



## The Impact of Audit Reports on Financial Information Content

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### ABSTRACT

Investors fund in order to access to more wealth. Financial information of companies is one of the important factors considered by investors in making decision. According to accounting standards, the major goal of providing forms and financial reports is providing useful information about financial position and the results of operations of commercial unit for user decision making. Several factors influence on financial information provided by companies. One of these factors can be audit reports. Therefore, major goal of this research is investigating the effects of audit reports on financial information reported in Tehran Stock Exchange. Method of this research is practical in goal and is descriptive in type. The types of auditor and auditor's assessment (audit organizations or institutions) were proposed as independent variables and financial information (stocks return) was proposed as dependent variable. In this research 117 accepted companies in Tehran Stock Exchange during 2009-2014 were selected as statistical sample. Research hypotheses were tested by fitting of linear regression models of combined data. The results showed that the type of auditor and auditor's assessment have a significant relationship with stocks return (financial information).

**Keywords:** The Type of Auditors, Stocks Return, The Type of Auditor's Assessment, Tehran Stock Exchange

**JEL Classifications:** E44, M42

### 1. INTRODUCTION

The existence of vivid and reliable financial information that is the product of a comprehensive reporting system is considered as the main elements of assessment of situation and function of a company and decision-making about the securities exchange issued by that. In the recent professional societies, from the perspective of users, the information is considered to be reliable that an independent organization on the company's reporting process and at the gravity center of this process, i.e., to monitor the financial statements. An example of such independent organizations are audit firms that mainly in the business units, the internal control structure of the reporting unit and the final product of the internal control system, the financial statements are reviewed and monitored (Hassas and Jafari, 2010). On the other hand, in the commercial world, transactions and economic events are documented via assembling evidence by accountants and recorded in the accounts. The results of transactions and economic events are available to interested parties out of extracted accounts and within framework of financial reports. However, the biased information, misleading, irrelevant or incomplete may cause the

wrong decision-making. Complexity of economics' issues and the process of converting them into information also cause the possibility of appearance of errors in processing information and as a result, it makes trouble to recognize the quality on presented reports for the reports' users. On the other hand, conflict of interest between producers of fiscal statements and users from them causes a concern for users. Besides, the lack of direct access of users and their distances to information producer causes uncertainty and ambiguity of the financial reports' users to them. In this situation the audit is formed on the basis of the above needs and it is a tool to eliminate the doubt and ambiguity of financial reporting by confirming their quality. It should be noted that in some conditions in reporting environment, allowing direct assessment of data quality by users is very difficult. Despite these circumstances, it makes indirect evaluation of information quality very necessary. This is a situation where there is justifying the need for auditing by independent auditors and making opinion, could be due to a conflict of interest, important economic consequences, complexity and lack of direct access. Auditors validate presented financial information and users can be sure that the using information enjoys good quality (Hajiha and FeizAbadi, 2013). According to this, the

current research is a review of subjective literature of audit report and the content of reported financial information will influence on listed companies in Tehran's Stock Exchange. Then, the impact of audit report and content of reported financial information and of companies listed on Tehran Stock Exchange will be discussed.

## 2. PROBLEM STATEMENT

Today shareholders can use audited financial statements as an important tool to notice how to operate their assets and ensure the accuracy of managers' performance. The usefulness of content of numbers and submitted figures in the financial statements that is the final product of accounting is the most controversial issue of subjects in scientific meetings. In general, the first and foremost goal is to provide financial statements. From the information reported to investors and creditors and other current and potential clients for investment decisions, accreditation and other similar decisions become beneficial. One of the most useful accounting information is efficient figure of shares. On the other hand, the possibility of bad intention in setting and preparation of the financial statements by the board, led to the need for the audit profession and individuals called auditor to be felt. Existence of vivid and comparable financial information is one of the main pillars to respond the executives and essential needs of economic decision-making. Done researches show that more disclosure and transparency will follow many advantages for companies: Long-term investment by the investors, improving access to new capital, less capital expenditures, credible and responsible management and ultimately higher stock price (Banimahd et al., 2014).

In addition, to take the advantage of financial information in decision-making of mentioned groups, that accounting targets and financial reporting require to reveal related information to appropriate species and access this information become feasible for everyone. Increase of disclosure about information for users who aren't able to determine the company future prospects is useful and this advantage is through reducing the risk of misallocation of their capital. Moreover, one of the crucial conditions for the confidence of investors and creditors in constructive economic activity is sufficient information to make decisions about purchasing, holding or selling stock and assess the performance of companies' managers (Hasani and Hoseini, 2010).

