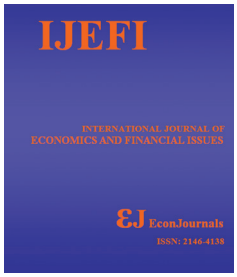

International Journal of Economics and Financial Issues

ISSN: 2146-4138

available at http: www.econjournals.com

International Journal of Economics and Financial Issues, 2024, 14(6), 46-54.

Legal Liability, Institutional Environment and Audit Pricing: Insights from China's Securities Law Revision

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Received: 13 May 2024 **Accepted:** 24 August 2024 **DOI:** https://doi.org/10.32479/ijefi.16727

ABSTRACT

This study investigates the impact of China's revised securities law (2019) on the audit pricing strategies of A-share listed companies. Using a difference-in-differences (DID) approach and a sample of 26,057 firm-year observations from 2016 to 2022, we find that the new law led to a significant increase in audit fees, especially for non-state-owned enterprises and firms in regions with stronger legal institutions. We attribute these effects to the heightened legal liability and regulatory scrutiny faced by auditors under the new regime, which incentivizes them to enhance audit quality and charge higher risk premiums. Our results are robust to a series of sensitivity tests and alternative specifications. We conclude that the revised Securities Law has achieved its intended objectives of improving market transparency and investor protection but at the cost of higher compliance burdens for listed companies. Our findings have important implications for policymakers, regulators, and market participants in China and other emerging economies undergoing similar legal and institutional reforms.

Keywords: Audit Pricing, Securities Law, Legal Liability, Institutional Environment
JEL Classifications: M42, G38

1. INTRODUCTION

Since the initial promulgation of the "Securities Law of the People's Republic of China" in 1998, this legal framework has been through several amendments and revisions. However, with the rapid evolution of China's capital market and its increasing complexity, the existing regulatory system has revealed significant shortcomings in promoting market transparency, fairness, and protecting investor rights. Especially in curbing illegal activities of listed companies and enhancing the safeguarding of interests and rights for ordinary investors, the old Securities Law of the People's Republic of China failed to achieve the expected efficacy. This backdrop prompted a thorough revision of the "Securities Law of the People's Republic of China" in 2019, aiming to further regulate securities market behaviour and enhance investor protection through legal means.

The revised "Securities Law of the People's Republic of China" (New Securities Law) aims to bolster legal deterrence and escalate the costs for non-compliance. It significantly increases the fines for listed companies and their associated entities, with the penalty for securities service institutions not conducting due diligence now reaching up to 10 times their income or a fine of 50 million RMB, a substantial increase from the previous fivefold income penalty. The maximum fine for individuals within listed companies responsible for violations has surged from 600,000 RMB to 10 million RMB. Furthermore, the introduction of a class action lawsuit mechanism is designed to ease the financial burden of litigation for small and medium investors. These initiatives aim to overcome challenges in the protection of the interests of investors and to strengthen the deterrent effect of penalties, ultimately improving the market's legal framework.

Under the new regulatory environment, increased penalties for non-compliance and heightened litigation risks have significant

implications. Companies that breach the securities law face reputational damage and increased operational risks. Auditors, as indispensable intermediaries in the capital market, ensure the authenticity and reliability of financial information for investors (Abbott et al., 2012). They must balance the protection of client interests with the fulfilment of their professional duties (Carlisle et al., 2023). This dual responsibility increases the pressure on auditors to enhance their practice quality to meet stringent legal accountability demands. Fulfilling these professional duties implies greater audit efforts and higher audit costs (Chen and Chen, 2024). Furthermore, the revised securities law introduces a class action mechanism, increasing the legal risk of joint and several liabilities for auditors and their clients. Facing higher litigation risks, auditors may demand higher audit fees as compensation for these risks (Hunt et al., 2022).

