

Research on Corporate Governance Structure and Audit Opinions

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Abstract-This paper analyzed the influence that the corporate governance is having on the audit opinions. Through a comprehensive analysis of the structure of the board of directors, board of supervisors, shareholder structure and management structure of the four dimensions, we analyzed the relationship between the two which is investigated, and then we constructed the corporate governance index, to analyze its impact on audit opinions. Based on the comparative study, we used the regression model and found that the board of directors, board of supervisors' structure, the board of shareholder and management structure did affect the types of audit opinions. Moreover, the corporate governance index reflected the quality of corporate governance, which was one of the important factors to influence the type of audit opinion. Companies with better corporate governance are more likely to be issued standard unqualified audit opinion types.

Keywords-corporate governance index, audit opinions, board of directors, board of supervisors

I. INTRODUCTION

CPA is the economic policeman in the capital market. On December 23, 2016, China's CPA Auditing Standards No. 1501-Forming audit opinions and issuing audit reports on financial statements, it proposed that CPAs should form audit opinions on whether financial statements are prepared and fairly reflected in all major aspects in accordance with the applicable provisions of the basis for preparing financial reports. It is necessary to consider whether the whole financial statements are prepared or not. In the absence of material misstatement due to fraud or error, CPAs should conclude whether reasonable assurance has been obtained in this regard. Corporate governance, as an institutional arrangement for controlling and managing companies, has a direct impact on the healthy development of listed companies and securities markets. The improvement of corporate governance is related to the quality of accounting information of listed companies. True and reliable accounting information is one of the preconditions for certified public accountants to issue standard audit opinions on listed companies. Certified public accountants will pay attention to the quality of accounting information when they give audit opinions on the financial statements of listed companies. In theory, perfect and reasonable corporate governance represents a higher level of management and a lower audit risk. Therefore, CPAs often issue standard and unreserved audit opinions after auditing listed companies

with better corporate governance. It can be seen that there is a great correlation between the perfection of corporate governance and audit opinions.

II. LITERATURE REVIEW

As early as 1980, Fama studied the relationship between corporate governance and audit opinions and found that the quality of corporate governance is related to the efficiency of the board of directors. The more reasonable the governance structure, the higher the probability of receiving standard audit opinions [1]. LA. PORTA (1997) found that if a company's ownership is concentrated in the hands of several people, the easier it is to obtain non-standard audit opinions [2]. Carcello and Neal (2000) believed that the situation of the audit committee had a significant impact on the audit opinions received by the company. The establishment of the audit committee was conducive to the company receiving standard audit opinions [3].

Liu Liguang and Du Ying (2002) argue that the higher the proportion of circulating shares, the less likely the company will have financial report fraud, while the higher the proportion of legal person shares, the higher the possibility of financial report fraud [4]. Xu Xiaonian (1999), Liu Guoliang and Zhang Hongjun (2000) argued that the higher the proportion of state-owned shares, the worse the performance of the company and the receipt of standard audit opinions. Research by Zhang Junrui and Dong Nanyan (2006) shows that the higher the overall level of corporate governance, the easier it receives standard audit opinions. Liang Shuxiang (2007) believes that the higher the proportion of the first largest shareholder holding shares, the lower the probability of receiving standard audit opinions [5]. Wang Zhen and Peng Jingfang (2007) believe that the proportion of circulating shares is positively correlated with the standard audit opinions received, which is consistent with the research results of other scholars [6].

Empirical studies at home and abroad agree that, the more perfect the corporate governance structure, the more likely it is to receive standard audit opinions. The lower the level of corporate governance structure, the less likely the company will receive standard audit.

III. PRESENTATION OF RESEARCH HYPOTHESIS

On the basis of the above analysis, we will analyze the whole internal corporate governance system from four dimensions: board of directors, board of supervisors, shareholders and management, as well as a comprehensive corporate governance index.