Auditor's report on the process of decision-making by users of financial statements is considered as one of the most useful tools. When auditors is not to make an acceptable opinion on the information given in financial statements, his opinion validate the financial statements and information contained in the financial statements remain unchanged, or to be more precise, the registered information will be approved. If qualified opinion a failed or lacks of opinion without an impartial financial expert questions all or part of the information contained in the financial statements. The effect of the auditing profession's activities and its role in the stock returns of companies listed in Tehran Stock Exchange and the investment process relies on the information provided by companies' managers as an evaluator reference and it is judged by the auditor. Through this result potential and actual shareholders are reflected (Jamei et al., 2012).

Auditing profession has effective role on improving informational system and inspiring confidence of each country's financial reports. With the increase in the number of users of the auditor's report as customers of public goods, has led the quality of auditors' work to be paid attention. Quality of auditors' work and their remark, can improve the country's financial informational system and finally making decision for an optimal economy. In the recent years the formation of CPAs, (Certified Public Accountants) a part of the activities of audit organization has been assigned to private institutions of its community (Moradzadeh and Rahmannedad, 2011). The content of accounting information and auditor's opinion and its role in decision-making of readers, especially investors in the stock exchange were the subjects that has been investigated and studied over the past four decades in the markets of Australia, Canada, England, France, Spain and the Islamic Republic of Iran. Now the main question is whether the type of the auditor and the auditor's opinion has an impact on stock's returns?

## 3. EXPRESSING MODELS AND VARIABLES OF THE RESEARCH

1. 
$$Y_{it} = \beta_0 + \beta_1 DQO_{it} + \beta_2 Size_{it} + \beta_3 Leverage_{it} + \beta_4 Growth_{it} + \beta_5 ROA_{it} + \beta_6 ROE_{it} + \epsilon_{it}$$
2. 
$$Y_{it} = \beta_0 + \beta_1 DUO_{it} + \beta_2 Size_{it} + \beta_3 Leverage_{it} + \beta_4 Growth_{it} + \beta_5 ROA_{it} + \beta_6 ROE_{it} + \epsilon_{it}$$

### 3.1. Financial Information Content (The Dependent Variable)

The content of financial information is called to the information that is effective on users' decisions on assessment of past events, present and future or assessment and correction of their past evaluation (Dianati et al., 2012).

### 3.2. Stock Returns (The Dependent Variable)

It is called to the benefit and profit from an investment. In other words, return is the ratio of total revenue (loss) from investments in a specific period to the quantity of the capitals that have been applied to earn this income initially in the same period and has been consumed (Robu and Robu, 2015).

### 3.3. Audit Report (Independent)

The main purpose of an audit is that the auditor declares a professional concept to the integrity of financial statements with reviewing the results of the investigation of the registers and documents that the examined final financial statements of the institution rely on them, and regarding the information and different explanation acquired during the process of the verification. The statement in the report entitled "Audit report" or the auditor's report and auditors' report as the person or authority who has assigned auditing to the auditor, is presented that may be issued in two forms either short or detailed in appropriate terms (Hajiha and Rafiei, 2014).

The auditor's opinion (independent) auditor's opinion is said to the professional reporting process respecting the financial statement (Rahimian and Hedayati, 2013).

The type of auditor (independent) the type of auditor is said to the type of audit institutions that include large and small audit institutions (Jahanshad and Navaei, 2013).

#### 4. RESEARCH LITERATURE

Callen and Khan (2013) in their research surveyed the quality of accounting information and delay information affecting this information on the stock price and its relationship with the future stock returns. They stated that whatever the quality of accounting is reduced, the relevance and reliability of it will be reduced and consequently, prediction accuracy of cash flows and returns will be reduced for investors.

Noor-ul-Haq et al. (2012) examined the relationship between economic power and the state auditor in 46 countries. They showed that whatever the quality of government is politically and economically powerful, then choosing four large auditing institutions is plausible. They also confirmed the affluent countries that have accepted international financial reporting standards, choosing four large auditing institutions is plausible. The results of their research confirmed that whatever the government of a country is stronger the demand is more for higher-quality audit services (Kadilli, 2015).

Leventis and Dimitropoulos (2010) audit services pricing, the interest quality and the board independence were examined for 97 companies, between the years 2000 and 2004. The results of this study show that there is a positive relationship between auditor independence and audit services pricing. Moreover, there is a positive relationship between audit services pricing and interest management that the result is for the companies with small size (Kausar et al., 2015).

