



# The Effect of Voluntary Disclosure Quality on Independent Auditors' Opinions and Fees

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**ABSTRACT:** This study examines the quality of voluntary disclosure on the opinion and fees of the independent auditors in listed companies in Tehran Stock Exchange. In line with this goal, all the listed companies in Tehran Stock Exchange that had provided the financial statements (balance sheet, loss and profit statement) and the required information in the years 2006 to 2011 were studied. A total of 123 companies from various industries were selected. To test the hypotheses, multiple variables regression (Inter method) was used and their statistical significance took place using t and F statistics. Also, in order to test the model autocorrelation Durbin-Watson test was employed. Research results show that there is no significant relationship between the quality of voluntary disclosure and the opinion and fees of the independent auditors.

**Keywords:** Voluntary disclosure, Auditors' opinion, Independent auditors' audit fees

ORIGINAL ARTICLE  
Received 11 Jun, 2014  
Accepted 05 Sep, 2014

## INTRODUCTION

Disclosure of accounting information that traditionally has been considered by researchers as one of the most important issues is the ultimate outcome of an accounting system. The ultimate goal of the accounting system is to provide information to stakeholders in the form of inter-organizational and intra-organizational reports. An accounting system in the dominant environment of the company gathers, identifies, measures, records, classifies, aggregates, and summarizes information related to transactions, financial performance and events that have financial effect, and ultimately presents it to interested parties as financial reports. As a result these reports influences on a variety of factors. On the other hand, crediting the provided information indicated the need to the audit. Therefore we expect that the increased level of voluntary disclosure that leads to disclosure quality improvement be followed by less audit costs. In addition, the increase of disclosure quality and information voluntary disclosure level improvement by companies affect auditors' opinion.

### A review on research literature

Ball (2009), in a study examined the relationship between audit fees and voluntary disclosure. Population of his research was 57,600 companies in the course of his research in America. His research shows that there is a negative significant relationship between the increase of voluntary disclosure level and audit fees.

Ball and Shivakumar (2009) stated that increased voluntary disclosure of information by companies in addition to reducing information asymmetry, leads to problems solving of representation, and as a result, it will be followed by transparency and confidence attraction of investors

and other stakeholders as well as auditors. By increasing the quality of accounting information, the likelihood of fraud, distortion and other abuses in the financial statements of these kinds of companies is minimized and presentation of acceptable opinion by independent auditors seems reasonable and logical.

Bani Mahd (2010) in a study entitled affecting factors on the acceptable opinion of auditor, examined some affecting factors on the issuing of acceptable audit report within a period of 7 years from 2001 to 2007 in 56 companies listed in Tehran Stock Exchange examined. The research method was correlational type and was conducted using logistic regression. Research findings indicate that issuing acceptable audit report is more influenced by factors such as manager's performance, the change of ownership, audit privacy, opinion selection, variation of auditor from a private audit institution to another private audit institution, and the size of the firm which is under investigation of auditor of the company. Among the above variables, all variables other than the size of the firm which is under investigation of auditor are directly related to the probability of issuing acceptable audit report.

Audit privacy led to an increase in auditor change among the companies of the study. In addition with the increase in auditor change, qualified opinion in audit reduces and instead, acceptable opinion increases. This suggests that audit privacy, reduces auditor independence and causes the opinion selection phenomenon rise, especially after the organization of the formal accountants community.

Cook and Hanifa (2012) examined the relationship between the number of executives, culture and characteristics of the companies, and the development of voluntary disclosure in annual reports

of the companies in Malaysia. They determined 65 cases of voluntary disclosure for the study. The results of the study showed that there is a significant relationship between the number of executives and the development of voluntary disclosure. There is also a significant relationship between cultural factors and voluntary disclosure.

**MATERIALS AND METHODS**

Research method is correlational type and to conduct it statistical tests are used. Data analysis method is applied using multivariate regression models discussed in the research. Student t -test was employed for hypothesis testing in order to prove the significance of correlational relationship between the variables. Fisher F statistic was used to determine the significance of regression model. Also the examination of the determination coefficient (R2) was performed using ANOVA mechanism. In addition, Durbin-Watson test was utilized to evaluate the absence of autocorrelation problem between hysteresis sentences. Examination of Kolmogorov - Smirnov used for evaluation of variables distribution normality.

After collecting data related variables and transferring the data to the spreadsheet of Excel, using statistical software such as SPSS, the correlation coefficient and related statistical tests between them is applied.

To determine the research sample, companies with the following characteristics are considered:

1. Their fiscal year is ended at March of each year.
2. The company has no fiscal year change from 2006 to 2011.
3. Company is not in financial intermediaries (Banks, investments and ...).
4. Their financial reports are available.

