing voluntary audit also brings signaling benefits and better competitive advantages in their business than the companies without audit. With this regard, we can conclude that the companies expect to have transparent financial information is to build better relationship with stakeholders.

6.2 Building New Knowledge

Since we are conducting an inductive study, the followings are the new knowledge we have built:

Regarding with new legislation, we have found that 75% of the companies are aware about the audit exemption rule for SMEs. Despite this, the companies are still continuing audits could say as positive toward CSR as a socially responsible entity in terms of voluntarily providing transparent information to the creditors, government, investors, suppliers and other interested users within the society. We also found that in Sweden there is still no other way better than ask for audited financial information when it comes to analyze the financial situation and also for taxation purpose.

We have found that banks provide corporate loan based on the credit score of the companies. If the companies have better credit score, they have more chances to get corporate loans. Moreover, we have found that banks use audited financial information of companies when to comes to make ranking to the companies. Banks have their own definition of categorizing size of companies. If companies are rather small- sized, owners’ credit records, collateral assets, business plan are additional facts that banks have to collect in order to share the default risk. For large companies, banks’ internal credit score and credit rate from external credit rating agencies will be considered. We have also found that in Sweden the common lending technique of banks is the credit scoring method.

We have found that SMEs do their financial statements audited as a primary requirement for the bank loan. We also found that bankers prefer to grant loan to the companies who have financial accounts audited than the companies without audits. However, we have found that the existing clients of banks who are audit exempted and want to discontinuous financial accounts audit, the banks will not stop granting loan if they have same credit score as before.

Regarding with determination of loan interest rate, we have found that if the companies have credible audited figures and have good credit score, they are regarded as a creditworthy customers and banks will grant loans with lower interest rate. And we have found that loan interest rate is also relied on having high amount of collaterals and securities, good business plan and good communication with banks. In fact, banks will look STIBOR% and market
interest rate first and then bankers will consider low or high margin on STIBOR% based on
the companies’ credit rate.

We have not found the common consensus regarding the audit fees whether it is costly or
acceptable to the small companies. We can say that the audit fees depend on the degree of
audit services what companies intend to get. From the bankers’ perspective, we also found
that having audited financial reports not only benefited in bank loans matter, companies can
also build good image when communication with stakeholders. We have found that
companies and bankers have same opinions on the benefits of conducting audits. Due to these
facts, we can conclude that audit exempted SMEs are still continuing accounts audited.

6.3 Recommendations
Since voluntary audit of audit exempted SMEs are increasing, audit fees should be reasonable
especially for micro-sized companies. If the audit fee is acceptable, more and more small
companies would conduct their financial accounts audited. In this regard, it not only benefit
the companies, but also the tax authorities will be more convinced with the audited financial
information when accessing the tax amount in less time.

On the contrary, if audit exempted companies will discontinue audit banks and tax authorities
should have considered other alternative way. We find that banks will not stop granting loans
to existing clients who will discontinue their financial accounts audited if the companies still
have good credit score. With this regard, we could recommend that if companies want to
discontinue audit, they should have accounting and auditing knowledge in order to prepare
financial statements by themselves.

The companies can think about the alternative services besides audit so that they are assured
with their financial information; this can be cost effective and convenient to the companies as
well as other stakeholders and interested parties to rely on the financial information produced
by the company with better transparency and reliability despite not conducting audit. The
companies can develop better internal control mechanism to ensure the company’s financial
situation.

6.4 Suggestions for further research
As this study has researched the expected benefits of audit exempted SMEs in Sweden
conducting voluntary audit, it would be good to evaluate other European countries’ opinion
on voluntary audits. Since most of the EU countries have their own audit exemption criteria; it
would also be challenging to compare two or more countries’ voluntary audit demands and
what are the reasons and benefits of conducting audits. This study finds small companies and
bankers’ perspective of expected benefit of voluntary audit, other stakeholders for instance
investors, trade creditors, suppliers, auditors, customers and tax authorities’ opinions on audit
should be assessed.

Regarding with discontinued audits and bank loans, our empirical analysis shows banks will
not stop granting loans to existing audit exempted SMEs if they still have good credit score on
unaudited figures. It would be interesting to compare credit score on audited and unaudited
figures. If credit score on unaudited reports would have same or better credit rate, that could
be interesting to observe what factors are affecting on companies’ credit rating.
References:


Audit from audit exempted SMEs in Sweden


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Audit from audit exempted SMEs in Sweden


