

The Study of Correlation between type of Auditors' Report & the Quality of Accrued Interest in Companies Listed in Tehran Stock Exchange

Dariyoush Takhsha Shamsabadi¹, Soheila Khozami²

¹Department of Accounting, Omidyeh Branch, Islamic Azad University, Omidyeh, Iran

²Department of Accounting, Shoushtar Branch, Islamic Azad University, Shoushtar, Iran

Abstract: Strong capital market is the ichle of economic development and growth. The accounting earnings and its components are among the most important information which is considered by individuals when taking decision. In fact, accounting earnings which is measured and reported based on the accruals, provides more accurate evaluation from the operation of a business unit and its financial situation. Managers start out manipulating earnings in different ways, one of which is the manipulation of accruals which causes the reduction in the quality of reported earnings. Since the earnings quality is one of the important items for the users of financial reports, specially investors, to take proper decisions, and reliance on these information is relevant only to the type of auditors' comment, therefore, in this study, in order to find out the quality of earnings based on the type of auditors' comment, we study the type of relation between auditors' comment and earnings quality which is measured through abnormal accruals.

The research has been conducted in Tehran Stock Exchange in the time interval of the years 2004 to 2008. In terms of reasoning, the research is inductive-deductive and as to data collection, it is a descriptive-correlation research and is based on real information in the companies' financial statement. Also, in terms of purpose, the research is a developmental research. In this study, the members of statistical population are 125 companies in each year. The results obtained from the study shows that there is a significant relation between accruals and qualified opinion with explanatory clause regarding continued operation.

Key words: Earnings quality, accruals, agency theory, earnings management, auditing, auditor's comments, company's features

1 INTRODUCTION

Fundamental changes in Iran's economics during the past years, as well as growth and development of economic foundations, in addition to the complexity of commercial transaction, and information systems on the other hand, have made prominent the need to reliable and relevant information for taking decision in different areas more than ever before (Abbas Arbab Soleimani, 1999). Financial reports, as the most significant instrument for transmitting financial information to investors, play crucial role in economic decisions.

The accounting earnings and its components are among the most important information which is considered by individuals when taking decision. In fact, accounting earnings which is measured and reported based on the accruals, provides more accurate evaluation from the operation of a business unit and its financial situation. Due to conflict of interest among managers and investors, as well as some inherent limitations of accounting such as failure in estimation process, and the possibility of applying different accounting methods by companies, have caused managers to take the opportunities to change and manipulate earnings to their benefit. So, reliability

and usefulness of accruals is questionable. Managers start out doing earnings manipulation in different ways, one of which is the manipulation of accruals which causes the reduction of the quality of reported earnings. The users of financial statements should be aware that sometimes, earnings is managed, therefore, the reported earnings shall be different from the real earnings, and consequently the reliability of the reported earnings is questionable. Therefore, investors should take more care in their decisions and act more cautiously. However, due to information asymmetry between investors and managers, investors do not often get aware of this, which causes the increase of agency costs.

One of the ways that users could use to ensure reliability of the reported information and in this way decrease agency costs is the report of independent auditors. Since one way to manipulate earnings by management is the manipulation of accruals which causes the decrease in the quality of the reported earnings, in the present study, it has been attempted to study the relation between the type of auditors' comment and the quality of reported earnings through abnormal accruals.

2 REVIEW OF LITERATURE

So many studies have been already conducted in Iran which has examined the quality of earnings, among which we could mention: "identification and analysis of the factors relevant to the evaluation of earnings quality in Iran's economic institutions" (Dr. Zariffard, 1999), "the study and explanation of the relation between the quality of earnings and the market reac-

• Corresponding Author: Dariyoush Takhsha Shamsabadi,

E-mail: d.takhsha.s@iauo.ac.ir

• Co-Author: Soheila Khozami

E-mail: s.khozami@iauo.ac.ir

tion to dividend changes" (Dr. Saghafi & Kordestani, 2004), "an investigation into the relation between the quality of earnings and capital costs" (Majidi, 2004), "the study of the relation between earnings quality and stock return with the emphasis of the role of accruals in Tehran Stock Exchange" (Khajavi & Nazemi, 2005), "the relationship between earnings quality and stock return" (Esmaeili, 2006), "the effect of accruals quality on the companies' capital cost" (Dr. Ahmad Ahmadpour & Hosseini, summer, 2006), and "the use of qualitative features of financial information in the evaluation of earnings quality" (Dr. Ahmad Ahmadpour & Ahmadi, Jan. 2008). However, the correlation between the type of auditors' comment and the quality of accrued interest has not been studied yet.

