# Timeliness of Audited Financial Reports of Malaysian Listed Companies

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## Abstract

*This study examines the determinants of audit delay among Malaysian public listed companies before the Code of Corporate Governance was revised. Specifically, the study examines the relationship between audit delay and audit opinion as well as the characteristics of audit committee independence, the frequency of meetings held during the financial year and the financial literacy of audit committee members. Based on 636 annual reports of companies listed on the Main board of Bursa Malaysia the study finds that only 2.3% of companies experienced delays and audit delay is associated with the type of audit opinion other than an unqualified one. Types of external auditor and change in auditor are also seemingly not significant factors influencing audit delay. The difference in characteristics of audit committee between companies with audit delay and companies without audit delay is not significant suggesting therefore that in form, listed companies have similar audit committee characteristics.*

**Key words**: timeliness, audit delays, reporting lags, financial distress, qualified audit reports

## *1. Introduction*

An important qualitative characteristic of financial reports identified by Imam, Ahmed and Khan (2001) is the timeliness of financial statements. This criterion is especially important for public listed companies as investors need timely and reliable information to make correct decisions for their investments in the stock markets. Malaysian Accounting Standard Board (MASB) emphasizes that the usefulness of financial statements is impaired if they are not available to users within a reasonable period after the balance sheet date. Abdulla (1996) suggested that the shorter the time between the end of the accounting year and the publication date of the year's financial statements, the greater the benefits that can be derived from the financial statements. According to *The Starbiz* (August2, 2012)Industry experts also agreed that failure of listed companies to release their audited reports on time is unacceptable for whatever the reasons. Timely publication of financial information of a company depends very much on the time taken to complete the audit because the financial statements cannot be issued until the audit has been concluded. Givoly and Palmon (1982, pg.491) contended that the 'single most important determinant of the timeliness of the earnings announcement is the length of the audit'. It cannot be denied that a time gap always exists between the end of the financial accounting period and the time when the audited information is made available to the public (Ponte, Rodriguez and Dominguez, 2008) yet minimizing the gap would enhance market efficiency. Audit delay is defined by Almosa and Alabbas, (2007) as the length of time from a company's fiscal year end to the date of the auditor report. Bursa Malaysia has proposed that the time line for releasing audited financial statements be reduced from four to two months in line with reductions introduced by other stock exchanges. If the time frame is reduced can Malaysian companies meet the new requirement? It is the objective of this paper to examine the extent and of audit delays and factors associated with such delays among Malaysian listed companies.

## *2. Literature Review*

### 2.1. Factors affecting delays

Several studies have been conducted to explore an understanding of the determinants of audit delay. Studies in various countries show differences in respect of periods, methodology, variables introduced and conclusions obtained (Ponte, Rodriguez and Dominguez, 2008). In Spain, Ponte *et al.* (2008) found that there is a negative relationship between audit delay and the company size (measured by total assets) as well as the industry sector a company is operating in. Small companies are less visible in the market hence the audit delay is found to be shorter for larger companies rather than smaller companies. Companies in a highly regulated sector appear to experience less delay compared to those in less regulated sectors. However, as stated by Oliver (1991), organizations do not always conform and comply with the institutional pressures and, for this reason, delays occur. Carslaw and Kaplan (1991) extended prior research of audit delays in New Zealand capturing both auditor and corporate attributes in their model. The study found that only company size and losses are statistically significant for both 1987 and 1988. However, Almosa and Alabbas (2007) in Saudi Arabia showed a different result whereby size is found to be positively related to audit delay and company's profitability and auditee sector are found to be inversely related to audit delay. The results showed that financial sector has a shorter audit delay. This is consistent with some existing studies which stated that highly-regulated industry like financial and energy sectors are more likely to have a shorter delay (Ponte *et. al*, 2008). Haw, Qi and Wu (2000) examined the relationship between firm performance and the timing of annual report releases in China. Their study found that good news firms tend to release their annual reports earlier than bad news firms, and loss firms release their annual reports the latest. Moreover, consistent with Chambers and Penman (1984) and Begley and Fischer (1998), firms unexpectedly accelerate the release of good news and delay the disclosure of bad news.