In order to answer the research questions and based on the available theoretical background, the following hypotheses were formulated:

**Research hypothesis:**

1. There is a significant relationship between the quality of voluntary disclosure and presentation of acceptable opinion by independent auditors.
2. There is a significant relationship between the quality of voluntary disclosure and audit fees of the companies.

**Model 1:** Logistic regression was used to measure the forecasting rate of the independent auditors' acceptable opinion presentation regard to the quality of voluntary disclosure of the companies, and other affecting factors on the audit quality. Regard to the method of performing and analyzing the study it can be said that in cases where the use of assumptions is not continuous and normality of

explanatory variables is not possible, and the response variable is binary (dummy that has 2 modles) the log<sub>i,t</sub> model is used. This model is established according to the following equation:

$$LOG\left(\frac{P}{1-P}\right)Z = \alpha_0 + \alpha_1 X_1 + \dots + \alpha_n + \alpha_n = \alpha'X$$

In which:

X1 = voluntary disclosure of the companies

X2 = the type of audit firm (Score 1 for the Audit organization and zero for the other)

X3 = Firm size

X4 = the Board Independence

P = Score 1 for companies that the independent auditors have presented acceptable opinion and zero for the other.

Where Xi, i = 1, ... , n explanatory variables, and P is the probability of the desired event occurrence. The goal of this model is to obtain X coefficients which is calculated through likelihood approach (LIKELIHOOD MAXIMUM). It should be mentioned that P value is estimated based on sampling from the given population and by calculating the ratio of the desired mode (or undesired mode) to the total number of sample. By determining the related coefficients an equation can be obtained based on which the probability of the desired event occurrence can be calculated. However, if we consider the equation in which α is coefficients row matrix and x is column matrix of the explanatory variables, we have:

$$LOG\left(\frac{P}{1-P}\right) = \alpha_0 + \alpha_1 X_1 + \dots + \alpha_n + \alpha_n = \alpha'X$$

$$\Rightarrow e^{\alpha'x} = \frac{P}{1-p}$$

$$\Rightarrow p = \frac{e^{\alpha'x}}{1+e^{\alpha'x}} = \frac{1}{1+e^{-\alpha'x}}$$

Thus, having related coefficients (which are estimated as sample) a model is obtained by which the probability of the event occurrence can be calculated for each individual of the given sample.

The equation  $p = \frac{e^{\alpha'x}}{1+e^{\alpha'x}} = \frac{1}{1+e^{-\alpha'x}}$  is called the logistic distribution function .

**Model 2:** The model used in this study to examine the relationship between voluntary disclosure and audit fees is driven from Ball (2009) with slight modification because of unavailability of data.

$$LNFEI_{i,t} = \beta_0 + \beta_1 SDISCLOSE + \beta_2 LNASSETS + \beta_3 ROA + \beta_4 ACCR + \beta_5 CURRENT + \beta_6 IAB + \beta_7 LOSS + e_{i,t}$$

In which:

LN-FEE: natural logarithm of total audit fees of the financial year.

SDISCLOSE: voluntary disclosure; the method of calculating it will be provided in the next section.

LNASSETS: the firm size which is equal to the natural logarithm of total assets at fiscal year end.

ROA: Return on assets

ACCR: Accruals divided by total assets

CURRENT: Current assets divided by total assets.

IAB: Total liabilities divided by total assets.

LOSS: Loss before extraordinary items 1 otherwise (0).

**Dependent variable:**

**Audit fee:** audit fee includes any kind of funds which is paid to auditor or audit firm for the provision of audit services and as agreed with the contract. In another definition audit fee is the fee that the auditor determines for services which he wants to offer customers. On the audit fees the estimation of labor hours of all staff at all levels will be considered (Shadman, 2004).

**Opinion:** Opinion is the report of the independent auditors in which the accepted responsibility by the independent auditors toward the financial statements is expressed (Auditing Principles of Accounting and Auditing Research Centre).

**Acceptable opinion:** Acceptable opinion means that the audit domain has been adequate, and it desirably shows financial statements as well as the results of operations in accordance with Generally Accepted Accounting Principles. Auditors in such circumstances do not accept any criticize, or any conditions (Auditing Principles of Auditing and Accounting Research Centre).