In 1986, in a research titled "the relationship between accounting accruals and conservativeness in the auditors' report", Francis and Krishnan have obtained the following results. They know accruals as the management of subjective estimates of future results which could not, by definition, be studied actually by auditors for previous events. For this reason, companies with high accruals are audited because of so many uncertainties, and also companies with low accruals are audited due to estimates potential errors. Experimental results of a large sample of American companies indicate that auditors are very conservative, which is more probably, the reason for issuing unauthentic reports for companies with high accruals. So many analysts state that the increase of accrued earnings to their decrease is, more likely, the result of conservativeness in reporting, and only large audit institutes show evidences of conservativeness in reporting. Also, the results of the study indicate that large audit institutes are more conservative than other audit institutes (Francis & Krishnan, 1986).

In 1988, in a research, Cushing has studied the effects of changes in accounting procedures on earnings per share in 666 qualified audit reports during the years 1955-1966. Having used earnings weighted average of 4 previous periods he concluded that at the time of momentous changes that have been associated with earnings management, firms have received qualified audit report (Cushing, 1988).

In 1992, in a research titled "the effect of qualified audit reports on earnings response coefficients", Choi and Jeter have reached to the conclusion that after issuing unauthentic audit reports, the market response to the firms' earnings announcements is significantly decreased, and confirm the results of the hypothesis that the type of audit reports decrease the market response to earnings announcement by changing the market perception of earnings volatility, or stability or both. Alternatively, the decline in earnings response coefficients may be observed, because the type of audit reports in companies that have suffered substantial economic changes is more probable, and these changes rather than resulting in qualified clause in this regard, lead to the decrease of stability or increase of volatility (Choi and Jeter, 1992).

In 1997, in a research titled "evidences about auditors regarding auditors and managers' decision on the occurrence of earnings management" Nelson provides a separate analysis of the managers' decision about how management efforts have accomplished earnings and how has been the auditors' atti-

tude to these efforts. Having studied 515 cases where auditing managers have encountered earnings management, the research provides an evidence that the managers manage earnings in such a way that the transaction structure conforms to the related accounting standards (the auditors waive the mitigation of managers' efforts for earnings management) (Nelson, 1997).

In 1998, in Baker's studies, evidences have been observed that the firms which are audited by large audit institutes have less abnormal accruals than other companies. The selection of a large audit institute can also be used as a means to demonstrate better quality of financial information to external sectors, so that higher reliability of the provided data shall be perceived when they are audited by large audit institutes. However, recent accounting scandals some large audit institutes involved in, might be seriously affected by such feeling (Baker, 1998).

Francis' researches in 1999 suggest that the companies which show further tendency to use accruals, are more likely audited by large audit institutes, and those companies, audited by large audit institutes, have less discretionary accruals because of having less earnings management activities (Francis, 1999).

In 2000, in a research titled "models of discretionary accruals and audit report clauses", having studied the companies which have received unauthentic audit reports due to restriction in auditing and deviation from acceptable accounting principles, Bartov has concluded that unauthentic audit reports are a function of the absolute value of abnormal accruals (Bartov, 2000).

In 2001, in a research titled "do auditors use accrued information", having examined companies which have never had unauthentic report and the rate of whose working capital accruals has been high, Bradshaw concluded that auditors had no attention to accruals in their opinions. The existing researches indicate that companies which have high accruals shall most probably face problem in profitability; while the auditors do not care the problems resulted from high accruals. Bradshaw has examined unauthentic reports in view of information users. From the view point of information users, unauthentic reports could be interpreted as a sign of low quality of the provided financial information. However, it does not have fundamental role on auditors to issue opinion about the quality of the reported earnings (Bradshaw, 2001).

In 2002, Dechow studied the role of accruals to measure companies' operation in a time series. Since accruals require assumptions and the forecast of future cash flow, the quality of accruals and interest is decreased as the forecast error in the abnormal accruals is increased. Finally, it can be concluded that the features of each firm such the absolute value of accruals, the duration of operating cycle, sales standard deviation, cash flows of accruals, interest and the firm size, could be applied as criteria for earnings quality (Dechow, 2002).

In 2004, in a research titled "the analysis of auditing reports and its correlation with abnormal accruals", having studied a large sample of companies which have received unauthentic reports during the years 1994-1999, Butler has found that there is a positive correlation between unauthentic reports and ab-

normal accruals due to the problem of continuing operation. In his research, he found that these companies have high negative accruals, resulted from severe financial crisis. However, he failed to find evidences to support the view that the companies which receive unauthentic reports have more earnings management than the companies which receive authentic reports (Butler, 2004).

