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Corporate Governance and Audit Quality: A Comparison of ASEAN Countries

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Abstract:

The issues of corporate scandal have negative affect in accounting manipulations, regulators, practitioners, researchers and organizations in the world. Due to the fact of this, there is need to review the code of corporate that governed the corporations of many countries. As such the new regulations and practices in developed countries, The audit committee and accounting firms which play a significant role in ascertaining the validity, acceptability, and reliability of high quality. Similarly, corporate governance plays a significant role in improving the auditing function and its effectiveness. The study is carry out on the sample of 120 non-financial firms listed on the Indonesian stock exchange, Busra Malaysia and Thai stock exchange is collected through the channel of annual reports of the year 2012, 2013, 2014, 2015 and 2016. We have used Logit regression to analyses the impact of corporate governance on audit quality of three ASEAN countries. The findings of the study have shown that in non-financial firms listed in Philippines audit committee and board characteristics has significant. This study will be helpful for the students, auditors, policymakers, and researchers in understanding the impact of corporate governance and audit fee.

Keywords: corporate governance; audit quality; ASEAN; non-financial firm.

JEL Classification: G34; H83

Introduction

Audit quality is a reliable evidence amongst the most basic issues in audit practice today. A couple individuals and social affairs; both inside and outside, have an excitement for the way of audited business information International Auditing and Assurance Standard Board. Audit quality assumes a vital part of keeping up an effective business sector environment, a free quality audit supports trust in the validity and honesty of financial articulations which is key for well-working markets and upgraded financial performance. External audits performed as per excellent evaluating measures can advance the use of accounting principles by reporting elements and guarantee that their financial proclamations are dependable, straightforward and helpful.

Sound audits can fortify strong risk management, internal control at firms and corporate governance, along these lines adding to financial performance. High quality outside auditing is a focal part of well-working capital markets. The accounting literature concentrates on two principal strengths that rouse auditors to convey quality a suit/protection motivating force and a reputation incentive. Under the main thought process, if auditors are legitimately obligated for audit disappointments, then they have a motivator to deliver high quality to avoid the costs of litigation. The insurance part emerges on the grounds that investors consider larger audit firms as these organizations can better meet investors 'lawful cases, in this manner giving financial resources plan of action against poor audit quality. Additionally, the reputational incentives motivate, accounting firms have to avoid audit disappointments since audit quality is profitable to customers. Customers imperfection to different auditors when an audit company reputation for quality turns out to be more awful (Skinner and Srinivasan 2012, Suryanto 2014).

Though, the Big Four firms as characterized in Business Week (Gerdes 2009, Hadi *et al.* 2016, Kachouri and Jarboui 2017) are Deloitte and Touche, Ernst and Young, PricewaterhouseCoopers (PwC), and KPMG which are positioned top among 50 open and legislative organizations. By and large, dependable and fair appraisal of information about public recorded organizations' financial position gave by the auditor is essential to speculators to settle on investment choice and improves the effectiveness of financial markets.

They are under statutory commitment to answer to the Securities Commission (SC) or Stock Exchange any action or undertaking of the organization that as they would see it constitutes an anomaly or rebelliousness with any posting prerequisites or securities law.

Additionally, the cordial association among the management, shareholders and the board were addressed in order to guarantee the investors and compete with the standard of developed countries who are already successful in theory and practice of the code of Corporate Governance (CAMA 2004). The events had a genuine

obliterating impact on stakeholders as far as misfortunes in their ventures. On the procedure to restore the certainty to the investors, diverse laws were put set up, for instance, Sarbanes Oxley Act Code 2000 in the United States (US) and launching of CG Code (2000) in Malaysia is required to relieve corporate outrages and other related issues. Hence, corporate disappointment and outrages are still there, for instance, the issue

This study assesses, how organizations give an ideal setting to considering the impact of auditor choice on their loan fees. This shows connecting with a Big Four auditor, which has a brand name reputation for supplying a higher-quality audit could upgrade the believability of financial proclamations, empowers young firms to decrease their acquiring costs.