Audit from audit exempted SMEs in Sweden


Appendix I: Interview Guide for SMEs

1. Company information (Name, company type, number of employees, annual turnover, balance sheet asset total etc.)
2. Do you know that at present, companies with: less or equal to 3 employees, annual turnover not exceeding 3 million Swedish Kronor and/or Balance sheet Asset total not exceeding 1.5 million Swedish Kronor are statutorily not required to conduct audit of their financial statements?
3. At present do your company conducts audit?
4. If yes, why do you conduct audit though not required by law, and do you think it is important for the company?
5. What do you think about the internal factors for choosing Voluntary Audit?
6. What do you think about the external factors for choosing Voluntary Audit?
7. Whom do you think that the company’s audited financial statements are useful for?
8. Do you think it is economically favorable for the SMEs from exemption of statutory audit in Sweden?
9. Do you prefer to do business with the companies who do not have their financial information audited?
10. How do you manage finance for your company?
11. If your financing source is not from owners’ contribution, do you manage your finance from banks? If yes, do banks ask for the audited financial statements of your company before granting loan?
12. How do you think that the interest rate on loan is lower or higher than other firms who have not their accounts audited?
13. Do you think that auditing as a monitoring and controlling mechanism for your company?
14. How do you think that auditing can help to improve owners and creditors relationship?
15. What is your opinion regarding audit fees? Is the audit fee acceptable?
16. How do you think that auditing is a cost burden or beneficial for your company?
17. If audit is a cost burden for your company, do you have other alternative ways of controlling instead of auditing?
18. If you believe audit is a beneficial tool for your company, can you list down your expected benefits you get by conducting audit?
19. Your expected benefits and actual benefits come from audit, do they match?
20. Do you think voluntary audit have good signaling benefits to your company? If yes, how?
21. Do you think conducting audit despite not required by the law fulfils Corporate Social Responsibility? If yes how?
22. Is there anything you would like to add? Please feel free to give your opinions?

Thank You !!!
Appendix II: Interview Guide for bankers

Interview duration 20-30 minutes

Relationship between Banks and Small and Medium-sized Enterprises (SMEs)

1. What types of involvement do you have with SMEs?
2. Do you have separate unit which is only deal with SMEs clients? If yes why you have separate unit for SMEs? Could you explain how that unit functions?
3. When you grant loan to SMEs which criteria are important to consider?
4. How do you assess the risk of SMEs when it comes to grant loan to them?
5. How do you observe the credit rating of client firm? Do you use publicly available credit rating from agencies or do you have your own criteria of assessing credit rating of your clients?
6. What types of lending techniques are mostly used when you lend loan to SMEs?
7. What do you think that if there is longer communication/relation with your SMEs client, are there any economic favor for SMEs clients?
8. Do you think that banks can act as a consultant for SMEs? Are there any services you provide to your SMEs clients besides granting loans?

Role of auditing for SMEs

9. Do you prefer to do business with the companies who have their financial information audited? If so, what is your opinion about audited financial statement of SMEs? Is it an important mechanism while you consider financing them?
10. Could you prioritize the following criteria as the role of audited financial statement for SMEs? a) Secure reason b) Better information sharing c) credibility of financial statements d) monitoring device
11. How would you rate the firms with unaudited financial statements? If a firm does not have audited financial statement do you prefer granting loans to them? If yes, could you explain the reason? And if no, could you explain the reason?
12. Will you demand for your client firm’s financial statements are audited? Why? Why not?
13. Do you have other alternative way of monitoring when it comes to track client firm performance besides of auditing? If so could you describe it?
14. Do you think that auditing is costly for SMEs? If yes what would you like to recommend the other alternative way that is also acceptable for granting loans to them?

Interest rate

15. When you grant loan to client, is your interest rate is fixed or it is flexible?
16. If it is flexible could you explain why and how did you determine flexible interest rate?
17. If your borrower firms have audited financial statement do you grant lower interest rate than firm without audited financial statement?
New legislation
18. Regarding with new legislation for audit exemption for SMEs in Sweden, how do you think that the criteria of audit exemption in Sweden are lower than other EU nations?
EU criteria of audit exemption:

<table>
<thead>
<tr>
<th>Criteria established by nations</th>
<th>Turnover (SEK)</th>
<th>Number of Employees</th>
<th>Balance Sheet Total (SEK)</th>
</tr>
</thead>
<tbody>
<tr>
<td>European Commission</td>
<td>83000000</td>
<td>50</td>
<td>41500000</td>
</tr>
<tr>
<td>Sweden (by Nov. 2010)</td>
<td>3000000</td>
<td>3</td>
<td>1500000</td>
</tr>
</tbody>
</table>

19. How do you see the new legislation? Is that barrier for bank and client relationship or is that can strengthen relationship?
20. How do you access the existing clients (SMEs) who have discontinued financial statement audit? Will you still prefer to continue granting loan to them?

What is your opinion about SMEs going for voluntary audit? How do you think that voluntary audit has impact on lending loans to SMEs?

Thank You!!!
Audit from audit exempted SMEs in Sweden