Jaggi and Low (2011) tested corporate data from 17 countries using weighted least squares and found that stringent securities regulation leads to increased audit workload and risk, thereby increasing audit fees. However, this relationship only exists in countries with weak investor protection. Utilizing data from Chinese A-share listed companies from 2016 to 2022, this study employs the difference-in-differences (DID) method to investigate the impact of the revised securities law's stricter regulations on China's audit fees. We observed a significant increase in audit fees following the new law. Factors such as client characteristics and the institutional context influence audit pricing (DeFond and Lennox, 2011; Menon and Williams, 2001). Furthermore, Loureiro and Silva (2021) noted that securities regulation impacts vary at national and corporate levels due to differences in information environment attributes. Through heterogeneity analysis, we found that the changes in audit fees for non-state-owned enterprises were more pronounced than for state-owned ones post-implementation of China's New Securities Law. Additionally, the policy's effectiveness is more evident in regions with better legal governance in China. This provides new empirical evidence for previous research.

Our study makes a valuable contribution to the literature on audit pricing and regulatory changes in the Chinese context. By examining the impact of the New Securities Law on audit fees across different types of firms and institutional environments, we provide new insights into the heterogeneous effects of legal reforms on auditor behaviour and market outcomes (Kamalu et al., 2023). Our findings have important implications for policymakers, regulators, and market participants, as they highlight the role of legal institutions in shaping the incentives and practices of auditors and listed companies.

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Audit fees reflect auditors' compensation requirements for the cost of audit inputs and the risks undertaken during audit service provision. To address significant misreporting risks, auditors transfer risks to clients by charging audit fee premiums or increasing audit fees to compensate for higher audit input demands (DeFond and Zhang, 2014; Simunic, 1980; Widmann et al., 2021). The factors which determine the audit fees are multifaceted, including business size and characteristics, internal governance, earnings management and legal regulation. Larger clients, generally involving more complex economic activities and accounting practices, require auditors to conduct a wider range of audit procedures involving more audit adjustments, resulting in increased audit fees. The complexity of audit units' operations, such as the measurement of accounts receivable and inventory, significantly positively affects audit charges (Firth, 1985; Francis, 1984; Menon and Williams, 2001). The more complex the operations, the higher the auditors' identification and assessment of significant misreporting risks, and the increased litigation risk from audit failure may lead auditors to choose audit fee premiums to transfer risk (DeFond and Zhang, 2014). However, high levels of corporate governance can help reduce significant misstatements in financial reporting and their potential legal litigation, allowing audit institutions to offer reduced fees for these entities (Hogan and Wilkins, 2008; Simunic, 1980). An active audit committee can be effective in reducing the company's compliance risk, lessening the risk premium charged by auditors, and thus lower audit fees (Smith et al., 2019). The behaviour of earnings management also affects audit pricing, with studies showing that increased levels of earnings manipulation lead to higher audit fees., as earnings management is often interpreted as a sign of mismanagement (Bryan and Mason, 2016).

In regulated environments, auditors incur higher risk exposure costs, leading to adjusted pricing strategies where audit fees are increased to offset potential risk losses (DeFond and Lennox, 2011). More comprehensive information disclosure policies also prompt auditors to pay attention to such information and consider it when pricing audit services (Yao et al., 2020). The implementation of new policies introduces increased business uncertainty, heightening the potential for audit failure. Consequently, auditors recalibrate audit fees to mitigate this elevated risk (Liu et al., 2021). Furthermore, media scrutiny, particularly negative coverage, amplifies the risk of audit failure. This prompts auditors to carry out more thorough audit tests and detailed procedures, leading to higher audit costs and fees (Bryan and Mason, 2016; Krishnan and Peytcheva, 2019).

In essence, auditors raise audit fees primarily to reduce risks, including audit and litigation risks. Additionally, enhancing audit quality is a crucial factor in increasing fees. Faced with clients requiring high-quality audit services, auditors may employ stricter audit techniques and broaden the audit's scope. Such measures demand substantial audit resource allocation, necessitating higher fees for compensation.

China's New Securities Law, aimed at improving market transparency and fairness, has intensified the requirements for listed companies' information disclosure and raised penalties for non-compliance, resulting in a more stringent external supervision environment. This rise in legal risk and associated liabilities for certified public accountants significantly elevates both risk and audit costs, affecting audit fees (Yang et al., 2021). The law's stricter penalties for infractions heighten compliance costs for