1. Literature review

Higher audit quality is pro-actively providing assurance to the investors, deliver a service that goes beyond the simple audit and creates an avenue to consulting (Behn, Carcello, Hermanson and Hermanson 1997). Hai (2018) argued that achieving higher audit quality should be balanced among the relationships of personal, professional an independence and competence of accounting firms. Lee *et al.* (1995) suggested that accounting firms cannot choose to independent unless it is competent. Clients observed that larger accounting firms are independent and competent in international markets and smaller accounting firms have low and incompetence experiences in local markets. The competence of Big Accounting Firms has made them involve and contribute in standard setting such as Anglo-Saxo. Nobes and Parker (2008) claim that an accounting system in Ministry of Finance, China was developed by Deloitte one of the Big Accounting Firms due to their independence and competence in international accounting standards board (IASB). Adequate training and competence in auditing are evidenced of high-quality auditing to the investors because the result is prepared by professional accounting firms (Gul, Ferid, Hai, Teoh, Beer and Schelluch 1994).

In addition, independence of an auditor is indicated as a factor that determined the accounting firms size (Abu Bakar, Rahman, and Rashid 2005). Mautz and Sharaf (1961) revealed that large accounting firms can be perceived through research facilities, independence, financial resources, qualified experience, and training staffs. However, small accounting firms with single client resulted in the risk of dependence due to the small portfolio of the client compared to those of Big accounting firms (Mautz *et al.* 1961, Azam *et al.* 2016, Zou *et al.* 2017). Large accounting firms protect their independence and reputation because of large client portfolio the firm's audit. Incompetence and low-experiences staff or any elements that can hinder the quality of independent auditors may less the standard of quality of audit

Palmrose (1988) reveals audit quality as far as levels of affirmations. More elevated amounts of affirmations (*i.e.* the probability of financial statements should comprise zero misstatements or fewer mistakes) have relationships with the standard audit quality at the way around. Audit failures have been created as the basis of this definition (in a situation where the issue of misstatement appears, or auditor failed to recognize inconsistent materials) which need to be found in the legal process. As indicated by Francis (2004) described low quality as an audit failure which may bring about a few results, for example, regulatory authorizations, litigation rates, and business disappointment.

According to Institute of Chartered Accountants in England and Wales (ICAEW) in (2002) as a regulator, defined "audit quality as the best expectations that contain evidence, reliability, and appropriate expertise opinion, free and fair judgments have the quality of the audit." However, regulator agrees that independent auditors that provide adequate audit evidence have a higher quality service and can be relied upon.

Francis (2004) audit quality is contrarily identified with non-fulfillment audit: the lower the nature of auditing, the higher the non-fulfillment rate. Regardless of the way that specialized qualities, for instance, an auditors' ability to distinguish and report mistakes, have been claimed as the characterizing parts of a quality audit. Duff (2004) suggests that audit quality is contained both specific quality and service term of quality (the desires and client's satisfaction). Specialized quality contains ability, experience, skill, integrity and independence scales. However, advantage quality is depicted by responsiveness, feeling and the procurement of client services and Non-Audit Service (NAS).

Audit quality is chosen by auditor's capacity to get ruptures of accounting norms and in this manner the auditors motivating forces to report such breaks *i.e.*, audit quality could be a result of auditor capacity and freedom. DeAngelo (1981) contends that huge enterprises are identified with higher audit quality as a result of they are extra autonomous. For large auditors like Big Four firms, no individual or customer is monetarily fundamental with respect to the estimation of an identified audit disappointment. Besides, Big Four industry has set up brand-name position and in this manner, have motivators to shield their prestige by providing desire quality audit (Simunic and Stein 1987).

Clients ascribe audit quality upheld the name of the auditor. All in all, the vast audits firms have needed to separate themselves from option auditors by using their money to partner with character capital (Beatty 1989, Bokhari and Khan 2013) and observed as giving higher quality audits upheld their apparent (1) capacity (by ethicalness of their genuine dispensing on auditor instructing offices and projects) and (2) autonomy (by the excellence of their size and tremendous arrangement of clients, that presumptively offers them the financial quality square up to, or go stroll from, a clients if fundamental).