The board of directors is an important part of corporate governance and plays an important role in the whole internal corporate governance. Fama and Jensen (1983) believe that the board of directors is the lowest-cost internal resource for supervising managers, and that shareholders' internal control responsibility is delegated to the board of directors to give the board the highest decision-making control in large or small companies [7]. The board of directors is the core of the dual principal-agent relationship and the hub of corporate governance. We believe that the governance efficiency of the board of directors affects the quality of accounting information of the company, thus affecting the types of audit opinions issued by CPAs. Therefore, this paper proposes hypothesis 1:

H1: The efficiency of board governance is positively correlated with the standard unqualified audit opinions.

The board of supervisors has the function of internal monitoring, which should supervise the use of the functions and powers of the board of directors or managers. The board of supervisors can promote the perfection of the internal supervision mechanism of enterprises, make the accounting statements of enterprises reflect the actual situation of enterprises more truthfully, and it is easier to issue standard audit opinions. To a certain extent, the board of supervisors can play a supervisory role, thus improving corporate governance, while affecting the type of audit opinions. Therefore, this paper proposes hypothesis 2:

H2: The governance efficiency of the board of supervisors is positively related to the standard unqualified audit opinions.

Shareholder structure is an important part of corporate governance structure, which determines the distribution of corporate control rights, the nature of principal-agent relationship between shareholders and managers, the corresponding control rights, supervisory rights and earnings rights of shareholders, and the structure of board of directors, thus affecting the way and efficiency of corporate governance. Chan Ezzamel, Gwilliam (2010) argues that ownership structure affects the intensity of audit process, and then affects the quality and opinion of audit [8]. Therefore, the following assumptions are proposed:

H3: The efficiency of shareholder structure governance is positively correlated with the standard unqualified audit opinions.

According to the principal-agent theory, modern enterprises can be regarded as a combination of a series of principal-agent contracts, in which the owner and the

operator have principal-agent relationship. Internal personnel, such as senior management, can directly determine the development of enterprises by grasping the actual control rights of most enterprises, pursue their own interests in the company's strategic decision-making, and even join forces to seek their own interests, thus overriding the owners and other external investors, and thus occupying the legitimate rights and interests of outsiders, forming the phenomenon of "insider control". Therefore, the following assumptions are proposed:

H4: The efficiency of management governance is positively correlated with the standard unqualified audit opinions.

In order to minimize the audit risk in the process of auditing, CPAs will pay more attention to the indicators reflecting the internal governance of the company. Scientific corporate governance mechanism will reduce the audit risk of CPAs and make CPAs more willing to issue standard and unreserved audit opinions. Good internal governance structure can effectively supervise the operation and financial operation of the company, thus reducing the risk of major misstatement of financial statements. Therefore, the comprehensive hypothesis of this paper is put forward:

H5: The more perfect the internal governance mechanism of the company, the more likely it is to be issued standard unqualified audit opinions.

IV. EMPIRICAL DESIGN AND RESULT ANALYSIS

This paper chooses the sample data of Chinese listed companies from 2012-2016 as the research object. The sample excludes financial listed companies and public utilities companies with special financial accounting, and listed companies with incomplete data and abnormal value. The final sample number is 7862. The data of listed companies come from CSMAR. This paper uses Excel to collect and sort out the follow-up analysis, and carries on further statistical analysis through STATA12.0.

A. Variable Selection

This paper constructs the following variable system, as shown in Table 4.1:

Among them, the corporate governance index (X): In the evaluation of corporate governance, academia mainly adopts a relatively simple weightless dummy variable summation method, such as Gompers, Ishii and Metrick (2003) articles using dummy variable summation to construct the shareholder rights index (G-index). This paper calculates corporate governance index from four angles: board of directors, board of supervisors, shareholders and executives,

$$X = \sum_{i=1}^{11} X_i$$
Among them, dumb variables need not be dealt with. When the number of board meetings, ownership

concentration and the number of shareholders' meetings are greater than the median, they should be 0, and when they are smaller than the median, they should be 1. The other

variables are 1 when they are larger than the median and 0 when they are smaller than the median.