listed companies. Its implementation signifies an optimization of the competitive policy system and the perfection of the external regulatory environment, increasing the likelihood of penalties for non-compliance with disclosure obligations, potentially raising the litigation risk for enterprises (DeFond and Lennox, 2011; Gunn et al., 2019). This suggests that the cost of risk for companies violating disclosure regulations has increased, directly impacting their litigation risk. With the new law, the heightened cost of non-compliance could expose listed companies to greater litigation risk, thereby increasing the complexity and risk of audit work (DeFond and Lennox, 2011). Consequently, auditors may charge higher fees to compensate for the increased workload and risks undertaken. The new law's stringent requirements for information disclosure by listed companies lead to higher demands for financial reporting quality. Quality financial reporting necessitates more detailed and comprehensive audit work, thus increasing the workload and responsibility of auditors (Dresdner and Fischer, 2020; Hwang and Hong, 2022). To ensure the accuracy and compliance of financial reports, auditors may need to expand the scope of the audit and add procedures, resulting in increased audit costs (Lee and Choi, 2023; Xu et al., 2020). As a result, the rise in audit expenses is expected to lead to increased audit fees for listed companies.

Therefore, we propose the following hypothesis:

H_1: Following the implementation of China's New Securities Law, audit firms tend to charge higher audit fees.

3. METHODOLOGY

3.1. Sampling and Data Collection

China's New Securities Law was enacted in 2019 and took effect in 2020. As a cornerstone of the capital market, this law plays a crucial role in enhancing the market environment and promoting high-quality development. Market responses were more pronounced on the law's adoption day than its actual implementation date (Greenstone et al., 2006). This research, therefore, identifies 2019 as the pivotal year for policy implementation, comparing data from 3 years before and after 2019, specifically from 2016 to 2022, focusing on China's A-share listed companies. These companies are chosen due to their significant transparency in information sharing and their essential role in China's capital markets, making them excellent subjects for analyzing the behaviour of firms, the productivity of markets, and the impact of regulatory changes during the country's economic development. Data for this research were sourced from the CSMAR (China Stock Market and Accounting Research) database, renowned for its focus on the Chinese stock market and accounting research.

To guarantee the precision of our results, the study excluded financial and insurance sector companies to avoid potential biases from non-representative data. Furthermore, firms marked with "ST" or "*ST" were also excluded from the analysis. The "ST" label is used for companies facing financial distress or consecutive net losses for 2 years, while "*ST" denotes companies that have breached securities regulations, both indicating higher investment risks and distinct trading characteristics that could distort the research findings. To enhance the study's robustness, continuous variables were refined through tail trimming, eliminating the top and bottom 1% of data points to minimize the influence of extreme outliers on the regression analysis. This detailed data preparation resulted in 26,057 observations suitable for regression analysis, providing a clean and reliable dataset for investigating the study's objectives.

3.2. Model Design

This study examines the impact of China's New Securities Law on audit fees by using it as a case study of how enhanced regulatory measures affect the securities market. It applies a difference-in-differences (DID) approach to assess the effects of stricter regulations on audit fees. Considering audit fees are subject to influences like client characteristics, potential issues like omitted variables may affect the analysis of how increased penalties impact audit fees. The DID method helps address these endogeneity concerns effectively (Bernardo and Fageda, 2017; Pan et al., 2020). Thus, Model (1) is established for analysis:

$$Lnfee_{i,t} = \beta_0 + \beta_1 Post_{i,t} + \beta_2 Treat_{i,t} + \beta_3 Post_{i,t} * Treat_{i,t} + \beta_4 Size_{i,t} + \beta_5 Leverage_{i,t} + \beta_6 ROA_{i,t} + \beta_7 Growth_{i,t} + \varepsilon_{i,t} \quad (1)$$

Given that the Hausman test results in a P-value of Prob=0.0000, which is <0.05, the fixed effects model is shown to be more accurate than the random effects model. Therefore, we employ the fixed effects model for empirical testing. Our focus is on the impact of the New Securities Law on audit fees, with the coefficient β3 of Post*treat representing the net effect of the policy's implementation on audit fees, which is expected to be significantly positive.

This variable serves as an indicator of the law's implementation status across different time periods within the dataset. Specifically, for any data corresponding to the year 2019 or before, "Post" is assigned a value of 0. This denotes the timeframe prior to the New Securities Law coming into effect. Conversely, for data from the year 2020 onwards, "Post" receives a value of 1. This allocation reflects periods during which the new legal framework was in force, thereby facilitating a structured analysis of the law's influence on the variables of interest.