In 2006, in a research titled "the structure of board of directors and unauthentic declarations: a case study of Portugal financial markets", having studied 91 companies from the list of leasing companies during the years 2002-2003, Farina & Viana have found evidences consistent with the hypothesis that there is a negative correlation between the board of directors' independence and unauthentic declarations, while there is no statistically significant correlation between the size of board of directors and type of declaration. The results can be also applied to other differing features; it also indicates that financial health, operation, growth opportunities, and cash payments are additional effective factors in the likelihood of receiving unauthentic declarations (Farina & Viana, 2006).

In 2006, in a research, Jenkins et al have studied factors affecting the quality of earnings during the years after 1990. In order to evaluate the quality of earnings, two criteria have been used: 1) discretionary accruals, and 2) value-relevance of earnings, which will be studied through Earnings Response Coefficient (ERC).

The results of the studies conducted by Jenkins et al indicate that when the firm's discretionary accruals are high, the earnings quality is low. In this study, the years of the 1990's decade have been divided into two sections of the years 1990-96 and 1997-99.

The major findings of this study are:

- 1) Significant increase of discretionary accruals and significant decrease of ERC, shows the decrease of earnings quality during the sample period.
- 2) The decrease of earnings quality causes degrading of the auditing effectiveness.
- 3) The conduction of a high quality audit cannot completely prevent the decrease of earnings quality (Jenkins et al, 2006).

3 RESEARCH THEORETICAL FRAMEWORK & LITERATURE

Accrued interest has better advantages as compared with dividend, which help investors more to evaluate firm's operation. However, since different methods and estimates are used in calculation of accrued interest, it is possible for the management to manipulate interest through changes in methods and estimates which puts the quality of reported earnings into question. On the other hand, in order to make effective decisions investors require reliable data that due to the lack of access to information and information asymmetry, the need to audit is come up. Auditing is considered as a factor for checking the quality of the reported data.

3.1 The Quality of Accrued Interest

The directors' power of action in applying realization and matching principles and using estimates and forecasts are among factors which affect "earnings quality". Based on the realization principle, the revenue is considered as realized when the following two conditions are met:

- 1) The profit gaining process has been completed or the major part of it is completed
- 2) There is a sufficient objective evidences for measuring the amount of income

The matching principle cause correct identification and proper measurement of the profit in each period, while in case of cash, there is no such principle and the events related to money earning or exerting effort of the claimed cash in the financial statements of a period might have happened in the previous financial periods or will happen in the next financial periods. The earnings quality could be examined from three perspectives: persistence of earnings, accruals and the earning reflecting the related economic transactions (Mack Nicholas, 2002). Persistence of earnings refers to repeatability (permanence) of the current income. The high rate of persistence of earnings means that the firm has more power to maintain the current incomes, and consequently it is assumed that the firm's quality of earnings is higher (Ali Saghafi, 2004).

In a study, having examined earnings quality assessment criteria used in the previous studies, and their relation with usefulness in decision-making and economic definition of earnings, it has been shown that in addition to common criteria, earnings quality also depends on the type and amount of contracts concluded based on the accounting information (Pourheidari, Omid, 2006).

In a study, Subramanyam has found that the market attaches more value to discretionary accruals, because probably discretionary accruals increase the ability of earnings to reflect the base price (Subramanyam, 1996). Also Dechow has reported that accrual-based earning is a better criterion than cash flows for measuring the firm's operation.

Therefore, in accrual accounting system, the management has the capability to select special accounting procedures for predicted earnings report. Since managers often use abnormal accruals as a tool for manipulation of earnings which is so cases deliberate. Therefore, we accept abnormal accruals as a criterion for earnings management and apply Jones model to estimate abnormal accruals.

3.2 Earnings Management & Its Definition

It is commonly believed that managers typically make their best for income smoothing. Income smoothing, discussed as earnings management in the new accounting literature, is doing some actions for decreasing volatilities of reported accounting earnings and generally shows a steady growth of it in each fiscal period.

Earnings management is defined in different ways.

Healy and Wahlen have offered the following definition of earnings management:

"Earnings management takes place when the manager uses his personal judgment for financial reporting and does such

with the aim of misleading some stockholders about real operation of the business unit or to influence the results of contracts which are based on the accounting information (Healy and Wahlen, 1999).

Scott refers to earnings management as the firm's option in selecting accounting procedures in order to achieve some of the manager's specific goals (Scott, 1997).