TABLE 4-1. DEFINITION OF VARIABLES AND MEASUREMENT METHODS

	Variable name	Measurement standard	Estimate	
Interpreted variables	audit opinion	1 is the standard audit opinion, 0 is the non-standard audit opinion.		
Explanatory variable	Corporate Governance Index (X)		Summation of 11 dumb variables	+
	Board of directors	Number of Board Meetings (x ₁)	Number of board meetings held annually	-
		Shareholding ratio of board of directors (x ₂)	Total number of shares held by board members	+
		Whether the chairman of the board changes normally or not (x ₃)	Normal 1, abnormal 0	+
		Total remuneration of the top three directors (x ₄)		+
	Board of Supervisors	Size of Board of Supervisors (x ₅)	Total number of board of supervisors	+
		Shareholding ratio of board of supervisors (x ₆)	Total number of shares held by members of the board of supervisors	+
	Shareholder	Equity concentration (x ₇)	Number of First Major Shareholders/Total Shares	-
		Number of meetings of shareholders (x ₈)	Number of meetings of shareholders' general meeting held by the company every year	-
		Shareholders' meeting attendance ratio (x ₉)	shares held by shareholders attending the annual general meeting of shareholders/total shares	+
	Management	whether the CEO Changing Normally (x ₁₀)	Normal 1, abnormal 0	+
Total compensation of top three executives (x ₁₁)			+	
control variable	Profitability (ROA)	Net profit / ((Total Assets at the End of the Year + Total Assets at the Beginning of the Year) / 2)	+	
	company size (Size)	Ln(Total assets at the end of the year)	+	
	Total asset turnover rate (TAT)	Business Income / ((Total Assets at the End of the Year + Total Assets at the Beginning of the Year) / 2)	+	
	Corporate Growth Ability (Growth)	Net profit / (Net profit - Last year's net profit)	+	
	BIG6	Six firms are 1, not 0.	-	

B. Model Building

Based on the above analysis, this paper constructs the following models:

(1) A model for studying the impact of board structure on audit opinions:

$$\text{audit opinion} = \alpha_1 * x_1 + \alpha_2 * x_2 + \alpha_3 * x_3 + \alpha_4 * x_4 + \sum \text{controls} + \epsilon$$

(2) A model for studying the impact of supervisory board structure on audit opinions

$$\text{audit opinion} = \alpha_5 * x_5 + \alpha_6 * x_6 + \sum \text{controls} + \epsilon$$

(3) A model for studying the impact of shareholder structure on audit opinions:

$$\text{audit opinion} = \alpha_7 * x_7 + \alpha_8 * x_8 + \alpha_9 * x_9 + \sum \text{controls} + \epsilon$$

(4) A model for studying the impact of management layer on audit opinions:

$$\text{audit opinion} = \alpha_{10} * x_{10} + \alpha_{11} * x_{11} + \sum \text{controls} + \epsilon$$

(5) A model for studying the impact of corporate governance index on audit opinions:

$$\text{audit opinion} = \alpha * x + \sum \text{controls} + \epsilon$$

C. Regression Analysis

The specific regression results are shown in the following table:

From the regression results, the explanatory variables in the board structure have a significant impact on the interpreted variable. The number of board meetings is negatively correlated with audit opinions. The proportion of board ownership, the normal change of chairman and the

total remuneration of the top three directors are positively correlated with audit opinions. Thus, hypothesis 1 is proved.

The explanatory variables in the structure of the board of supervisors are significantly correlated with the interpreted variables. The total size of the board of supervisors is positively correlated with the audit opinions at the level of 10%, and the shareholding ratio of the board of supervisors is positively correlated with the audit opinions at the level of 1%. Thus, hypothesis 2 is confirmed.

The explanatory variables in shareholder governance structure are significantly correlated with the interpreted variables. The concentration index of shareholders and the number of shareholder meetings are negatively correlated with audit opinions at the level of 1%, and the proportion of shareholders attending shareholder meetings is positively correlated with audit opinions at the level of 5%. Thus, hypothesis 3 proves that the efficiency of shareholder structure governance is significantly related to the standard unqualified audit opinions.