Employing a difference-in-differences (DID) model requires the construction of treatment and control groups to identify the differential impacts of policy implementation. Given the broad applicability of the New Securities Law, we distinguish these groups based on the variance in the degree of impact of the New Securities Law (Campello and Larrain, 2018; Vig, 2013). This legislation, with its stronger penalties and increased competition in the audit market, impacts all listed entities and audit firms. Notably, smaller audit firms, due to their reduced market share and management challenges, might encounter greater litigation risks following the law's implementation, thereby being more significantly affected compared to larger firms. Accordingly, firms ranked in the top 10 by the Chinese Institute of Certified Public Accountants serve as the control group (Treat = 0), with the rest forming the treatment group (Treat = 1). "Post" is a dummy variable that represents the status of the law's implementation across different time frames. It serves as an indicator of when the

law was in effect, with data until 2019 marked as 0 before the law's impact, and from 2020 forward marked as 1 post the new legal framework.

Audit fees, representing the compensation auditors receive for their efforts and risk (DeFond and Zhang, 2014), are captured by the natural logarithm of audit fees (Francis and Simon, 1987; Gist, 1995; Harjoto and Laksmana, 2022), denoted as Lnfee in the text. Following Bepari et al. (2022), Ghosh and Tang (2015) and Cahan and Sun (2015), we include control variables such as size (calculated as the logarithm of total assets at year-end) (Gull et al., 2018), Growth (the ratio of current year's revenue to the previous year's revenue minus one), Leverage (total end-of-year liabilities divided by total assets), and ROA (total assets net margin, calculated by dividing net profit by average total assets at the beginning and end of the year) (Nekhili and Gatfaoui, 2013), to account for their influence on audit fees.

4. RESULTS

4.1. Descriptive Statistics

Table 1 displays the descriptive statistics, revealing an average logarithm of audit fees standing at 13.94, indicating significant variations in audit fees across different firms. Additionally, the average corporate asset size is documented at 22.27, with leverage ratios extending from a high of 0.934 to a low of 0.052. Asset returns peak at 0.239 and drop to −0.416, indicating financial losses for some listed entities. The mean growth rate for companies is calculated at 0.15, with a median value of 0.084, emphasizing considerable growth differences among firms.

Table 1: Descriptive statistics of the variables

Variable	Max	Min	Mean	P50	SD	N
Lnfee	16.32	12.61	13.94	13.82	0.655	26057
Post	1	0	0.632	1	0.482	26057
Treat	1	0	0.402	0	0.490	26057
Size	26.45	19.73	22.27	22.08	1.309	26057
Leverage	0.934	0.0520	0.410	0.400	0.203	26057
ROA	0.239	−0.416	0.0330	0.0340	0.0730	26057
Growth	4.101	−0.672	0.150	0.0840	0.397	26057

Table 2: DID regression results

Variable	(1)	(2)
	Lnfee	Lnfee
Post	0.0905***	0.0715***
	(30.82)	(19.93)
Post* treat		0.0136**
		(2.46)
Treat		−0.0208***
		(−3.93)
Size	0.2990***	0.3376***
	(66.87)	(103.19)
Leverage	0.1595***	0.1465***
	(9.39)	(9.55)
ROA	−0.2893***	−0.3639***
	(−11.51)	(−14.79)
Growth	−0.0068*	−0.0094***
	(−1.89)	(−2.65)
_cons	7.1668***	6.3238***
	(74.29)	(90.76)
Year Fixed Effect	YES	YES
Firm Fixed Effect	YES	YES
N	26057	26057

***P<0.01, **P<0.05, *P<0.1, t statistics in parentheses

4.2. Regression Results

The analysis of the New Securities Law's effect on audit fees utilized Model (1) for the initial regression assessment, as detailed in Table 2. In the regression tables presented throughout this paper, the values in parentheses represent t-statistics. Significance levels are denoted as follows: *P < 0.1, **P < 0.05, ***P < 0.01. Column (1) introduces only the post-implementation dummy variable and other control variables, with the post variable's coefficient at 0.0905, significantly positive at the 1% significance level. This suggests a notable increase in audit fees following the law's introduction. Nonetheless, this finding alone does not conclusively prove that the rise in audit fees is directly attributable to the law's enactment, as concurrent external factors could also play a role. To mitigate the influence of such concurrent factors, column (2) adds the Treat variable, interaction of post and treat for a difference-in-differences analysis. The interaction term's coefficient, at 0.0136 and significant at the 5% level, indicates that the law's introduction positively affected audit fees, affirming Hypothesis 1.