**Independent variables:**

**Voluntary disclosure quality:** quality of voluntary disclosure is the reliabilities and timely of the information which will be helpful for decision making by users of this information and if the disclosure of information is not affected by specific rules and is conducted by the company voluntarily it is considered as voluntary disclosure (Owusu Ansah, 1998. Quarterly Journal of Accounting and Auditing)

**The calculation method of the voluntary disclosure level of companies:** In order to calculate the voluntary disclosure concession the proposed indicators by the Botosan (1997) which is derived from the Jenkins Committee Comments, was used. The index value is the same. Thus, for each of them, in the case of disclosure existence value of 1 is considered and in the case of lack disclosure a value of zero is considered. The voluntary disclosure concession is obtained from dividing the total of obtained concessions by total available concessions (71). It is noteworthy that , this approach is applied in researches of researchers such as Cook( 1989,1991 ) ,Owusu-Ansah (1998 ) and in Parchini (2009 ). The method of its calculation is as follows :

$$SDSCORE = \frac{\sum_{j=1}^n d_j}{n}$$

SDSCOR: the companies' voluntary disclosure concession

Dj: The concession related to voluntary disclosure of index so that the value 1 if the information is disclosed and zero if the value is not disclosed.

n: total number of the given unessential disclosure of information in index (71)

**Type of auditor:**

In this study, audit organization is selected as the great audit, and other audit firms are selected as small audit. Regard to the criterion of the audit firm size, it is assumed that audit organization has higher quality than other audit firms. Therefore, if the audit organization is the sample auditor of the company, the value of 1 and otherwise 0 is given.

**Firm size:** natural logarithm of total assets (firm size) which is measured using the natural logarithm of total assets.

**Independence of the Board:**

Non-responsible members of the Board are those members who are not executive directors of the company and are professional managers with expertise in the decision control (Setayesh and Kazem Nejad, 2010). In this study, to assess the independence of the Board of Directors, the ratio of the number of the Board non-responsible members to the total number of the Board is used.

**RESULTS**

Wald test parameters in Table 1 are shown. It is observed that among the four independent variables of the model, two variables of the model have significant influence on the dependent variable, and the other two variables have no significant impact. These calculated results are obtained based on calculated error level for the Wald test. In bilateral logistic regression analysis, the criterion for acceptance or rejection of significance of independent variables effect is the standard error of 0.10. In this model the independent variables of voluntary disclosure and type of auditing institution that have error level greater than 0.10, have no significant impact on the dependent variable. Since, their significance is respectively 0.115 and 0.569, which is more than 10 percent. The impact of firm size variable and independence of the Board variable in this study, given the significance of less than 0.10 on the dependent variable of the research, i.e. acceptable opinion presentation is significant, because their significance is respectively equal to 0.011 and zero, which is less than 10%. This means that regard to the

variables of voluntary disclosure and type of auditing, the prediction of independent auditors' opinion type is not possible. However, according to the results of this study, using the variables of firm size and the Board independence, the independent auditors' opinion type can be predicted.

Table 2 shows that the estimated coefficient for the variable of voluntary disclosure is equal to 0.009. According to the significant column it is illustrated that the estimated coefficient is not significant at confidence level of 95%, because its significance is 0.831 and this number is greater than 5% accepted error level in this study. So the existent of any relationship between audit fees and voluntary disclosure at confidence level of 95% will not be approved.

The above table also shows that the estimated coefficient for firm size is equal to 0.255. According to

the significant column it is illustrated that the estimated coefficient is significant at confidence level of 95% (the significance of this coefficient is equal to zero which is less than 5%). Therefore, statistically significant relationship between firm size and audit fees at confidence level of 95% is confirmed. Also, in table 4-5 the coefficients of the other variables in the model and the significance of each of them is shown. It is observed that the coefficient of financial leverage variable which is used in this study by the ratio of total debt divided by total assets is significant. This means that there is a significant relationship between financial leverage and audit fees. But based on the research findings there is no significant relationship between other variables and audit fees. In table 3 the summary of the hypotheses test results is presented.

**Table 1:** Test of the model independent variables effect

|         | Variable                   | Symbol    | Coefficient | Standard Error | Wald Statistics | Freedom Degree | Significance | Prediction Coefficient |
|---------|----------------------------|-----------|-------------|----------------|-----------------|----------------|--------------|------------------------|
| Stage 1 | Voluntary Disclosure       | SDISCLOSE | .631        | .400           | 2.487           | 1              | .115         | 1.879                  |
|         | Firm size                  | LnAsset   | -.449       | .176           | 6.484           | 1              | .011         | .638                   |
|         | Type of audit organization | AuditOrg  | .122        | .214           | .324            | 1              | .569         | 1.130                  |
|         | Independence of the Board  | Esteghlal | 5.840       | .544           | 115.032         | 1              | .000         | 343.638                |
|         | Fixed Coefficient          | Constant  | .707        | .970           | .532            | 1              | .466         | 2.028                  |