TABLE 4.2. REGRESSION RESULTS OF THE IMPACT OF CORPORATE GOVERNANCE STRUCTURE ON AUDIT OPINIONS

Variables	Board of directors	Board of supervisors	Shareholder	management layer	Comprehensive index
Number of Board Meetings	-0.0663*** (0.0171)				
Shareholding ratio of board of directors	0.0255*** (0.0055)				
Whether the chairman of the board changes normally or not	0.7821*** (0.2990)				
Total remuneration of the top three directors	5.95e-07*** (1.10e-07)				
Size of Board of Supervisors		0.9324* (0.0578)			
Shareholding ratio of board of supervisors		2.3289*** (0.6444)			
Equity concentration			-0.0200*** (0.0067)		
Number of meetings of shareholders			-0.0754** (0.0407)		
Shareholders' meeting attendance ratio			0.0181*** (0.0048)		
Is the General Manager Changing Normally				0.9134*** (0.2259)	
Total compensation of top three executives				5.64e-07*** (1.06e-07)	
Corporate Governance Index					0.3095*** (0.0450)
ROA	-0.0020 (0.0902)	0.0253 (0.0951)	0.0250 (0.0932)	-0.0033 (0.0926)	0.0023 (0.0925)
SIZE	0.7400*** (0.0646)	0.8683*** (0.0617)	0.7595*** (0.0623)	0.7075*** (0.0664)	0.7961*** (0.0626)
TAT	-0.0791 (0.0832)	-0.0612 (0.0858)	-0.0982 (0.0825)	-0.1136 (0.0807)	-0.0873 (0.0826)
GROWTH	0.0056 (0.0082)	0.0013 (0.0063)	0.0030 (0.0071)	0.0028 (0.0065)	0.0030 (0.0071)
BIG6	1.0648*** (0.3837)	-15.1130*** (1.2927)	-1.1121*** (0.3814)	-1.2298*** (0.3850)	-1.1064*** (0.3812)
Constant	-13.4806*** (1.3381)	-0.8250** (0.3784)	-14.0929*** (1.2944)	-13.3343*** (1.3890)	-15.5895*** (1.3260)
Observations	7,862	7,862	7,862	7,862	7,862

Note: *** p<0.01, ** p<0.05, * p<0.1; Standard errors in parentheses

The explanatory variables and the explanatory variables in the management structure are significant at the level of 1%. Whether the general manager changes normally or not and the total compensation of the top three executives are positively correlated with the interpreted variables. Thus, Hypothesis 4 is confirmed, which shows that the efficiency of management governance is positively correlated with the standard unqualified audit opinions.

In the comprehensive index regression, the explanatory variables and the interpreted variables are significantly correlated. Corporate governance index is positively correlated with audit opinions. Thus, Hypothesis 5 proves that the better the corporate governance index, the cleaner the audit opinions.

D. Robustness Check

In order to ensure the universality of the results, this paper uses Probit model and panel logit model to regression. The results are basically consistent with the results of the main empirical test, indicating that the results of the main regression test are robust and universality.

V. CONCLUSIONS AND SHORTCOMINGS

A. Conclusions

Corporate governance factors that may affect audit opinions can be divided into five levels. The explanatory variables are divided into board structure, board of supervisor structure, shareholder structure, management structure and corporate governance index. Logit model, Probit model and panel Logit model are used for regression. It is found that under the premise of classified research, the structure of board of directors, board of supervisors, shareholders and management do affect the types of audit opinions; at the same time, in the dumb variable summation model constructed, the quality of corporate governance reflected by index is indeed one of the important factors affecting the types of audit opinions, and companies with good corporate governance are more likely to issue standard and unqualified audit opinions.

B. Insufficient Research

In addition to the company's financial situation, there are also many factors affecting audit opinions, including the size of accounting firms, the level of audit revenue, the change of accounting firms and so on. Due to the limited time and space, this paper only chooses the size of the firm to analyze, which can be further expanded on the basis of this paper in the future.

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