### 2.2. Auditor factor

Leventis *et. al* (2005) reported that type of auditor, audit fees, the number of remarks in the audit report, the presence of extraordinary items and the expression of uncertainty in the audit report are all statistically significant factors in affecting timely reporting. Companies which choose the external auditor from internationally affiliated firms, or pay a premium audit fee have shorter audit report lag. Large multinational and more reputable auditing firms might take less time to conduct assurance services for several reasons. These companies may have more resources (Palmrose, 1986) and higher quality staff (Chan, Ezzamel and Gwilliam, 1993). Moreover, Francis and Wilson (1988) suggested that audit firms invest in their brand name reputation in order to command fee levels for higher quality assurance. Audit firms would then have an incentive to provide a higher quality audit in order to protect their brand name and future revenues. Auditees may be willing to pay a higher fee for the promptness of the assurance service which has been related in the literature to perceived audit quality (Carcello, Hermanson and McGrath,1992). On the other hand, companies that report extraordinary items in their income statement or have a large number of remarks, or an uncertainty qualification in their audit report have a longer audit report lag. All these reflect potentially bad news in the eyes of the users of the annual report. The result is consistent with Haw *et. al* (2000) which stated that bad news companies tend to release their annual reports later. As for the control variables like nature of ownership, profitability, gearing, number of subsidiaries, industry type, reliance on another auditor for an opinion, and a change of auditor from the previous year, no significant association have been found with audit delay. In Malaysia Raja Adzrin and Khairul Anuar (2003) found that audit delay in public listed companies from year 1996 to year 2000, is significantly longer for companies classified as non-financial industry, receiving other than unqualified audit opinions, incurring losses and having higher risk. This study also found that companies with the accounting year end other than 31 December and are being audited by small and medium size audit firms require longer period to audit. Based on literature therefore, audit delay is associated with several factors relating to the company itself, the auditors, or external factors.

## *3. Methodology*

### 3.1. Data

Data for this study is based on the 2006-2007 annual reports of Main Board companies. The annual reports are obtained from Bursa Malaysia website.

This period is chosen because of two factors; the revision in the Code of Corporate Governance in relation to the composition of audit committee members beginning 2006 which could result in more effective monitoring for timely submission of annual accounts and the adoption of International Financial Reporting Standards (IFRS) in Malaysia effective January 1, 2006 which could affect the timeliness in submission of annual reports too due to the complexity in the reporting requirements of IFRS. Ruzaidah and Takiah (2004) have shown that the quality of corporate annual reports is significantly related to certain characteristics of audit committee and timeliness is one of the important measures of quality in annual reports. The companies on main board are chosen for this study because public reprimands on audit delay are found to be more compared to companies from other boards and the most common violation of the Listing Requirements which merit a public reprimand by Bursa Malaysia is regarding timeliness in submission of annual reports (Ahmed Razman and Hashanah, 2003).

### 3.2. Measurements of audit delay

Audit delay is measured as the number of days from the date of financial year end to the date of auditor report. Paragraph 9.23 (b) of the Bursa Securities Listing Requirements requires that the audited financial statements to be submitted within a period not exceeding four months from the financial year end. The independent variables, type of audit opinion issued, is quantified by two categories which is either it is an unqualified audit opinion or other than unqualified audit opinion. Types of audit opinion other than an unqualified one can be an unqualified opinion with emphasis of matter, qualified opinion, adverse opinion or a disclaimer. The characteristics of audit committee (AC), is measured by the independence of the board, frequency of meetings held and qualification of AC members. The study utilizes descriptive statistics to analyse data in relation to audit delay and the type of audit opinion as well as the characteristics of audit committee. Companies with audit delay are matched or paired to companies without audit delay. Four propositions are to be tested for association with audit delays: types of audit opinion, audit committee independence, regularity of meetings and financial literacy of its members.

## *4. Findings and Discussions*

**Table 1: Analysis of Annual Reports for Main Board Companies**

| Annual Reports | 2006 | 2007 | Total |
|---|---|---|---|
| Companies with audit delay | 9 | 6 | 15 |
| Companies without audit delay | 557 | 597 | 1,154 |
| Annual reports unavailable | 68 | 30 | 98 |
| Companies with undated audit report | 2 | 3 | 5 |
| Grand total | 636 | 636 | 1,272 |

From Table 1 only 2.3% of the audit reports examined experienced delays with slightly more in 2006 compared to 2007 with one company having repeated audit delay in both years respectively. This rate is lower than previously reported by Hashanah and Razman (2003) in an earlier time period. The rest of the companies are all first-time delays. Since the number of companies with audit delay is too small for statistical test, only descriptive analysis will be performed.

