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Audit Committee Financial Expertise and Audit Report Lag: Malaysia Further Insight

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ABSTRACT

Recent audit and financial reporting quality research suggest that audit committee financial expertise is a crucial ingredient for high quality financial reports. However, Malaysian literature has reported no association between audit committee financial expertise and audit report timeliness. Using audit report lag, we examined whether Malaysian audit committee financial expertise is relevant for financial reporting timeliness. Using data from 2005 to 2011 from the top 100 Malaysian companies and the fixed effects panel data approach, we find that audit committee financial expertise is not significantly associated with audit report lag proxies. We further examined this issue with the basic premise that audit committee independence enhances the role of audit committee financial expertise. However, the interaction between these mechanisms shows an insignificant association. Additional investigation reveals that these results are driven by the lack of independence on Malaysian boards. We also find evidence suggesting that neither a large number of subsidiaries nor the quality of financial reporting sufficiently justify the recent Malaysian reforms relating to the financial reporting timeframe.

Keywords: Audit Committee Financial Expertise; Audit Report Lag; Malaysia

INTRODUCTION

Many studies have shown that audit report timeliness is crucial because it is associated with public confidence in the audited financial statements (Ettredge, Sun & Li 2006) and leads to adverse consequences if delayed (Carmichael, Ghosh & Lee 2011; Mande & Son 2011). Indeed, most prior Malaysian studies (e.g. Che-Ahmad & Abidin 2008; Mohamad-Nor, Shafie & Wan-Hussin 2010; Wan-Hussin & Bamahros 2013) assert that audit report timeliness in Malaysia significantly lags behind developed countries, such as the US, and some developing countries, such as Egypt, Oman and Bahrain. Although the World Bank (2012) had indicated that Bursa Malaysia had conducted a consultation process with other stakeholders to shorten the timeframe for audited financial statements, i.e. from four months to two months, Bursa Malaysia has disregarded this intention and only reduced the timeframe for annual reports from six months to five months with effect from 31 December 2014, and then to four months with effect from 31 December 2015. According to Dato' Tajuddin Atan, the CEO of Bursa Malaysia Berhad, the recent changes are sufficient to improve the timeliness in the Bursa and that the timeframe is similar to other markets (Bursa Malaysia 2013).

The objective of this study is to examine the association between audit committee financial expertise and audit report lag. The motivation for this study stems from recent research that investigates the effect of corporate governance mechanisms on the timeliness of audit reports (e.g. Abdullah 2006; Afify 2009; Puasa, Salleh & Ahmad 2014; Abernathy, Beyer, Masli, & Stefaniak 2014; Baatwah, Salleh & Ahmad 2015b; Knechel, Sharma, & Sharma 2012; Sultana, Singh & Van der Zahn 2015). In addition to investigating various corporate governance mechanisms, such as the board of directors and audit committee characteristics, previous research had also provided emphasis on the audit committee financial expertise since discharging audit committee responsibilities require directors with extensive financial knowledge and experience (Bédard, Chtourou & Courteau 2004). Most prior empirical evidence assumes that audit committee financial expertise would enhance the timeliness of audit reports since fewer errors in annual accounts are made, thus requiring less audit work. Although audit committee financial expertise has long been recognized as an important audit committee characteristic (Klein 2002; Xie, Davidson & DaDalt 2003), a large number of Malaysian research on audit committee financial expertise and audit report lag has failed to find a significant association (Ismail, Mustapha & Ming 2012; Mohamad-Nor et al. 2010; Nelson & Shukeri 2011; Shukeri & Islam 2012; Wan-Hussin & Bamahros 2013).

The hesitation of Bursa Malaysia to reduce the timeframe of audited financial statements to two months may be the main reason that the previous research did not find any significant association between audit committee financial expertise and audit report lag, even though the motivation for requiring companies in Malaysia to appoint a financial expert on the audit committee is to enhance the timeliness of financial reporting. We argue that the results

of prior research have suffered from bias because important variables were omitted and no elaboration were given as to why audit committee financial expertise was not associated with audit report lag. Wan-Hussin and Bamahros (2013) has even suggested that most Malaysian research on audit report lag is biased because it suffers from the omission of crucial variables. While they acknowledge that the study of Che-Ahmad and Abidin (2008) is comprehensive, they contend that it fails to consider corporate governance variables.

