Audit Quality and Audit Report Lag in Malaysia

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\textbf{Abstract:} The purpose of this paper is to conceptually examine the relation between two dimensions of auditor quality, namely, auditor industry specialization and auditor reputation and the audit report lag based on past literature. Given if the empirical research is carried out based on conceptual framework discussed in this paper, the insights drawn from this study may be of assistance to policy makers as they consider the costs and benefits associated with varying levels of audit market concentration as well as providing a snapshot of the level of non-compliance on audit timeliness in Malaysia.

\textbf{Keywords} Auditor reputation, Auditor industry specialization, Audit report lag, Indonesia manufacturing listed companies

\textbf{Paper type} Conceptual paper

1. Introduction

Alkhaitib and Marji (2012) contended that the most dependable source and reference of bookkeeping related data accessible to outside clients is the audited financial statements. One subjective trademark obviously explained with the Conceptual Framework for Financial Reporting is pertinence. As expressed by FASB, for the financial related information to be valuable, it must be both appropriate and consistent.

As expressed by Alfredson et al. (2009) "to have pertinence, financial information must have a quality that impacts users financial choice (p. 15)." To be pertinent and of monetary esteem, the financial related data contained in the in the year-end final statement should conveyed to clients when practicable after the financial year-end (Al-Ajmi, 2008; Alkhaitib and Marji, 2012).

Delays in reporting financial information will effect on the adequacy of reports. The timeliness of audit reports is becoming a critical issue as the timing and delivery of the reports will influence the significance of financial statements (Dopuch et al., 1986; Field and Walkins, 1991; Jaggi and Tsui, 1999). In related work, several studies have shown that demonstrated that putting off the revelation and distribution of the audited financial statements may adversely affect securities exchange proficiency (Leventis et al., 2005; Alkhaitib and Marji, 2012) and market reaction to earnings announcements (Chambers and Penman, 1994) can prompt auditor switching (Mande and Son, 2011).

It is very much perceived that the convenience of audit reports is impacted by various factors. Earlier research on audit report lags have archived that the delay in audit reports can be ascribed to particular firm qualities and complexities (client firm size, number of subsidiaries, client monetary condition, foreign operations, and audit fees), audit risk (possession structures, financial distress indicators, high hazard accounts, and altered audit opinion), audit firm attributes (auditor reputation and non-audit fees), and corporate governance (board independence, audit committee independence, frequency of boards, and or audit committee meeting).

The greater part of research in this area stays focused in the USA, yet obviously there is a need to stretch out this research to another worldwide reach. This investigation investigates the part of examiner industry specialization (Habib and Bhuiyan, 2011) in deciding review report convenience and is a zone of concentrate that has received little consideration. Industry-expert evaluators are relied upon to give predominant administrations and validity (Solomon et al., 1999; Owhoso et al., 2002). Thusly, industry-authority inspectors are likely ready to lead a more successful review and have the capacity to finish the review engagements more practically than non-specialist auditors. Also, the relationship between reviewer notoriety (proxies by Big 4 inspecting firms) and the review report slack also has been reviewed. It can be contended that enormous inspecting firms have more assets (Palmore, 1986b), more in danger as far as brand name notoriety (Francis and Wilson, 1988), have higher quality staff (Chan et al., 1993b), and are in this way liable to give a high-quality audit. At the end of the day, Big 4 auditors are relied upon to give a quicker, efficient service leading to shorter audit reporting lags.

As said already, the financial importance of an audit report lag is a worldwide issue but then most of the research US based utilizing US information (e.g. Ashon et al., 1989; Bamber et al., 1993; Schwartz and Soo, 1996; Lee et al., 2009). There has just been constrained research from outside the USA, for instance, Egypt (Afify, 2009), Jordan (Alkhaitib and Marji, 2012), Bahrain (Al-Ajmi, 2008), and New
Zealand (Habib and Bhuiyan, 2011), studies using Malaysian data sets are limited.

The remainder of this paper is organized as follows. The next section presents the significance of the paper. Section 3 discusses the relevant related literature where else conceptual framework for the paper is discussed in Section 4. Discussion of results and implications for future research are discussed in the concluding section which is Section 5.