Expected by these contentions, early studies utilize the experience, information asymmetry, and service between the Big Four and Non- Big Four firms and demonstrate that Big Four industry performs audits of upper quality and are more extra moderate. Firms prefer toward name-brand (Big Four) auditors on the off chance that they are liable to extra agency clashes. Coopers (2002) contends that audit quality relies upon a few elements together with auditors "information and knowledge of the organization being examined and the business in which it works". Teoh and Wong (1993) place that to the degree that investors see Big Four auditors as giving higher quality audit, *i.e.*, as recording a great deal of believable income for his or her auditees, the stock worth response to amazing reported profit for vast four auditees should be greater than that of option auditees.

These arguments, therefore, recommend that auditors with industry experience area unit a lot of doubtless to observe misrepresentations and irregularities than auditors while not. DeAngelo (1981) contends that firm size might be an intermediary for quality (auditor independence) since there is no single client is vital to a Big Four auditor and this make auditor protect their reputation (their whole clientele) for not misreporting. Against this, firm with just single client may consistently infer that they require a lot of to realize by going in conjunction with their client and misreporting than.

The work expertise in massive Big Four companies is so doubtless to "mold" auditors that end up being totally different from auditors in non-Big Four companies. As an alternative, those recruited by large four firms might have comparatively additional conservative personalities that additionally results in conservative audit outcomes. Evidence indicates that client of massive four audited firms has lower irregular collections which means less forceful profit management conduct thus higher income quality (Becker, DeFond, Jiambalvo and Subramanyam 1998). Gottschalk (2011) that the perspective of audit quality may be categorized into twofold.

The lawful perspective of auditing offers a basic classification of either "audit disappointment" or "non-audit disappointment." An audit disappointment happens if the auditor is not free truth be told, or if an autonomous auditor mistakenly problems a spic audit report due to the lack to collect adequate equipped proof by auditing due process. Conversely, a "decent audit" or a non-disappointment is one within which the auditor agrees to examine gauges. and problems the proper feeling with regard to the client's financial explanations at an acceptable level of audit risk.

From at opportune time, audit quality has been characterized as a result restrictive on the neighborhood of specific characteristics of auditors. The widely utilized definition by Alduwaila *et al.* (2018) characterizes the issue of audit quality as "the sector evaluated mutual chance which independent auditor can each notice an opening in an exceedingly customer's accounting, and report the rupture what is more contends that business firm size is a mediator for audit quality, as no single client is imperative to greater accounting firms and, then, larger accounting firms are additional inconceivable than smaller accounting firms.

The Sarbanes Oxley (SOX) Act (2002) allocated particular obligations to the audit committee, it is the responsibility of the committee to oversight auditors work, compensate and resolve financial reporting. Audit committee likewise has right to select or appoint independent advice and consultants (Klein 2003).

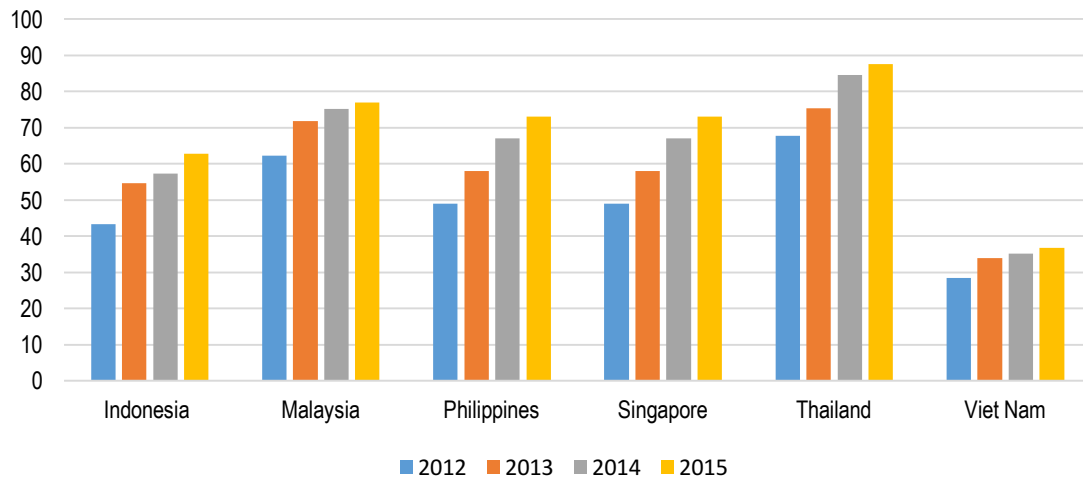
According to ASEAN corporate governance Scorecard Country report and assessment (2015). The mean score of all the member's counties has increased during the period of four years from 2012 to 2015. The Thailand in leading, Malaysia is second and Vietnam is at last.