Although earnings management may be defined differently, but here it bears the basic concept that earnings management eliminates the firm's actual performance. Given these definitions, earnings management in the present study is defined as purposeful activities that managers start doing it to mislead users of information to maintain their personal interests.

3.3 Incentives for Income Smoothing

Income smoothing is defined as intentional decrease of income level volatilities, so that the firm's profit seems normal. Managers smooth the income for different reasons. One of the main purposes of smoothing the income is to make a more stable flow to support higher level of payable income (Beidleman 1973). More stable earnings flow could be perceived as lower risk which is led to the increase of share price and decrease of borrowing costs. Another purpose of smoothing the income is the tendency of business managers to increase forecasting power, also encourage and persuade investors, and reduce the firm's risk (Bamea, 1975). Due to the increase of earnings stability and decrease of its fluctuations, the investors can have more accurate prediction of the future earnings.

Kellog .I. & L.B. Kellog express: 1) encouraging investors to purchase the firm's stocks and 2) increasing the firm's market value as the two major motivations of managers in earnings management (Kellog, 1991).

In 1999, Healy and Wahlen summarize the managers' motivation for practicing earnings management as follows: The managers have incentive for earnings management when the interests of their contract depend on the results of accounting information. Some of the incentives include managers' higher salaries and benefits, agreement for job security bond and loan contract. Also, the managers manage earnings to have an impact on the market.

Among other objectives of income smoothing, resulted from economic context, we could mention considerations for tax and political costs and debt contracts.

The relation between income smoothing behavior (such as change in accounting procedures, timing the sale of fixed assets, and accruals change) as well as economic consequences have been widely discussed in the financial literature. Income smoothing incentives can be linked to three variables used in the literature of economic consequences. These three variables are the firm size, taxes on income, and debt contracts. In addition to three mentioned variables derived from literature of economic consequences, the two variables of earnings variability and deviation of operating activities could be also other incentives for income smoothing (Omid Pourheidari, 2006).

3.4 Measuring Income Smoothing

Income smoothing is measured by the use of discretionary accruals mainly based on Jones model (Jones, 1991). Jones model is based on the assumption that non-discretionary accruals are constant. His model controls the effect of changes in the firm's economic situations on no-discretionary accruals.

Chi-square tests and univariate regression tests from 166 specific firms with qualified opinions and 166 peer companies with non-qualified reports have shown that all models, except D-Angelo model, are successful in determining earnings management. Specially, chi-square tests have shown that the firms with authentic comments have lower discretionary accruals than the firms with qualified reports, which indicates the fact that the firms which receive qualified reports have higher accruals. Univariate logistic regressions have also shown a significant relation between discretionary accrual and the likelihood of receiving qualified reports. Therefore, just like Dechow, Sloan, and Sweeney, the use of univariate tests which had no control over the explanation of researches differences, the aforesaid research provides an evidence which suggest that Jones model, modified Jones model, and Industry model are able to determine earnings management.

3.5 The Quality of Auditing & Earnings Management

Auditing, from the view of representation theory, is a control mechanism which provides reasonable assurance that the financial statements are free of significant errors, and so it supports stockholders' interest. When the manager's interests are in conflict with the stockholders' interests, the manager might not make any attempt to increase the stockholders' interest. In addition, management remuneration is often based on the reported earnings. Therefore, managers have enough motivation for manipulating the reported earnings to maximize their assets, and they often have the ability to do so.

If stockholders were fully informed about the managers' actions, there would be no information asymmetry between these two groups. The information asymmetry takes place when there is no complete information, which is the same hypothesis of representation theory (Fama, 1980). Due to information asymmetry, it is difficult for stockholders to find out earnings management. Auditing is a control mechanism because it helps stockholders to collect reliable information. Auditing is used to reduce information asymmetry, and the reduction in information asymmetry is a sign of high level of audit quality (Schauer, 2001). The auditors decrease information asymmetry between managers and stockholders by providing reasonable assurance that financial statements are free of significant errors (Baker's researches, 1998). The high quality of auditing must more likely lead to success in finding out and preventing earnings management. Therefore, higher levels of audit quality must be associated with lower levels of earnings management. So, the increase of auditing quality could be led to the increase of earning quality.

4 RESEARCH QUESTIONS & HYPOTHESES

Scientific research always starts with a problem; it aims to find

answer to problems using scientific methods. The most difficult step in research process is to highlight the problem under study (Hooman, 1994).