2. Significance of the Paper

The paper will contribute to the body of knowledge on two dimensions of auditor quality, namely, auditor industry specialization and auditor reputation and the audit report lag. The study should particularly be of significance in that it will:

- This study provides the conceptual framework for further empirical evidence on the relation between auditor quality and audit report lag using data in Malaysia setting.
- Knowledge obtained from this study would assist the accounting regulators as they consider the expenses and advantages related with differing levels of audit market concentration and additionally giving a depiction of the level of non-compliance on audit timeliness in Malaysia given the empirical study is being carried out.

3. Review of Related Literature

The audited financial statements contained in the yearly report are viewed as a dependable wellspring of data for users of financial data. A gap does, in any case, exist between the finish of the financial year and the publication of the financial statements and in spite of the fact that a gap is important to empower the creation of value data, any broadened deferral may effect on the usefulness and relevance of the information. The issue of timeliness of financial reporting has attracted extensive consideration from professional bodies, researchers, regulatory agencies, and users of accounting information as an important qualitative characteristic of financial accounting information. Convenient bookkeeping data will prompt speculator certainty and in this enhance market efficiency (Leventis et al., 2005). As mentioned previously, users of financial statements consider timeliness as one of the key determinants of audit quality (Leventis et al., 2005; Al-Ajmi, 2008).

The standard part of auditing is to guarantee the quality of the corporate earnings in this way enabling stakeholders to rely on financial statements with certainty. Contrasts in auditor quality are thought to prompt varieties in credibility, objectivity employed, and the quality of the earnings provided by clients. Given examiner quality is multidimensional and intrinsically imperceptible, no single attributes or intermediary is utilized to catch this idea. Past research has by and large auditor brand name to mark proxy for audit quality while researchers (e.g. Craswell et al., 1995; Balsam et al., 2003; Krishnan, 2003b; Chen et al., 2005; Gul et al., 2009) have contended that auditor industry specialization adds to review quality.

With respect to auditor industry specialization, analysts (e.g. Craswell et al., 1995; Amber et al., 2003; Chen et al., 2005) have hypothesized that a by-product of an audit firm choosing to specialize in a given industry is an improvement in the superiority of services provided as well as the credibility afforded to the auditor. As expressed by Dopuch and Simunic (1982), expert auditors are probably going to put more in staff enlistment and preparing, data innovation, and best in class review advancements than non-specialist auditors.

The utilization of auditors with industry specialization will audit quality and thusly enhances the quality of financial reporting (Dopuch and Simunic, 1982). The other impact of industry specialization is audit fees charged by specialist auditor to their clients. Since the advancement of industry-particular abilities and aptitude requires exorbitant speculation, the industry-specialist auditors will hope to charge higher expenses contrasted with non-specialist auditors (Habib, 2011). Be that as it may, expert learning can likewise advance creation economies of scale into the review procedure and turn out to be more productive and prompt lower cost makers of audit works (Craswell et al., 1995; McMeeking et al., 2006). Palmrose (1986a) consequently contends that the subsequent generation of economies of scale enables specialist auditors to charge relatively lower fees to their clients.

Likewise, O'Reilly and Reisch (2002) declare that auditors with an inside and out information of an industry’s operation and qualities might be better ready to perceive unique problems and issues for clients operating in that industry. The audit issues relate to unique industry features (e.g. accounting systems, tax rules, and special reporting requirements); thusly, customer particular learning assumes a critical part in a compelling and productivity review task (Gul et al., 2009).Subsequently, industry expertise auditors will advance a higher audit quality through audit effectiveness as well as enhance audit efficiency through economies of scale. Industry-pro auditors require a shorter time to wind up noticeably acquainted with the client’ financial reporting systems and to resolve complex accounting issues compared to non-specialist auditors (Habib and Bhuiyan, 2011). In like manner, industry-expert auditors will be able to complete the audit of a
company’s financial statements faster than those non-specialist counterparts.

On the basis of the above discussion, our first hypothesis is:

**H1.** The audit report timeliness of audits conducted by an industry-specialist auditor is shorter than those conducted by a non-industry-specialist auditor.