4.3. Heterogeneity Analysis

4.3.1. Nature of property rights

In China, state-owned enterprises (SOEs) make up a large proportion of listed companies. Compared to non-SOEs, SOEs undertake more social responsibilities and receive more resources from the government, such as subsidies and preferential policies (Zhou et al., 2023). Additionally, the Chinese government reforms SOEs' internal governance structures and implements internal control systems within SOEs to enhance the quality of accounting information and ensure stable operations. Generally, SOEs have more standardized management and stronger risk resistance than non-SOEs (Gong and Choi, 2021; Ruan and Liu, 2021). With the implementation of the New Securities Law, although the risk and pressure on audit firms and listed companies increase, SOEs possess stronger risk resilience and bargaining power (Le et al., 2023), leaving little room for audit firms to raise audit fees. For non-SOEs, audit firms adopt more cautious auditing strategies to manage the risks introduced by the New Securities Law, leading to higher audit pricing.

We categorize listed companies into state-owned enterprises (SOEs) and non-SOEs, employing model (1) for a difference-in-differences analysis, with findings displayed in Table 3. For the SOE category in column (1), the coefficient for the interaction term Post*treat stands at 0.0037, indicating no significant impact. Conversely, in the non-SOE segment shown in column (2), the coefficient is 0.0267, significantly positive at a 5% threshold. These outcomes reveal that the New Securities Law's effect on audit fees is contingent upon the company's ownership structure, showing a stronger positive correlation between the law's introduction and audit fees in non-SOEs. This pattern underscores an emerging trend where auditors raise audit fees more substantially for non-SOEs after the New Securities Law comes into effect.

Table 3: Grouped regression results of property rights

Variable	(1)	(2)
	State-owned enterprises	Non-state-owned enterprises
	Lnfee	Lnfee
Post*Treat	0.00365	0.0267**
	(0.53)	(2.99)
Post	0.0968***	−0.00389
	(21.63)	(−0.67)
Treat	−0.00880	−0.0367***
	(−1.34)	(−4.37)
Size	0.328***	0.373***
	(82.55)	(59.59)
Leverage	0.207***	−0.0950**
	(11.65)	(−3.09)
ROA	−0.355***	−0.367***
	(−12.91)	(−6.35)
Growth	−0.00705	−0.00711
	(−1.65)	(−1.16)
_cons	6.516***	5.650***
	(77.79)	(41.18)
Year fixed effect	YES	YES
Firm fixed effect	YES	YES
N	7610	18447

***P<0.01, **P<0.05, *P<0.1, t statistics in parentheses

Table 4: Grouped regression results of legal environment level

Variable	(1)	(2)
	High legal environment level	Low legal environment level
	Lnfee	Lnfee
Post*treat	0.0269***	0.00830
	(3.47)	(0.87)
Post	0.0533***	0.0695***
	(10.18)	(13.17)
Treat	−0.0244***	−0.0197*
	(−3.63)	(−2.08)
Size	0.363***	0.329***
	(80.80)	(70.94)
Leverage	0.132***	0.182***
	(6.13)	(8.13)
ROA	−0.462***	−0.254***
	(−13.05)	(−7.40)
Growth	0.000391	−0.0236***
	(0.09)	(−4.15)
_cons	5.743***	6.531***
	(59.62)	(66.52)
Year fixed effect	YES	YES
Firm fixed effect	YES	YES
N	13335	12722

***P<0.01, **P<0.05, *P<0.1, t statistics in parentheses

4.3.2. Regional legal environment level

The implementation of China's New Securities Law has significantly reformed the country's capital market regulatory framework, with its regulatory effectiveness contingent upon the quality of the institutional enforcement environment (Beyaert et al., 2023; Song et al., 2024). The success of audit reputation and legal penalty mechanisms is greatly influenced by the external institutional context (Zheng and Ren, 2019). In areas with robust legal frameworks, regulations are tighter, regulatory bodies are more adept and efficient, enforcement is stricter, and investor protection is more thorough. Facing heightened risks of penalties and litigation, auditors in these regions are inclined to employ more cautious auditing strategies to safeguard their reputation, consequently necessitating higher audit fees because of the increased need for audit resources (Lauck et al., 2021). Accordingly, we suggest that the implementation of the New Securities Law has a notably more substantial effect on audit fees in areas with stronger legal environments.