**Table 2: Types of Audit Opinion Associated with Audit delay**

| Audit Opinion | Year 2006 | | Year 2007 | | Total | |
|---|---|---|---|---|---|---|
| | Frequency | % | Frequency | % | Frequency | % |
| Unqualified | 2 | 22 | 3 | 50 | 5 | 33 |
| EOM | 6 | 67 | 2 | 33 | 8 | 53 |
| Disclaimer | 1 | 11 | 1 | 17 | 2 | 14 |
| Grand total | 9 | 100 | 6 | 100 | 15 | 100 |

Out of the 15 companies with audit delay, only one third received an unqualified opinion, with slightly more than half receiving an Emphasis of Matter (EOM) report indicating that most audit delays are related to companies in financial distress. For year 2007, there is an even distribution of companies between unqualified audit opinions and 'others'. According to Haw *et. al* (2000), good news firms tend to release their annual reports earlier than bad news firms, and loss firms release their annual reports the latest. Subsequently, audit opinion other than an unqualified one which is associated mostly with audit delay usually conveys a signal of problems or bad news.

It implies that something unusual or serious has happened and more time is needed to extend audit work in order to resolve the problem. From the range of distribution of the companies, it appears that audit opinion is associated with audit delay and this is consistent with the findings of previous studies, being one of them stated that qualified audit opinions are released later than unqualified opinions (Soltani, 2002). In this study, audit delay seems to be associated mostly with audit opinion other than an unqualified one.

Among the companies that receive an emphasis of matter opinion, the issue is regarding net loss in the company that causes default in loan obligation when they fall due which subsequently cast doubt about the going concern status of the company. Such companies depend on the successful outcome of restructuring plans which at the date of audit report, the result is not yet known for example quoting an excerpt from one audit report: "We draw attention to Note 2 to the Financial Statements. The Group incurred losses of RM126.3 million and RM369.6 million (as restated) for the financial years ended 31 December 2006 and 2005. The Company also incurred losses of RM192.6 million and RM381.9 million (as restated) for the financial years ended 31 December 2006 and 2005. The financial statements of the Group and the Company have continued to be prepared on the basis of accounting principles applicable to a going-concern. This going-concern basis presumes that the Group and the Company will be able to operate and generate sufficient cash flows in the foreseeable future and financial support from their lenders will continue to enable the Group and the Company to meet their obligations as and when they fall due and, accordingly, the realization of their assets and settlement of their liabilities will occur in the ordinary course of business".

One of the consequences of having doubt in going concern is to cause the company to be put under the list of PN 17 (Practice Note 17) companies for further monitoring. In Paragraph 2.1 (e) of Practice Note 17 issued by Bursa Malaysia, it has outlined one of the criterion about going concern that may cause a firm to be put under the list of PN 17 companies is whereby "the auditors have expressed a modified opinion with emphasis on the listed issuer's going concern in the listed issuer's latest audited accounts and the shareholders' equity of the listed issuer on a consolidated basis is equal to or less than 50% of the issued and paid-up capital of the listed issuer". The main reason why companies received an audit report which departs from an unqualified report is uncertainty as to its going concern status. Paragraph 26 of the International Standard on Auditing, ISA 570 has outlined further audit procedures to be performed when uncertainties of going concern have arisen. It is the auditor's responsibility to extend audit work in order to dispel or confirm going concern uncertainties. However, such an extension would inevitably mean more time involved in the finalization of accounts and therefore, extended audit time may affect the timeliness of information released through annual report (Hashanah, 1998).

Besides the issue of going concern, material litigation is another reason of the examined companies getting an emphasis of matter audit opinion. Furthermore, emphasis of matter is also used when the auditors want to draw extra attention to some issues which they think is necessary.

The main cause for disclaimers is doubt about going concern with no adjustments in the basis of preparation of the financial statements. Other reasons are involvement in material litigation, failure in preparing subsequent management accounts and failure of auditors to obtain sufficient evidence on some matters. All these have caused the auditors to disclaim an opinion. An example of disclaimer: "Because of the significance of the matters as discussed in the Basis for Disclaimer of Opinion section, we do not express an opinion on the financial statements."