It is generally acknowledged that the quality of audit work varies among audit firms (DeAngelo, 1981; Francis et al., 1999). The Big 4 audit firms have higher audit quality than those non-Big 4 (DeAngelo, 1981; Watts and Zimmerman, 1986; Becker et al., 1998; Caneghem, 2004), as they have solid motivating forces to give a high review quality level because of the reality that they have: more qualified staff, a more noteworthy number of clients, greater chance to convey critical resources to auditing (enrollment, preparing, and innovation), and more in risk, for example, client termination of services contract and loss of reputation (Chan et al., 1993b; Caneghem, 2004; Chung et al., 2005). Leventis et al. (2005) find that because of the utilization of better qualified and prepared staff together with the utilization of unrivaled review innovation, Big 4 accounting firms take less time to conduct audit engagements.

It has been recorded in the literature that Big 4 auditors are positively associated with higher quality of financial reporting. Findings reported in various examinations clearly support that Big 4 auditor serves as an earnings management constraint (a proxy of financial reporting quality). Based on US data, Becker et al. (1998) showed that clients of Big 4 auditors report relatively less discretionary accruals than the discretionary accruals reported by clients of non-Big 4 audit firms.

According to Krishnan (2003b), Big 4 auditors are able to constrain aggressive and opportunistic reporting of discretionary accruals by their clients compared to non-Big 4 auditors. Francis et al. (1999) stated that even though clients of Big 4 firms report higher level of total accruals, they have lower amounts of discretionary accruals. Gore et al. (2001) suggested on the basis of UK sample that in the case where high level of non-audit services are provided, Big 4 firms are more able to constrain earnings management. Chen et al. (2005) found that Big 4 auditors are associated with less earnings management for Taiwan IPO firms. However based on sample of Belgian publicly listed firms, Bauwhede et al. (2003) stated that the superior performance of Big 4 auditors over non-Big 4 auditors is only in the case of income-increasing earnings management. Based on evidence gained, in general, Big 4 auditors provide more effective audit services than non-Big 4 auditors.

Afify (2009) and Cohen and Leventis (2013) stated that Big 4 accounting firms have a tendency to have a more grounded impetus to complete their review work more rapidly so as to keep up their brand name. Likewise, worldwide subsidiary audit firms have more incentives to be more aggressive by providing a faster service in order to increase their audit market share (Leventis et al., 2005). What's more, it is contended that Big 4 audit firms have more assets (Palmrose, 1986a), higher quality and better prepared staffs (Chan et al., 1993a), and propelled review innovation (William and Dirsmith, 1988), and can lead audit all the more proficiently and convenient (Gilling, 1977; Hassan, 2016). A few past studies s (e.g. Abdulla, 1996; Leventis et al., 2005; Owunsu and Leventis, 2006) have documented that organizations will likely to report on a timely basis if their financial statements are audited by one of the Big 4 auditing firms.

Based on a sample of 171 publicly listed firms from the Athens Stock Exchange, Leventis et al. (2005) found that audit delay is diminished by appointing a big international accounting firm. In another study conducted by Owunsu and Leventis (2006) uncovers that companies listed on Athens Stock Exchange are that audited by Big 4 accounting have shorter final reporting lead-time compared to companies audited by local accounting firms. However, no such studies have been undertaken for Indonesia companies (Maijoor and Vanstraelen, 2006).

Based on the above discussion, our second hypothesis is:

**H2.** The audit reports produced by Big 4 auditors are timelier than those reports produced by non-Big 4 auditors.

### 4. Conceptual Framework

Based on the literature review, that explains or describe briefly regarding factors that could lead to shorter audit duration, this proposed or designed framework able to be followed to identify some variables that can be used to test the hypotheses identified in the previous section.

![Figure 1- Conceptual framework](image-url)
5. Conclusion

One important factor in measuring the transparency and quality of financial reporting is timeliness: the shorter the time it takes to audit the financial statement, the better it is for its stakeholders.

This study can be further used to obtain empirical evidence on the current relation between auditor quality and audit report lag using data in Malaysia. This would disclose the current situation of auditor quality and report lag in Malaysia.

If empirical research is carried out based on this conceptual framework, the knowledge that shall be expected to be obtained from study would assist the accounting regulators as they consider the expenses and advantages related with differing levels of audit market concentration and additionally giving a depiction of the level of non-compliance on audit timeliness in Malaysia.

6 References