The adequacy of audit committee relies upon the degree to which the group can resolve issues and issues confronted by the organization and to enhance their checking elements of the organization (Abbott, Park and Parker 2000). A more dynamic audit committee is relied upon to give a viable observing component. In addition, Akgun and Tektufekci (2017) require that all individuals from an audit committee should be autonomous of the company's management as well as those who oversee the financial reporting processes and accounting procedures. This idea is in line with Malaysia Corporate Governance.

Table 1. Mean corporate governance score of ASEAN countries

	Indonesia	Malaysia	Philippines	Singapore	Thailand	Vietnam
2012	43.29	62.29	48.9	48.9	67.66	28.42
2013	54.55	71.69	57.99	57.99	75.39	33.87
2014	57.27	75.22	67.07	67.02	84.53	35.14
2015	62.68	76.91	73.09	73.09	87.5	36.75

Figure 1. Mean corporate governance score of ASEAN countries



Source: ACMF Working Group D Secretariat 2015.

In Malaysia corporate governance, on the Section 344A (2) of the Bursa Malaysia Listing Requirement requires audit advisory group to comprise at least three individuals, a greater part of which must be non-executive directors. The code (Part 2, AA III) expresses that the group of audit advisory must have no less than 33% (*i.e* 1/3) independent non-executive directors. A study by Zandi and Elwahi (2016) found that the Malaysian audit board independent sees that the board assumes a successful part in checking financial capacities and audit roles. As indicated by McMullen (1996) estimated that an independent non-executive audit board is more viable. They concentrate on 128 organizations which disclose financial reporting issues. They found that organizations with financial reporting issues are less inclined to have audit advisory groups made just out of independent executive's board. Audit group independent upgrade the viability of checking limits. It serves as a sustaining administrator to the free of inside and outside auditors. It is set that the more independent of the audit counseling gather, the higher the level of oversight and the more likely that people exhibit impartially in evaluating the propensity of the association inside reporting control and accounting. This demonstrates a self-governing audit board can help companies deal with the intelligence of business. Through the way when they are gone up against with financial difficulties, they are required to propose certain movement plans to direct the issue.

The absence of freedom from the management may incidentally transform the individuals from the audit group into an expansion of the management group itself and this will crush the goal of having the audit advisory group in any case. There ought to be an expansive majority of independent or non-executive's directors, audit group individuals that serve on the audit advisory group to improve firm value. A financial master is any part who has the training or experience of a public accountant, principal accounting officer of an issuer, principal financial officer, auditor or has been in a position requiring the comprehension of sound accounting guidelines and financial articulation involvement in the arrangement and auditing of financial proclamations of practically identical issuers, involvement in the use of such standards regarding the representing appraisals, understanding of audit committee functions, accruals and reserves, and experience with internal accounting" (Dalley 2003).

Financial knowledge decreased extortion in corporate financial reporting. A formal acknowledgment of this necessity was recently made in the US with the passing of the SOX (2002) which requires every public recorded organization to uncover regardless of whether it has a financial master in the audit group. Coopers (1999) and SEC (2003) regulators contended that financial mastery is fundamental to guarantee that the audit committee satisfies their essential obligations of regulating the financial reporting prepare and upgrading financial reporting quality.

Schmidt and Wilkins (2012) claim that financial master of audit board is essential since it audit advisory group is in charge of the financial reporting process and audit quality. He focused on that audit boards with financial

ability can offer huge worth to the stakeholders and client, since their financial information is the favorable position of distinguishing any control. DeFond and Francis (2005) find that market contestants respond decidedly to the arrangement of an audit advisory group with a financial master in accounting, however, no response is noted for audit advisory group with non-accounting financial capability. This is because of the way that the arrangement of council individuals with accounting financial knowledge enhances the oversight capacity of the advisory group and therefore gives a tenable sign to the investors that the organizations seek to a higher audit quality and financial reporting.