The main questions of the research are as follows:

- 1- Is there any significant relation between auditors' reporting and quality of earning (firms' abnormal accruals)?
- 2- Does the company features affect the relation between the quality of earnings (firms' abnormal accruals) and manner of auditors' reporting?

5 RESEARCH METHODOLOGY

5.1 Statistical Sample & Population

The research statistical population includes all manufacturing companies listed in Tehran Stock Exchange. The research statistical sample has been obtained by applying the following conditions:

- 1- The company's stocks have been traded in Stock Exchange during the years 2004 to 2008 (five years).
- 2- They should not have any alteration in the activity or change of fiscal year during the mentioned fiscal years.
- 3- They should not be financial institutions and banks (investment companies, financial intermediary, holding companies, banks, and leasing companies), because they pay less interest to managers than payment through accruals.
- 4- The end of fiscal year of all companies is March 20.
- 5- The company's required information is available.

On this base the statistical population of the research includes 185 companies in each year. In order to select the required statistical sample size, the following relation is applied:

$$n = \frac{N * Z_{\alpha/2}^2 * P_0(1 - P_0)}{(N - 1) * \epsilon^2 + Z_{\alpha/2}^2 * P_0(1 - P_0)}$$

To select maximum sample P_0 is considered to be 0.5, α is 0.05, and ϵ is 0.25, and measure the sample size. On this base, the members of a statistical sample include 125 companies in each year.

5.2 Research Model

To test the first hypothesis of the research, the relation between type of auditors' reporting and abnormal accruals, regression model (1) is applied:

$$Abnormal\ Accruals_{i,t} = \beta_0 + \beta_1 Mod_{i,t} + \epsilon_{i,t}$$

In equation (1), the independent variable has been considered as follows:

Mod: If the comment is qualified, rejected, or in case of no comment or an authentic one with explanatory clause, it is one, otherwise it would be zero.

Abnormal Accruals: Total accruals

In this research, Jones model of 1991 is used to calculate abnormal accruals:

$$Total\ Accruals_{i,t} = \alpha_0 + \alpha_1 \Delta Sales_{i,t} + \alpha_2 E_{i,t} + \epsilon_{i,t}$$

First, using model (2), the coefficients of the above variables for all companies are estimated in a cross-sectional manner for each year, and having put the obtained estimated coefficients in Jones model, total accruals for each company in each year is estimated, and then by comparing the real accruals with the estimated accruals, the abnormal accruals are accounted.

Total Accruals (TA): Income before extraordinary items and discontinued operations after deducting cash flow from operations divided by total beginning assets

Δ Sales: Sales oscillations from the year t1 to the year t divided by the total beginning assets

PPE: Net property, plants and equipment in the year t divided by the total beginning assets

The independent variables of equation (2) are: Sales oscillations (ΔS), net property, plants and equipment (PPE), and the dependant variable is the total accruals. Dividing variables by beginning assets is done to standardize variables.

Also, in order to investigate the effect of a special type of auditing comments on the abnormal accruals, the following regression is used:

$$MABTAC_{i,t} = \beta_0 + \beta_1 Magb_{i,t} + \beta_2 Magt_{i,t} + \beta_3 Mash_{i,t} + \beta_4 Mast_{i,t} + \beta_5 Adam_{i,t} + \epsilon_{i,t}$$

In regression (3), Mod comments are divided into the following categories; that is the effect of a type of report on the dependant variable is processed and the significance of the relation is analyzed in compound for companies in five years.

Magb: If the authentic comment with an explanatory clause is related to a problem which has no significant effect on financial statements, it is one, and otherwise it is zero.

Magt: If the authentic comment with an explanatory clause is related to the problem of discontinued operation, bankruptcy, or cases of uncertainty, it is one, and otherwise it is zero.

Mash: If the qualified opinion is due to limitation in confines of auditing or deviation from principles, it is one, otherwise it would be zero.

Mast: If the qualified opinion is due to limitation in the confines of auditing or deviation from principles together with a clause stating the problem of discontinued operation, bankruptcy or cases of uncertainty, it is one, otherwise it would be zero.

Adam: : If the comment is due to fundamental limitation in the confines of auditing or deviation from principles together with a clause stating the problem of discontinued operation, bankruptcy or cases of uncertainty, it is one, otherwise it would be zero.