Similarly, while we acknowledge Wan-Hussin and Bamahros (2013) as a more recent and comprehensive study that explores the contributing factors of audit report lag in Malaysia, this study has also omitted important variables, such as the specific effect variables and board variables that may have resulted in bias in some reported results. For example, prior literature (see Dyer & McHugh 1975; Khlif & Samaha 2014) finds that adjustment, closing annual accounts and audit work, which are time-invariant, are the most important factors that cause delay in issuing the audit report. Although the required audit work can be proxied by some observable variables (Bamber, Bamber, & Schoderbek 1993), adjustment and closing annual accounts are not publicly observable, and companies take a different amount of time to adjust and close their accounts (Davies & Whittred 1980). In addition, it has ignored the effect of the corporate governance reforms made by Bursa Malaysia in 2007 concerning audit committee composition. Furthermore, prior research fails to control the effect of board characteristics on the effectiveness of audit committee characteristics (Rainsbury, Bradbury & Steven 2008; Sharma, Naiker & Lee 2009). Thus, our study addresses all these concerns by using the panel data method and controlling more variables relating to corporate governance and to audit report timelines.

Apart from the omission of certain variables, evidences from Malaysian literature on audit committee financial expertise and audit report lag does not imply that audit committee financial expertise is ineffective in providing timely audit reports. However, we argue that prior literature has ignored the interaction between audit committee financial expertise and independence all together.

Malaysian regulators have stipulated that audit committees must have at least one director with an accounting expertise. However, although initially Malaysian corporate governance reforms did not prohibit executive directors from being present on the committee, subsequently, these reforms require that the committees are exclusively composed of non-executive directors, with a majority being independent directors.

Prior audit committee literature shows that audit committee independence affects the effectiveness of the audit committee (Bronson, Carcello, Hollingsworth & Neal 2009). In addition, audit committee financial experts are more effective when they are independent (Dhaliwal, Naiker & Navissi 2010; Sharma & Kuang 2014). In a setting with full audit committee independence, Abernathy et al. (2014) and Baatwah et al. (2015b) reported that audit committee financial expertise is associated with short audit report lag, while Baatwah, Salleh, and Ahmad (2013) contend that audit committee independence contributes to the effectiveness of audit committee financial expertise. Thus, we argue that in settings with lenient requirements for audit committee independence, it is important to consider the interaction between audit committee financial expertise and audit committee independence.

Using 676 observations made and the fixed effects panel data approach, we find evidences consistent with prior Malaysian literature suggesting that audit committee financial expertise is not associated with short audit report lag. We also find that audit committee independence has an insignificant association with audit report lag. When audit committee financial expertise is associated with its independence, the insignificant association still persists. Further tests suggest that if the board has a large number of independent directors, the audit committee financial expertise and independence significantly enhance the timeliness of audit reports. Further analysis also reports that companies with a large number of subsidiaries are not the main constraint for auditors in providing timely audit reports, and that financial reporting quality is not threatened by short audit report lag.

Our study contributes to the literature pertaining to corporate governance and audit report timeliness in two ways. First, we explored the effectiveness of the interaction between audit committee financial expertise and the independence of the board and audit committee in improving the timeliness of audit reports. Second, for the Malaysian literature, audit committee financial expertise is significantly associated with improved audit report timeliness, albeit the lack of independence on Malaysian boards which undermines this role. As for policymakers, our study contains important implications for Malaysian regulators and companies in relation to how the timeliness of financial reporting and corporate governance can be enhanced.

The paper proceeds as follows. The subsequent section is a review of prior literature and develops the study hypotheses. Section four details the research design. This is followed by the empirical results section, while the conclusion is presented in the final section.

Literature Review and Hypothesis Development

Audit Report Lag

The audit report lag is defined as the time in days that lapse between the year-end and the date of signing the audit report (Davies & Whittred 1980; Dyer & McHugh 1975). Prior literature indicates that a shorter time for audit reports is associated with manifold advantages (Wan-Hussin & Bamahros 2013). From this, a significant amount of research investigating the factors explaining audit report lag from developed and developing countries emerged (e.g. Abbott, Parker & Peters 2012; Ashton,

Willingham & Elliott 1987; Bamber et al. 1993; Carslaw & Kaplan 1991; Ettredge et al. 2006; Leventis, Weetman & Caramanis 2005). This literature has identified and discovered that audit report lag is affected by company and auditor related factors, such as company size, audit complexity, leverage, performance, auditor type, industry type, and so on. It appears that a growing number of studies have examined and reported a link between corporate governance mechanisms and audit report lag (see Abernathy et al. 2014; Afify 2009; Baatwah et al. 2015b; Knechel et al. 2012).