Fama and Jensen (1983) referred managerial discretion as an effect of the instructive asymmetry that prompts to agency costs and agency issues. The partition of the exercises of management, informational asymmetry and the ownership which may result in misunderstanding or trust. The manager's self-premium could prompt the mismanagement of firm assets, for the case, through putting resources into risk and impulsive activities to the detriment of the stakeholders who give capital. In this way, to control irreconcilable situations and diminish agency costs, different inside and outside components (known as a corporate mechanism) have been recommended. For instance, the team of board director is built up as an alternative solution for such clashes. The activity of company's board is important due to the fact that they are outside directors and differentiate from management, this will allow the board to provide high-quality monitoring and serve stakeholders with due process (Fama and Jensen 1983).

2. Data and methodology

Data source

The collection of secondary data of 120 firms listed on the Indonesian stock exchange, Bursa Malaysia and Thai stock exchange is collected through the channel of annual reports of the year 2012, 2013, 2014, 2015 and 2016 and the annual reports were used to collect the data concerning the audit committee and big Four/Non-big Four. 40 firms from each stock market are selected to for a balanced panel of 120 firms.

The independent and dependent variables are measured, classified, and quantified into a numerical type. Therefore, the association between the audit committee and audit quality is examined and assessed in a very applied statistical means from the data collected. The study is predicated on a panel data study.

Logit regression

We are using logit regression in our study, the purpose we are using this technique is that it breaks down the relationship between dependent and independent variable. As our dependent variable is a dummy variable so this technique is recommended by Al-Ghamdi (2001). Who argued that the logit regression techniques can be connected when the dependent variable is categorical. As a result, the remainder of this study discussion will focus on independent variables in this regression analysis.

Model specification

To measure the impact of corporate governance on quality we have used the models, which are given below:

$$AUDITQ_{it} = \alpha_0 + \alpha_1 NED_{it} + \alpha_2 FENED + \alpha_3 ACM_{it} + \alpha_4 BS_{it} + \alpha_5 SIZE_{it} + \alpha_6 LEV_{it} + \alpha_7 PROF_{it} + \varepsilon_{it} \quad (1)$$

where: for each company (i) and each year (t), AUDIT is a dummy variable which gives value 1 if it is engaged with big four auditing firm; NEDAC is the ratio of non executive director member of the audit committee to a total member of audit committee; FENEDAC is a dummy variable which gives one if the non-executive director of the audit committee is accounting qualified and zero otherwise; ACM audit committee meeting which represents the frequency of audit committee meetings.

3. Correlation analysis

In Table 2 we have disced the result of correlation test. The results show that there is a bivariate statistical correlation among all the relevant variables. The correlation table shows that audit quality is positively related to a ratio of non-executive directors to total directors. And financial expertise of Non-executive. Whereas it is negatively related to Audit committee meeting. The correlation among other independent is moderately okay.

Table 2. Correlation analysis

	AUDITQ	NED	FENED	ACM	SIZE	PROF	LEV
AUDITQ	1						
NED	0.5079*	1					
FENED	0.4764**	0.5354*	1				
ACM	-0.2327	-0.2127	0.2906	1			
SIZE	-0.2037**	0.2056**	-0.3148*	-0.3328*	1		
PROF	-0.4433**	0.3313*	-0.3711*	-0.4492*	0.1982	1	
LEV	0.4391***	0.2452**	-0.5741*	-0.2101*	0.2101	-0.1205	1

3.1 Results and discussion

Based on hypothesis stated the relationship between corporate governance and AUDIT QUALITY is explored using logit regression techniques. As our sample comprises of three different countries so the results of each country are presented in Table 3. Below we have discussed the results of each country.

Malaysia

Malaysia is among top economies of South East Asia and during last two decades and especially after the Asian Financial crisis it has shown tremendous progress in codes of Corporate governance. In term of score among Asian countries, it stood second.