Also, to test the second hypothesis of the research, i.e. the relation between company features on the quality of earnings and

type of auditors' reporting, regression (4) is applied:

$$\begin{aligned} |Abnormal\ Accruals|_{i,t} = & \beta_0 + \beta_1 MktCap_{i,t} + \beta_2 Book / Mkt_{i,t} + \beta_3 ROA_{i,t-1} + \\ & \beta_4 ROA_{i,t} - 12 + \beta_5 Debt / Assets_{i,t} + \beta_6 CurrRatio_{i,t} + \\ & \beta_7 Assets_{i,t} + \beta_8 AuditFirm_{i,t} + \beta_9 Mod_{i,t} + \varepsilon_{i,t} \end{aligned}$$

In regression (4), the confounding variables (such as: equity market value, book to market value, return on assets, leverage ratios, and type of company's auditor) were examined to study the effect of company features on the relation between auditors' reporting and abnormal accruals.

MktCap: Logarithm of equity market value

Book/Mkt: Equity book value divided by its market value

ROA: Income before extraordinary items divided by total beginning assets

ROA2: ROA square

Debt/Assets: Long-term liabilities divided by the total beginning assets

CurrRatio: Current assets divided by current liabilities

Audit Firm: If an auditing institute is the company's auditor, it is one, otherwise it would be zero.

Also, to study the effect of company features on the type of auditors' reporting and quality of earnings (abnormal accruals), regression (5) is applied:

$$\begin{aligned} |Abnormal\ Accruals|_{i,t} = & \beta_0 + \beta_1 MktCap_{i,t} + \beta_2 Book / Mkt_{i,t} + \beta_3 ROA_{i,t-1} + \\ & \beta_4 ROA_{i,t} - 12 + \beta_5 Debt / Assets_{i,t} + \beta_6 CurrRatio_{i,t} + \beta_7 AuditFirm_{i,t} + \\ & \beta_8 Magb_{i,t} + \beta_9 Magt_{i,t} + \beta_{10} Mash_{i,t} + \beta_{11} Mast_{i,t} + \beta_{12} Adami_{i,t} + \varepsilon_{i,t} \end{aligned}$$

6 RESEARCH RESULTS

6.1 Descriptive Statistics

Differing comments of 625 companies under study during the years 2004 to 2008 in the chart 1.

- **Chart No.1**

They have been separated, categorized and their percent has been given based on the size of auditing institute. In this study, auditing organization has been considered as the largest auditing institutes and other institutes have been put in another category.

In chart No.2, we have studied the average and mean of variables in the observations made based on the type of comments.

- **Chart No.2**

Based on the results of the chart No.2, it is observed that the average of abnormal accruals is higher in companies which receive qualified reports with explanatory clause regarding the continued operation and non-comment reports than other companies. Also, the negative point indicates that these companies have higher negative accruals. These companies have lower market to book value which is due to overmuch loss of these companies; they are not that good in the market, so prices are lower than the book value. Other variables of these companies are also lower than other companies.

6.2 Testing Research Hypotheses

The research preliminary hypothesis investigates any correlation between the quality of reported earnings (abnormal accruals) and auditors' comment in the companies listed in Tehran Stock Exchange, and to test the case, null and alternate hypotheses have been defined as follows:

H₀₁: There is no significant relation between the quality of reported earnings (abnormal accruals) and the auditors' comment in the companies listed in Tehran Stock Exchange.

H₀₁: $\beta = 0$

H₁₁: There is a significant relation between the quality of reported earnings (abnormal accruals) and the auditors' comment in the companies listed in Tehran Stock Exchange.

H₁₁: $\beta \neq 0$

Where Bi is the independent variables coefficients of multivariable regression

As it is observed in the chart No.3, using OLS model, determination coefficient of regression (R²) is -0.0013 which indicates a very weak explanation of the dependant variable (abnormal accruals) by independent variable (auditors' unauthentic comment). This could be due to significant differences in the size of companies under study, and also the industries related to these companies, which have caused inconsistency in regression residuals variance. Also, the figure 1.505 of Durbin-Watson statistic shows lack of correlation between residuals

- **Chart No.3**

Statistical validity of the total regression is assessed by F coefficient, and as it is observed in chart No.3, F coefficient indicates the figure 0.211 that based on the significance number (Prob.) of this variable, which shows the relation 0.646 > 0.05, the total regression does not have the required statistical validity.

In order to examine the effect of a special type of comments on earnings quality, the unauthentic reports are divided into five groups (authentic reports with explanatory clause (MAGHB), authentic reports with explanatory clause and continued operation (MAGHT), qualified reports (MASH), qualified reports with explanatory clause regarding continued operation (MAST), non-comment reports (ADAM), and then we study again the results of regression.