Chen et al. (2010) examined the effect of auditor size (as a factor of audit quality) on interest management and capital costs for the two categories of Chinese companies. A group of companies owned by the states and others non-state-owned companies. The results of this study showed that the impact of auditing quality in reducing interest management is stronger in private companies than public companies. In addition, cost of capital, that investor consider for the information risk as a value. Private companies are more influenced by the quality audit than public companies.

#### 5. RESEARCH HYPOTHESES

H<sub>1</sub>: There is a significant relationship between type of auditor's opinion and stock returns.

H<sub>2</sub>: There is a significant relationship between type of auditor (audit organization or institution) and stock returns.

#### 6. RESEARCH METHODOLOGY

This study is considered descriptive in terms of type of research and applicable, in terms of category of researches based on purpose. The statistical community this research includes all the

companies listed in Tehran Stock Exchange from 2009 and after that until 2014 which were present in stock exchange including 463 companies. In this study, sampling method is elimination systematic as following conditions:

1. Not to be among insurance companies, investment, leasing, banks and financial institutions, financial moderators, because these companies have the nature of the different activities
2. The companies that their financial data can be written during this 6 years and in this period have not had out of stock exchange and entered stock exchange or even have not have stock exchange interruptions and other transactions
3. In order to ensure comparability and avoid the heterogeneity of its fiscal year ending March 18<sup>th</sup> and financial year should not be changed during the years 2009-2014
4. Financial statements and explanatory notes are available accompanying them.

In this study, the panel data is applied using software Eviews 7.

#### 7. THE RESULTS OF HYPOTHESIS TEST

##### 7.1. The Results of First Hypothesis Test

After the initial analysis of the regression model output as the Table 1 were determined after an examination of the research's variables, it was revealed that fiscal leverage is not effective on stock exchange's returns in this model that with elimination of this variable the underneath right model was analyzed.

As it is observed in Table 2, based on the results of initial model's estimation, regarding to P value. Statistic F is proved that the model is approved by 99% confidence.

Durbin-Watson with 2.3176 shows lack of correlation between the errors. In addition, according to the obtained coefficient of determination, used variables in the model explains totally 0.52% of the dependent variable's behavior.

##### 7.2. The Results of Second Hypothesis Test

After the initial analysis of the regression model output as the Table 3 were determined after an examination of the research's variables, it was revealed that fiscal leverage is not effective on stock exchange's returns in this model that with elimination of this variable the underneath right model was analyzed.

As it is observed in Table 4, based on the results of initial model's estimation, regarding to P value. Statistic F is proved that the model is approved by 99% confidence.

Durbin-Watson with 2.30 shows lack of correlation between the errors. In addition, according to the obtained coefficient of determination, used variables in the model explains totally 0.32% of the dependent variable's behavior.

#### 8. CONCLUSION

Concerning the significant level variable, the type of auditor's opinion is 0.0244 and this number is smaller than 5%. So, the

**Table 1: The results of first hypothesis test**

**The independent variable: The type of auditor's opinion**  
**A total of 117 firms during the period of 6 years from 2009 to 2014**  
**Total views: 702**  

$$Y_{it} = \beta_0 + \beta_1 DQO_{it} + \beta_2 Size_{it} + \beta_3 Leverage_{it} + \beta_4 Growth_{it} + \beta_5 ROA_{it} + \beta_6 ROE_{it} + \epsilon_{it}$$

Variables	Variable coefficient	SD	t	Significant
C	-5.363379	0.648846	-8.266030	0.0000
DQO	0.079977	0.035755	2.236783	0.0257
SIZE	0.902556	0.112073	8.053284	0.0000
LEV	-0.084771	0.287793	-0.294554	0.7684
GROW	0.110607	0.053391	2.071642	0.0387
ROA	0.807440	0.394601	2.046217	0.0412
ROE	0.279628	0.067092	4.167865	0.0000
Coefficient of determination - 0.4947			F - 1.8835	
Durbin-Watson - 2.1169			The probability statistic F - 0.0000	

ROE: Return on equity, ROA: Return on assets, SD: Standard deviation

**Table 2: Results of first model test after removing the variable leverage**

**The dependent variable: Stock returns**  
**A total of 117 firms during the period of 6 years from 2009 to 2014**  
**Total views: 702**  

$$Y_{it} = \beta_0 + \beta_1 DQO_{it} + \beta_2 Size_{it} + \beta_4 Growth_{it} + \beta_5 ROA_{it} + \beta_6 ROE_{it} + \epsilon_{it}$$