**Table 2:** The Model Variables Coefficients

| LN-FEE <sub>it</sub> =β <sub>0</sub> +β <sub>1</sub> SDISCLOSE+β <sub>2</sub> LNASSETS+β <sub>3</sub> ROA +β <sub>4</sub> CURRENT+β <sub>5</sub> IAB+β <sub>6</sub> LOSS+ e <sub>it</sub> |   |            |                              |            |                          |        |              |                         |       |
|---|---|------------|------------------------------|------------|--------------------------|--------|--------------|-------------------------|-------|
|   | Variables                                     |            | Non-standardized Coefficient |            | Standardized Coefficient | t      | Significance | Collinearity Statistics |       |
|   |   |            | B                            | Std. Error | Beta                     |        |              | Tolerance               | VIF   |
| 1   | Fixed Coefficient                             | (Constant) | 1.143                        | .122       |                          | 9.380  | .000         |                         |       |
|   | Voluntary Disclosure                          | SDISCLOSE  | .009                         | .041       | .008                     | .214   | .831         | .951                    | 1.051 |
|   | Firm Size                                     | LnAsset    | .255                         | .021       | .450                     | 12.362 | .000         | .969                    | 1.032 |
|   | Total liabilities divided by total assets     | IAB        | .137                         | .062       | -.084                    | -2.205 | .028         | .774                    | 1.292 |
|   | Loss  | LOSS       | -.056                        | .032       | -.066                    | -1.714 | .087         | .982                    | 1.019 |
|   | Return on assets                              | ROA        | .000                         | .000       | -.040                    | -1.121 | .263         | .944                    | 1.215 |
|   | Current assets divided by current liabilities | CURRENT    | .019                         | .042       | .017                     | .454   | .650         | .774                    | 1.292 |

a. Dependent Variable: LnFee

**Table 3:** The summary of the hypotheses test results

| Hypothesis Number | Hypothesis  | The obtained results of the study |
|-------------------|---|-----------------------------------|
| 1                 | There is a significant relationship between the voluntary disclosure quality and acceptable opinion presentation by independent auditors. | Rejection                         |
| 2                 | There is a significant relationship between the voluntary disclosure quality and audit fees of the companies.                             | Rejection                         |

## DISCUSSION

**Hypothesis 1: By increasing the voluntary disclosure quality the acceptable opinion presentation by independent auditors can be predicted.**

The research results indicate that the first hypothesis is rejected in the sample of this research. Because among the four independent variables test of the model, two variables of the model have a significant influence on the dependent variable, and the other two variables have no effect. These calculated results are obtained based on the calculated error level for Wald test.

**Hypothesis 2: There is a significant relationship between the voluntary disclosure quality and audit fees of the companies.**

According to the research findings it can be observed that the estimated coefficient for the variable of voluntary disclosure is equal to 0.009. According to the significant column it is illustrated that the estimated coefficient is not significant at confidence level of 95%, because its significance is 0.831 and this number is greater than 5% accepted error level in this study. So the existent of any relationship between audit fees and voluntary disclosure at confidence level of 95% will not be approved. Also, based on the test data it is found that the independent variable of firm size has a direct and significant effect on the dependent variable of audit fees, and the coefficient of financial leverage variable i.e. the ratio of total assets and liabilities has an impact on audit fees. This hypothesis also is rejected here and is inconsistent with the findings of (Ball et al 2012). Contrary to our expectations it is based on theoretical principles presented in the previous sections. This means that based on the present research results in the tested independent population, auditors, when determining their considerations extent, might not notice the level of voluntary disclosure of presented information.

**Recommendations based on the results of the research hypotheses:**

Regard to the results of the first hypothesis test, the size of two independent variables affecting the dependent variable, namely the independence of the Board and the firm size, based on the sample tested in the present research, should be considered larger, and be used more to relying on these two affective variables, a more favorable opinion presentation by independent auditors be more probable.

According to the results of the second hypothesis, the independent variable of voluntary disclosure were examined in this study population,

and determined that it has no effect on the dependent variable of audit fees. This results from the fact that population in this study, in practice, due to the economic, social and management structures of the population does not follow voluntary disclosure indexes. But the independent variable of firm size has a direct impact on audit fees, because the accounting cost is a function of the amount and the issue of auditing by the independent auditors. So the factor of disclosure quality as a determinant factor of audit fees is not reliable. Therefore, it is recommended in order to determine audit fees, as long as the existing conditions at the present population for appearing the given indicators are not favorable, no consideration be taken into it.

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