Like other markets, research conducted in Malaysia has also recognized the importance of audit report lag; since 2000 more research began exploring and explaining related factors (e.g. Ahmad & Kamarudin 2003). Although Malaysian regulators and practitioners emphasize a shorter audit report lag, research has found that auditors in Malaysian companies usually take 100 to 115 days to finalize and issue an audit report. This time is comparatively longer than the reported time in other countries; for example, in the US they take between 40 to 50 days (Bamber et al. 1993; Ettredge et al. 2006); in New Zealand, 61 days (Habib & Bhuiyan 2011); in Egypt, 67 days (Afify 2009); in Oman, 51 days (Baatwah et al. 2015b); and in Bahrain, 48 days (Al-Ajmi 2008). Indeed, the timeframe for the audited financial statements in most countries falls between 60 and 90 days. As such, we believe that the Malaysian timeframe is one of the reasons for discouraging companies and their auditors from providing more timely information.

Insights into the Malaysian empirical evidence suggest that there are two streams of literature. One stream exclusively examines the effect of the company and auditor specific factors on audit report lag (see Abidin & Ahmad-Zaluki 2012; Ahmad & Kamarudin 2003; Che-Ahmad & Abidin 2008; Yaacob & Che-Ahmad 2012). This research documents the significant effect of these factors on the audit report lag. Although this stream of literature considers the important variables within the audit report lag model, it fails to find consistent results, nor does it consider the recent development of the audit report lag literature. The other stream mainly focuses on the effect of corporate governance (see Abdullah 2006; Ishak, Sidek & Rashid 2010; Ismail et al. 2012; Mohamad-Nor et al. 2010; Nelson & Shukeri 2011; Wan-Hussin & Bamahros 2013; Puasa et al. 2014). Although this stream of research suffers from significant flaws relating to the methodology, it provides an insight into recent developments in the literature pertaining to audit report lag. It finds that audit report lag is affected by board characteristics, audit committee characteristics and ownership characteristics. However, this literature reports that audit committee financial expertise has little effect on audit report lag.

Building on this literature and its shortages, we examine the association between audit committee financial expertise and audit report lag using the two-way fixed effects panel data model to control for unobservable and time specific effects, and, simultaneously, incorporate board and audit committee characteristics. The following is a review of the prior literature on audit committee financial expertise.

AUDIT COMMITTEE FINANCIAL EXPERTISE

Prior literature has argued that audit committees are an important part of the decision control system for internal monitoring by the board of directors (Fama 1980; Fama & Jensen 1983). They identified a number of audit committee responsibilities that mainly focus on enhancing company performance and shareholders' wealth (see Blue Ribbon Committee (BRC) 1999; DeZoort, Hermanson, Archambeault & Reed 2002). However, previous literature posits that the responsibilities of the audit committee cannot be easily discharged unless such committees have independent directors with relevant expertise, in support with Kalbers and Fogary (1993) who suggested that audit committee expertise enhances the power of the audit committee, and, in turn, produces quality financial reporting. Bédard et al. (2004), on the other hand, suggest that the financial reporting process is the main audit committee's responsibility and that this responsibility can be accomplished through directors who have extensive financial knowledge and experience.

Consequently, many researchers have investigated the influence of audit committee financial expertise on a variety of financial reporting quality and audit quality measures. For example, McMullen and Raghunandan (1996) report that companies with financial problems are unlikely to have audit committee members with financial expertise. Subsequent studies (e.g. Abbott, Parker, Peters & Raghunandan 2003; Xie et al. 2003) report the significant positive influence of audit committee financial expertise on the quality of financial reporting and audit quality. Recent evidences from this literature show that the positive impact of directors with financial expertise on financial reporting quality is exclusively attributed to accounting and auditing expertise and not to other financial expertise (e.g. Dhaliwal et al. 2010; Goh 2009; Krishnan & Visvanathan 2008). With regard to the Malaysian evidence, it is found that audit committee financial expertise is significantly associated with greater demand for high audit quality (Yatim, Kent, & Clarkson 2006), high quality earnings management (Nelson & Devi 2013; Saleh, Iskandar & Rahmat 2007), healthy financial performance (Rahmat, Iskandar & Saleh 2009), voluntary disclosure (Akhtaruddin & Haron 2010), less quarterly financial reporting restatements (Ismail & Rahman 2011), and effectively mediating the auditor-client disputes (Salleh & Stewart 2012).