**Table 3: Mean Delay and Types of Audit Opinion**

| Audit Opinion | Mean Delay (Days) | | |
|---|---|---|---|
| | Year 2006 | Year 2007 | Total |
| Unqualified | 6 | 46 | 30 |
| Others | 72 | 140 | 80 |

From Table 3 the mean delay in days is calculated by summing up the days of delay then divided by the number of companies in certain category. It is seen that mean delay for companies receiving an unqualified audit opinion is shorter as compared to companies with audit opinion other than an unqualified audit opinion. The data appears to be consistent with findings from some previous studies which stated that the more serious the qualification, the greater the delay (Soltani, 2002) and companies with uncertainty qualification in their audit report have a longer audit report lag (Leventis *et. al*, 2005).

Mean delay in year 2007 is relatively longer because the days of delay is longer for some companies. The range of delay in year 2007 is from 3 days to 216 days while in year 2006 is only from 3 days to 90 days.

**Table 4: Audit committee characteristics**

| Analysis | 2006 (N=9) | | | | 2007 (N=6) | | | |
|---|---|---|---|---|---|---|---|---|
| | Companies with audit delay | | Companies without audit delay | | Companies with audit delay | | Companies without audit delay | |
| | Frequency | % | Frequency | % | Frequency | % | Frequency | % |
| ***Audit opinion*** | | | | | | | | |
| Unqualified | 2 | 22 | 8 | 89 | 3 | 50 | 5 | 83 |
| Others | 7 | 78 | 1 | 11 | 3 | 50 | 1 | 17 |
| | 9 | 100 | 9 | 100 | 6 | 100 | 6 | 100 |
| | Average | | Average | | Average | | Average | |
| ***Audit Committee*** | | | | | | | | |
| Independent directors | 2.44 | | 2.56 | | 2.67 | | 2.17 | |
| Meetings held | 5.89 | | 5.11 | | 5.17 | | 4.83 | |
| Qualified directors | 1.89 | | 1.89 | | 2.5 | | 2 | |

Table 4 indicates number of independent directors, number of audit committee meetings held during the financial year and number of qualified directors sitting on the board. There appears to be no significant difference between the companies with audit delay and companies without audit delay in terms of their characteristics of audit committee. This is perhaps the efforts of companies in complying with the Code of Corporate Governance, especially after its revision which could have caused all audit committees to look the same.

On the other hand, the number of independent and qualified directors has increased in year 2007. The increment is perhaps due to that public listed companies are working hard to comply after the revision of the Code. However, regardless of the revised Malaysian Code dated 1 October 2007 whereby the board should establish an audit committee comprising at least three members, a majority of whom are independent and all members of the audit committee should be non-executive directors, no 100% compliance is achieved. There are still companies with executive/non-independent directors sitting on the audit committee. This is perhaps it is not easy to comply due to difficulty in getting the right persons to be appointed.

## *5. Conclusion*

This paper examines the extent and nature of audit delays among Malaysian Main listed companies. The study reports that only 2% of Main companies showed delays in the period 2006-2007. Consistent with findings in some of the previous studies, audit delay appears to be associated with the types of audit opinion issued with the length of audit delay being longer for other than unqualified opinions. Characteristics of audit committee between companies with audit delay and companies without audit delay do not appear to be very different. Though there is enhanced compliance in the code of corporate governance especially after its revision, it is undeniable that compliance merely in form and structure is somehow easier than in substance. Whether the enhanced compliance has caused the audit committee to function more effectively in reducing audit delay or not is still unknown. Therefore, future research of audit delay may consider other measures of audit committee effectiveness rather than the three measures used in this study (independence, frequency of meetings and qualification) because compliance in form has caused the companies to look almost the same in their audit committee structure. That the delay is only 2.3% and reduced from the rate reported for periods 1998 -2002 does suggest that it is possible to reduce the submission time frame and deliver financial reports in a timelier manner.

Future study can utilize interviews with audit committee members to help gain more in-depth understanding about the effectiveness of the audit committee in meeting timely date of submission. The consideration of how supportive is the management towards audit committee in supplying relevant and reliable information could perhaps be an area of study to find out its association with audit delay.

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