Data from the China Provincial Marketization Index Report (2021) was employed to assess the legal environments across Chinese provinces (Song et al., 2024; Wang et al., 2017). The sample was bifurcated into groups based on provinces' annual rankings, with the median serving as the demarcation line. According to the results presented in Table 4, for the group with a superior legal environment (column 1), the interaction term Post*treat yielded a coefficient of 0.0269, significantly positive at the 1% level. On the other hand, for the group in a less developed legal environment (column 2), the coefficient was 0.0083, showing no significance. This outcome demonstrates that the link between the escalation of punitive risks and audit pricing becomes more pronounced in areas with effective legal systems following the implementation of the New Securities Law, corroborating the findings of (DeFond and Lennox, 2011).

4.4. Robustness Tests

4.4.1. Parallel trends examination

In utilizing the difference-in-differences approach to evaluate policy impacts, it's crucial that the policy introduction is exogenous and that both the treatment and control groups display consistent trends before the policy rollout, mitigating the effects of external variables (Bertrand and Mullainathan, 2004). A trend verification test was performed to solidify the reliability of our analysis, depicted in Figure 1. This figure illustrates the parallel trends test results, with the x-axis marking the timeline and the y-axis showing audit fees, and dashed lines marking confidence intervals. The audit fees' confidence intervals hovered around zero in the 3 years leading up to the enactment of the New Securities Law, showing uniform audit fee levels across both groups and thus meeting the parallel trends criterion. Following the law's introduction between 2019 and 2022, a marked increase in audit fees was observed, alongside a pronounced discrepancy in audit fees between the two groups, post-law implementation. These observations confirm the adherence of our data set to the parallel trends condition essential for the difference-in-differences analysis application.

4.4.2. Placebo test

In the difference-in-differences framework, the placebo test serves to mitigate the influence of unobservable variables (McKenzie, 2012). This involves randomly selecting a proportionate number of samples from both the experimental and control groups to create a new treatment group. Each member of this group is then randomly assigned a policy implementation date, and a fictitious policy dummy variable is created for regression as per Model (1), a process conducted 500 times. This method constitutes the placebo test for our research, with findings depicted in Figure 2. The bulk of the randomly generated coefficients fall to the left of the true coefficient value of 0.0136 and predominantly cluster around zero.

Table 5: Robustness results using dependent variables afee

Variable	(1) Entire sample	(2) State-owned enterprises	(3) Non-state-owned enterprises	(4) High legal environment level	(5) Low legal environment level
	Afee	Afee	Afee	Afee	Afee
Post* treat	0.0005**	0.0000817	0.00106**	0.00107**	0.000332
	(2.13)	(0.27)	(2.74)	(3.14)	(0.81)
Post	0.0034***	0.00453***	0.0000209	0.00255***	0.00332***
	(21.56)	(23.17)	(0.08)	(11.09)	(14.62)
Treat	−0.0008***	−0.000243	−0.00157***	−0.000916**	−0.000806*
	(−3.48)	(−0.84)	(−4.32)	(−3.10)	(−1.97)
Size	−0.0125***	−0.0134***	−0.0102***	−0.0112***	−0.0132***
	(−86.54)	(−75.74)	(−37.36)	(−55.77)	(−64.45)
Leverage	0.0059***	0.00843***	−0.00455***	0.00516***	0.00758***
	(8.74)	(10.79)	(−3.41)	(5.42)	(7.78)
ROA	−0.0163***	−0.0155***	−0.0176***	−0.0213***	−0.0109***
	(−15.20)	(−12.92)	(−7.04)	(−13.65)	(−7.37)
Growth	−0.0004***	−0.000265	−0.000319	0.0000440	−0.00101***
	(−2.58)	(−1.43)	(−1.20)	(0.22)	(−4.15)
_cons	0.9019***	0.918***	0.855***	0.871***	0.917***
	(292.08)	(246.50)	(142.60)	(202.98)	(211.28)
Year fixed effect	YES	YES	YES	YES	YES
Firm fixed effect	YES	YES	YES	YES	YES
N	26057	7610	18447	13335	12722