As it is observed in the chart (4), using OLS model, determination coefficient of regression (R²) shows the figure 0.0204 which indicates that 2.04% of the changes in abnormal accruals are explained by this factor.

Statistical validity of the total regression is measured by F coefficient. As it is seen in chart (4), F coefficient indicates the figure 3.608, and given the significant number (Prob.) of this variable which shows the relation 0.003 < 0.05, the total regression has the required statistical validity.

- **Chart No.4**

In the next step, the effect of each independent variable on the dependent variable is measured by abnormal accruals. The t-coefficient and significant number (Prob.) of individual variables indicate that the independent variable, qualified opinion

with an explanatory clause regarding continued operation and C constant factor have the required statistical validity, because significant number of this variable is smaller than the significant level of 0.05. Therefore, H01 hypothesis is rejected, and consequently H11 hypothesis is approved.

As to Durbin-Watson number (1.547), it should be stated that the value of this index indicates lack of autocorrelation between variables.

Testing Second Hypothesis:

The second hypothesis examined the effect of company features on the type and quantity of relation between auditors' reporting and abnormal accruals. To test this case, the null and alternate hypotheses have been defined as follows:

H02: Company features do not have any significant effect on the relation between the quality of reported earnings (abnormal accruals) and the auditors' comment in the companies listed in Tehran Stock Exchange.

$$H_{.2} : \beta = 0$$

H12: Company features have significant effect on the relation between the quality of reported earnings (abnormal accruals) and the auditors' comment in the companies listed in Tehran Stock Exchange.

$$H_{12} : \beta \neq 0$$

where Bi is the independent variables coefficients of the multivariable regression.

As it is observed in the chart (5), even when the company features are added, there is still no significant relation between unauthentic comments and abnormal accruals. Given P-Value of F test, (0.000) the following regression has statistical validity.

• Chart No.5

In order to study the correlation between abnormal accruals and a special type of unauthentic comments, the unauthentic reports are divided into five groups: authentic reports with explanatory clause (MAGB), authentic reports with explanatory clause regarding continued operation (MAGT), qualified reports (MASH), qualified reports with explanatory clause regarding continued operation (MAST), and non-comment reports (ADAM), and then we review the results of regression.

• Chart No.6

Chart No.6 shows the results of regression to test the second hypothesis. As it is observed, when the company feature variables are added, based on P-value of F test, the following regression shall have statistical validity, it is also observed that with 95% level of confidence, there is a significant relation between qualified opinions with explanatory clause regarding continued operation and abnormal accruals which indicates the fact that company features do not have any influence on the correlation between type of accruals and type of comments, and just the correlation rate (0.0816) has been made a

little stronger.

Given Durbin-Watson value of 2.1325, there is also the problem of autocorrelation between variables. Also, based on P0value of t test, there is a significant relation between book to market value, ROA, ROA2, and the ratio of long-term liabilities to assets with abnormal accruals.

5 CONCLUSIONS

The obtained results indicate that there is a significant relation between accruals and qualified opinion with explanatory clause regarding continued operation.

The findings spell that the companies which receive qualified reports with explanatory clause regarding continued operation, have higher negative accruals, which indicate the low quality of the reported earnings. The results of the study suggest that investors should also pay special attention to the type of auditors' comment when taking useful decisions, and when the auditors' comment is as qualified with explanatory clause regarding the continued operation, the possibility of earning manipulation through accruals is higher in these companies, and consequently the earnings quality in such companies is lower, therefore, the reported earnings for taking useful decisions is not reliable.

Also, company features do not have any influence on the type of relation and it just further correlation between variables. The results of the study are consistent with the results of Butler's research in 2004. The sample of the study is 7093 American companies during the years 1994-1999. He has also observed a significant relation between abnormal accruals and comments in which continued operation clause has been set forth. It is to be mentioned that R2 correlation coefficient has been also low (8.2%) in his research which shows weakness of correlation between variables.

Another finding of the research is that companies which receive qualified reports with explanatory clause regarding continued operation, have higher negative abnormal accruals than other companies.