Variables	Variable coefficient	SD	t	Significant
C	-5.369807	0.647964	-8.287203	0.0000
DQO	-0.080519	0.035690	-2.256060	0.0244
SIZE	0.893987	0.108116	8.268751	0.0000
GROW	0.108474	0.052861	2.052068	0.0406
ROA	0.883124	0.297320	2.970281	0.0031
ROE	0.273190	0.063241	4.319816	0.0000
Coefficient of determination - 0.5246			F - 2.0021	
Durbin-Watson - 2.3176			The probability statistic F - 0.0000	

ROE: Return on equity, ROA: Return on assets, SD: Standard deviation

95% confidence level existence of a relationship between types of auditor's opinion significantly influences on stock returns, and the first hypothesis is confirmed. Due to the positive coefficient of this variable, the relationship of these variables is direct.

Also concerning the significant level variable, the type of auditor is 0.0132 and this number is smaller than 5%. So, the 95% confidence level existence of a relationship between the types of auditor (audit organization or institution) significantly influences on stock returns, and the second hypothesis is confirmed. Due to the positive coefficient of this variable, the relationship of these variables is direct.

## 9. SUGGESTIONS RESULTS OF THIS RESEARCH

It is recommended to companies' managers, always design and implement their accounting system properly so as to see more

**Table 3: The results of second hypothesis test**

**The independent variable: Type of auditor (audit organization or institution)**  
**A total of 117 firms during the period of 6 years from 2009 to 2014**  
**Total views: 702**  

$$Y_{it} = \beta_0 + \beta_1 DUO_{it} + \beta_2 Size_{it} + \beta_3 Leverage_{it} + \beta_4 Growth_{it} + \beta_5 ROA_{it} + \beta_6 ROE_{it} + \epsilon_{it}$$

Variables	Variable coefficient	SD	t	Significant
C	-5.128633	0.659260	-7.779373	0.0000
DUO	0.088979	0.035546	2.503234	0.0126
SIZE	0.873747	0.114196	7.651291	0.0000
LEV	-0.167028	0.297767	-0.560935	0.5751
GROW	0.113647	0.052801	2.152339	0.0318
ROA	0.733349	0.425790	1.722326	0.0855
Coefficient of determination - 0.2990			F - 2.0245	
Durbin-Watson - 2.3041			The probability statistic F - 0.0000	

ROE: Return on equity, ROA: Return on assets, SD: Standard deviation

**Table 4: Results of second model test after removing the variable leverage**

**The dependent variable: Stock returns**  
**A total of 117 firms during the period of 6 years from 2009 to 2014**  
**Total views: 702**  

$$Y_{it} = \beta_0 + \beta_1 DUO_{it} + \beta_2 Size_{it} + \beta_4 Growth_{it} + \beta_5 ROA_{it} + \beta_6 ROE_{it} + \epsilon_{it}$$

Variables	Variable coefficient	SD	t	Significant
C	-5.135537	0.659055	-7.792272	0.0000
DUO	-0.088423	0.035566	-2.486135	0.0132
SIZE	0.855669	0.109204	7.835479	0.0000
GROW	0.109606	0.052305	2.095507	0.0366
ROA	0.896723	0.304350	2.946357	0.0033
ROE	0.276096	0.064351	4.290493	0.0000
Coefficient of determination - 0.3283			F - 2.038	
Durbin-Watson - 2.3056			The probability statistic F - 0.0000	

ROE: Return on equity, ROA: Return on assets, SD: Standard deviation

return in their area. Investors are also recommended that choose the companies that auditors have confirmed their accounting reports. Because, investing in these companies can be secure and the future investment less risky.

Considering that after the re-stock investors show more trust and willing to the companies that there is opinion of formal auditors on their audit reports. Therefore, the value of their shares immediately increases and immediate returns occur on share's price. Therefore, it is recommended to managers to exploit official auditors to audit their registers so as to be able to earn return immediately from supplying their shares.

## 10. RESEARCH LIMITATIONS

1. Collecting variable's data of share's immediate return have had many difficulties because of the complexity of calculation and access to information, and it seems, change in the number

of days after the meeting could change the results.

2. Management and political problems and macro-economic indexes such as changes in the company's managers after a general meeting is an issue that can affect the research's results by interfering in share's returns.

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