***P<0.01, **P<0.05, *P<0.1, t statistics in parentheses

Figure 1: Parallel trends test result

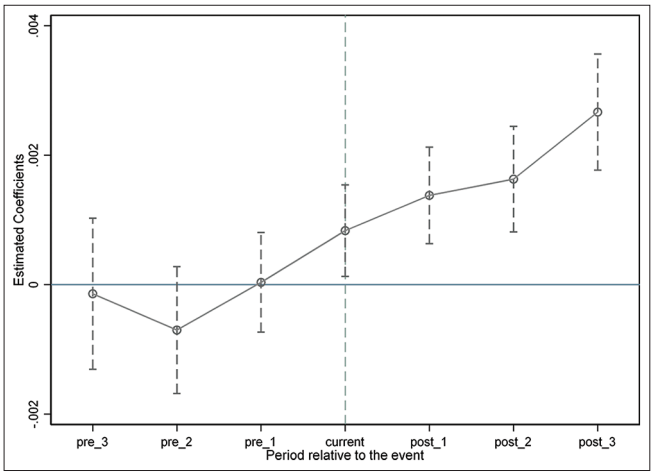
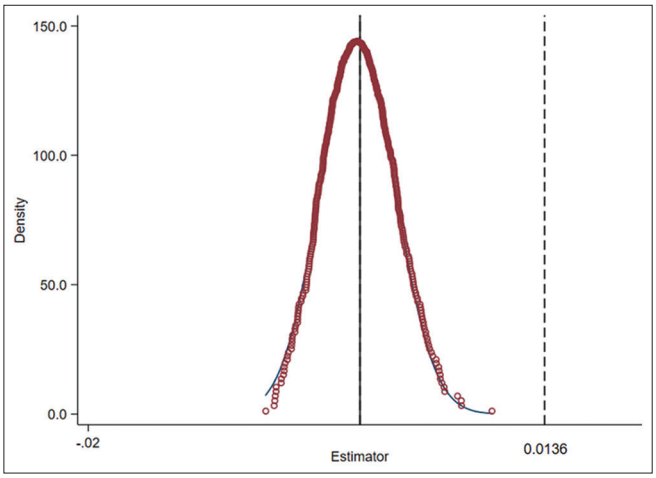


Figure 2: Placebo test result



This pattern suggests that the influence of unobservable factors on the initial regression outcomes is negligible, thereby validating the reliability of our findings.

4.4.3. Change dependent variable's proxy

Following Gandía and Huguet (2020), we replaced the Lnfee with the ratio of audit fees to total assets, labelled as Afee, for the dependent variable and reran the regression using Model (1). The outcomes, illustrated in Table 5, show that across the entire sample (column 1), the Post*Treat coefficient stands significantly positive at the 5% level. When conducting a segmented regression by ownership type (columns 2 and 3), the Post*Treat coefficient within the state-owned enterprise (SOE) group did not reach significance, while it demonstrated a significantly positive effect within the non-SOE group at the 5% level. Further segmentation by the strength of the legal environment (columns 4 and 5) reveals that in areas with less developed legal frameworks, the Post*Treat coefficient was not significant. Conversely, in regions with robust legal systems, this coefficient was significantly positive at the 5% threshold. These findings affirm the durability of our conclusions upon substituting the dependent variable's proxy, thus showcasing substantial robustness.