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TABLE NO. 1							
		Authentic	Authentic with explanatory clause	Authentic with explanatory a Continued operation	Qualified	Qualified with explanatory clause Continued operation	Non-comment
Total accruals	Average	0.074	0.057	(0.087)	0.056	(0.096)	(0.088)
	Mean	0.063	0.049	0.087	0.042	(0.099)	(0.149)
Abnormal Accruals	Average	0.037	0.034	(0.067)	0.022	(0.102)	(0.098)
	Mean	0.023	0.054	0.067	0.015	(0.092)	(0.148)
Market value logarithm	Average	5.481	5.425	4.937	5.28	4.628	4.459
	Mean	5.479	5.398	4.937	5.194	4.778	4.534
Market to book value	Average	0.425	0.617	0.522	0.592	(1.909)	(1.948)
	Mean	0.29	0.465	0.522	0.439	(0.67)	(1.893)
ROA	Average	0.981	0.926	0.771	1.037	0.7	0.666
	Mean	1.002	0.901	0.771	0.949	0.635	0.644
ROA2	Average	1.118	1.012	0.623	1.602	0.585	0.505
	Mean	1.005	0.811	0.623	0.898	0.403	0.42
Liabilities to Assets	Average	0.129	0.144	0.088	1.429	0.187	0.165
	Mean	0.071	0.062	0.088	0.075	0.135	0.159
Current Ratio	Average	1.242	1.125	0.917	1.152	0.651	0.591
	Mean	1.111	1.095	0.917	1.074	0.62	0.621
Assets	Average	689.220	2.356.838	307.000	1.131.222	164.751	154.382
	Mean	263.735	358.831	307.000	246.915	121.246	152.518
Type of auditing institute	Average	0.465	0.476	0.5	0.3	0.21	0.5

TABLE NO. 2			
Explanatory variable	Coefficient	T-Statistics	P-Value
Constant Factor	0.126041	10.24946	0
Unauthentic comment	(0.006171)	(0.459576)	0.6461
F-Statistics	0.211118		0.646053
Durbin-Watson Statistics			1.505683
Adjusted (correlation coefficient) R2			(0.001266)

TABLE NO. 3			
Explanatory variable	Coefficients	T statistics	P-Value
Constant Factor	0.126041	10.36259	0
Authentic with explanatory clause	(0.018842)	(0.839529)	0.4015
Authentic with explanatory clause & continued operation	(0.026618)	(0.304951)	0.7605
Qualified	(0.014149)	(1.041975)	0.2978
Qualified with explanatory	0.044416	2.295682	0.0220

TABLE NO. 4

<i>Explanatory variable</i>	Coefficients	T statistics	P-Value
<i>Constant Factor</i>	0.159716	3.422462	0.0007
<i>Market value logarithm</i>	(0.010562)	(1.329148)	0.1843
<i>Book to market value</i>	(0.013205)	(4.111393)	0.0000
<i>ROA</i>	0.031302	1.828605	0.0679
<i>ROA2</i>	0.001899	0.539607	0.5897
<i>Long-liabilities to fixed assets</i>	0.028726	0.747824	0.4549
<i>Current Ratio</i>	(0.006743)	(0.871472)	0.3838
<i>Assets</i>	-10E5.54	0.478001	0.6328
<i>Auditing Institute</i>	0.002752	0.255669	0.7983
<i>Unauthentic comment</i>	(0.011550)	(0.858810)	0.3908
<i>F-statistics</i>	4.656840	---	0.0000
<i>Durbin-Watson statistics</i>	---	---	1.567073
<i>Adjusted (correlation coefficient) R2</i>	---	---	0.050100

TABLE NO. 5

<i>Explanatory variable</i>	Coefficients	T statistics	P-Value
<i>Constant Factor</i>	(0.09229)	(1.34236)	0.18
<i>Market value logarithm</i>	0.013728	1.205108	0.2286
<i>Book to market value</i>	0.012378	2.483055	0.0133
<i>ROA</i>	0.049448	2.054312	0.0404
<i>ROA2</i>	(0.01559)	(3.19486)	0.0015
<i>Long-liabilities to fixed assets</i>	(0.10639)	(2.00982)	0.0449
<i>Current Ratio</i>	0.020222	1.87683	0.061
<i>Assets</i>	4.68E-10	0.293506	0.7692
<i>Auditing Institute</i>	0.012931	0.870153	0.3846
<i>Authentic with explanatory clause</i>	(0.00076)	(0.02474)	0.9803
<i>Authentic with explanatory clause regarding continued operation</i>	(0.09334)	(0.78876)	0.4306
<i>Qualified</i>	(0.01078)	(0.57421)	0.566
<i>Qualified with explanatory clause regarding continued operation</i>	(0.07096)	(2.26182)	0.0241
<i>No comment</i>	(0.06867)	(0.79453)	0.4272
<i>F-statistics</i>	5.270388	---	0.0000
<i>Durbin-Watson statistics</i>	---	---	2.132512
<i>Adjusted (correlation coefficient) R2</i>	---	---	0.081698