The result if the study is highlighting that the board independence which is measured as the ratio of non-executive directors to the total director. The result of the study is revealing some interesting facts Board independence and board size are in negative relation with audit quality which is indicating that the Malaysian firms with more directors on the board and majority of them are independent that firms suffer in audit quality Whereas the financial expertise of board members and frequency of audit committee meeting is positively related with audit quality. This shows that if a board has members with accounting and finance degrees then this will affect the audit quality. Overall the impact of corporate governance on audit quality is significant.

Thailand

Among ASEAN countries the Thailand is among the country which is leading the corporate governance code. The average growth in a score of Thailand is highest among region countries.

The result if the study is highlighting that the board independence which is measured as the ratio of non-executive directors to the total director. The result of the study are revealing some interesting facts Board independence, board size, board expertise and frequency of meeting by audit committee has a significant positive impact on audit quality and are in negative relation with audit quality which is indicating that the Malaysian firms with more directors on the board and majority of them are independent that firms suffer in audit quality. Similarly, frequency of meeting of the audit committee will enhance the quality of audit of any firm in Thailand.

Indonesia

Indonesia is among most important countries of this region. During recent times the Indonesia has shown a tremendous growth and is among emerging economies of the world.

The result if the study is highlighting that the board independence which is measured as the ratio of non-executive directors to total director. The result of the study are revealing some interesting facts Board independence and board size are in negative relation with audit quality which is indicating that the Indonesian firms with more directors on the board and majority of them are independent that firms suffer in audit quality Whereas the financial expertise of board members and frequency of audit committee meeting is positively related with audit quality. This shows that if a board has members with accounting and finance degrees then this will affect the audit quality. Overall the impact of corporate governance on audit quality is significant.

Table 3. Logit regression

Dependent Variable AuditQ	Malaysia			Thailand			Indonesia		
	Coef	Robust Std. Error	Z	Coef	Robust Std. Error	Z	Coef	Robust Std. Error	Z
<i>NED</i>	-0.7860	0.195	-2.75*	0.8860	0.245	2.15*	-0.5860	0.245	-1.75*
<i>FENED</i>	0.4320	0.146	1.87**	0.3240	0.146	2.07**	0.3240	0.146	0.87**
<i>ACM</i>	0.2650	0.548	1.56	0.2220	0.447	2.31	0.2220	0.447	0.31
<i>logBS</i>	-1.3250	0.543	-2.71**	-1.8750	0.648	-2.71**	-1.8750	0.648	-0.77**

Dependent Variable AuditQ	Malaysia			Thailand			Indonesia		
	Coef	Robust Std. Error	Z	Coef	Robust Std. Error	Z	Coef	Robust Std. Error	Z
<i>logSIZE</i>	1.3230	0.421	3.38***	1.1230	0.321	2.56***	1.123	0.321	4.56***
<i>PROF</i>	0.4324	0.342	1.12	0.2340	0.342	2.17	0.234	0.342	1.36
<i>LEV</i>	-0.1029	0.108	2.45*	-0.0129	0.008	1.95*	-0.029	0.008	1.72*
<i>Cons</i>	-0.7690	-0.786	-0.769	-0.7860	-0.734	-1.573	-0.786	-0.534	-0.432
No of obs	200			200			200		
<i>Prob>Chi2</i>	0.000			0.000			0.000		
Pseudo R2	0.3452			0.4321			0.5342		
Mean Vf	126			1.30			1.30		

Note: *, **, *** denote statistical significance the 0.10, 0.05 and 0.01 level respectively

Conclusion

The Asian financial crisis has brought about many significant changes in the corporate sector and capital market regulations. One of the major issues which leads ASEAN countries to Asian financial crisis is poor performance of audit mechanism. So, addressing this issue the code of corporate introduces in the start of the twentieth century and subsequent amendments have highlighted the significance of the issue of audit quality.

Audit quality assumes a vital part of keeping up an effective business sector environment, a free quality audit supports trust in the validity and honesty of financial articulations which is key for well-working markets and upgraded financial performance. External audits performed as per excellent evaluating measures can advance the use of accounting principles by reporting elements and guarantee that their financial proclamations are dependable, straightforward and helpful. This study is a comparative analysis of three ASEAN countries. The result of the study highlight that Thailand is leading in corporate governance implementation which consequently improving the quality of the audit. Whereas Malaysia and Indonesia are not as efficient as Thailand and Indonesia is at last among these countries.

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