4.4.4. Change the grouping method for control and treatment groups

In the assessment of the authenticity and reliability of corporate financial information, the quality of accounting information emerges as a critical indicator, highlighting the accuracy and transparency of financial reports. Lower quality, indicating information that does not truthfully reflect a company's financial condition, poses higher risks for auditors during financial audits (Wang et al., 2023). With the advent of the updated Securities Law, which enhances oversight and sanctions related to audit practices,

Table 6: Robustness results using changed grouping method

Variable	(1)	(2)
	Lnfee	Afee
Post* Treat	0.112***	0.00526***
	(6.38)	(6.83)
Post	0.0690***	0.00320***
	(22.94)	(24.42)
Treat	−0.0691***	−0.00364***
	(−5.48)	(−6.58)
Size	0.338***	−0.0125***
	(103.16)	(−86.51)
Leverage	0.145***	0.00584***
	(9.47)	(8.70)
ROA	−0.363***	−0.0163***
	(−14.77)	(−15.24)
Growth	−0.00787*	−0.000305*
	(−2.20)	(−1.96)
_cons	6.318***	0.902***
	(90.67)	(292.12)
Year fixed effect	YES	YES
Firm fixed effect	YES	YES
N	26057	26057

***P<0.01, **P<0.05, *P<0.1, t statistics in parentheses

auditors working with entities presenting low-grade accounting details are necessitated to approach their audits with increased diligence, a shift markedly driven by the law's implementation.

Consequently, our research employs the quality level of corporate accounting data to segregate the experimental group, utilizing the adjusted Jones model for quantifying the extent of accruals manipulation as a criterion for appraising the quality of accounting data (Dechow and Dichev, 2002). Entities with an average accruals manipulation score surpassing their sector's median are identified as possessing inferior accounting quality and thus integrated into the experimental cohort, designated with treat as 1; conversely, they're marked as 0. This division is subsequently applied in Model (1) for regression analysis. Findings, as depicted in Table 6, with Lnfee and Afee as the dependent metrics in columns (1) and (2), respectively, reveal that the Post*Treat coefficient is significantly affirmative at the 1% level, affirming the solidity of our findings.

5. CONCLUSION

This study provides novel and robust evidence of the economic consequences of China's revised Securities Law (2019) on the audit market. Using a DID research design and a large sample of A-share listed companies, we find that the new law led to a significant increase in audit fees, particularly for non-state-owned enterprises and firms in regions with stronger legal institutions. These findings are consistent with our hypothesis that stricter legal liability and regulatory oversight under the new regime would motivate auditors to enhance their audit quality and charge higher risk premiums.

Our results contribute to the literature on audit pricing and regulatory changes by highlighting the heterogeneous effects of legal reforms across different types of firms and institutional environments. We show that the impact of the revised Securities Law on audit fees is more pronounced for firms with weaker governance and information environments, suggesting that auditors perceive these firms as riskier and more demanding under the new regulatory framework. We also find that the effect of the law is stronger in regions with more developed legal institutions, indicating that the effectiveness of securities regulations depends on the quality of legal enforcement and investor protection.

Our findings have important implications for policymakers, regulators, and market participants in China and other emerging economies. On the one hand, our study suggests that the revised Securities Law has achieved its intended objectives of improving market transparency, deterring corporate misconduct, and protecting investor interests. The increased audit fees can be viewed as a necessary cost for enhancing the credibility and reliability of financial reporting. On the other hand, our results also highlight the potential unintended consequences of legal reforms, such as increased compliance burdens and transaction costs for listed companies, especially those with weaker governance and information environments.

To address these challenges, we recommend that policymakers and regulators in China and other emerging markets should continue to strengthen the legal and institutional frameworks for securities regulation, while also providing more guidance and support for listed companies to improve their governance and disclosure practices. Moreover, market participants, including investors, analysts, and intermediaries, should pay more attention to the quality and pricing of audit services in the post-reform era, as they can serve as important signals of firms' financial reporting credibility and risk profiles.

Finally, our study points to several promising avenues for future research. First, scholars can examine the long-term effects of the revised Securities Law on audit quality, financial reporting transparency, and market efficiency in China, using more granular measures and longer time horizons. Second, researchers can investigate the spillover effects of the law on other aspects of corporate behaviour and market outcomes, such as firms' investment, financing, and innovation activities. Third, future studies can explore the potential heterogeneity in the impact of the law across different industries, regions, and ownership types, as well as the moderating roles of firms' internal governance and external monitoring mechanisms.

6. ACKNOWLEDGMENT

This work was supported by University Sciences Research Project of Anhui Province (Project Number: 2022AH052526) and Research Project on Educational Teaching Planning of Anhui Vocational and Adult Education Association (Project Number: AZCJ2023079). The authors also acknowledge UNIMAS for providing the resources and environment necessary for the completion of this research.

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