This study focuses on the effect of audit committee financial expertise on audit report lag. A wide range of prior literature posits that audit committee financial expertise is linked with timely audit reports (e.g. Knechel et al. 2012; Mohamad-Nor et al. 2010). However, as the aforementioned literature does not specifically explain how it can shorten audit report lag, we conjecture that audit committee financial expertise leads to a short audit

report lag in terms of its effect on (1) year-end accounts closing and adjustment; (2) audit work; and (3) auditor-client adjustment negotiation. Findings by Dyer and McHugh (1975) show that these components consumed 37%, 48% and 14% respectively of the total period of year-end audit function. Furthermore, since audit committee financial expertise is associated with less intentional and unintentional errors in accounts (Dhaliwal et al. 2010), reduced audit risk and effort (Yatim et al. 2006) and reduced auditor-client disputes (Salleh & Stewart 2012), the audit report lag is shorter. Supporting this argument, Abernathy et al. (2014) found that the presence and high proportion of accounting expertise on audit committees is associated with timelier audit reports for US companies. Baatwah et al. (2015b) and Sultana et al. (2015) also found that audit committees with financial expertise resulted in reduced audit report lag.

As noted earlier, Malaysian empirical evidence contradicts this expectation and reports that audit report lag is not significantly explained by audit committee financial expertise (e.g. Mohamad-Nor et al. 2010; Wan-Hussin & Bamahros 2013). These results challenge the expectation and requirement of Bursa Malaysia in respect to the presence of financial experts on the audit committee. Given the paucity of evidence supporting the preceding arguments, and given the absence of evidence using Malaysian data suggesting a significant link between audit committee financial expertise and audit report lag, we pose the following hypothesis:

H_1: Audit committee financial expertise is associated with audit report lag.

We argue that the unexpected results concerning the association between audit committee financial expertise and audit report lag for Malaysian data are explained by the omission of interaction between audit committee financial expertise and independence. This is consistent with Abdullah, Yusof, and Mohamad-Nor (2010) and Baatwah et al. (2013) who anticipated an interaction between audit committee independence and expertise in ensuring audit committee effectiveness. It is widely known among authoritative bodies, practitioners and researchers that audit committee independence constitutes a crucial mechanism for ensuring the effective monitoring of audit committees (Blue Ribbon Committee (BRC) 1999; DeZoort et al. 2002). Fama and Jensen (1983) had indicated that independent directors are needed for the effective monitoring function of the board's committees by the audit committee. Further, McMullen and Raghunandan (1996) claimed that independent directors on the audit committee do not hesitate to question management's actions and policies. Prior empirical evidence supports this claim and reports that audit committee independence is associated with high quality financial reporting (e.g. Bédard et al. 2004; Dhaliwal et al. 2010; Klein 2002). Using Malaysian data, it is shown that companies with audit committees that comprise a high proportion of independent directors or that are fully independent have high quality accruals (Saleh et al. 2007), performance (Ameer, Ramli & Zakaria 2009), and level of voluntary disclosure (Akhtaruddin & Haron 2010).

Prior to revising the Malaysian code on corporate governance in 2007, executive directors were allowed to be present on the audit committee. Such directors might hinder the audit committee from performing its role effectively and raise the external auditor's concern about the internal control quality (Abdullah et al. 2010). By using the pre revision sample, Abdullah (2006) and Mohamad-Nor et al. (2010) found that audit committee independence is not associated with timely audit report. In contrast, for companies listed in 2009, Wan-Hussin and Bamahros (2013) reported timely audit reports for audit committees with high proportion of independent directors.

Based on prior Malaysian results concerning the effect of audit committee financial expertise on audit report lag, we posit that audit committee financial expertise is not enough to discipline the managers from committing intentional and unintentional errors, and signaling the quality of control to external auditors. Thus, we expect that audit committee independence will enhance the role of financial expertise in audit report lag because an independent audit committee will further increase the integrity of the managers and reduce audit risk. This is consistent with Dhaliwal et al. (2010), and Sharma and Iselin (2012) who, respectively, reported that independent audit committee financial experts are associated with high quality accruals and less occurrence of financial reporting misstatements. Thus, we propose the following interaction hypothesis:

H_2: The association between audit committee financial expertise and audit report timeliness is significantly moderated by the audit committee independence.

Research Method and Data

Data

Our sample selection process began with the top 100 Malaysian listed companies in 2011. The main reason for selecting these companies is that they have achieved a high level of compliance with corporate governance best practices, quality of disclosure, financial sustainability, and corporate responsibility efforts. Furthermore, these companies constitute 69% of the total market capitalization of all Malaysian public listed companies in 2011 (Minority Shareholder Watchdog Group 2011). In selecting these companies as the initial sample, we traced data for these companies over the period of 2005 to 2011, resulting in 700 observations as the initial sample. One crucial criterion in our sample selection process is that a company must have data for at least two years to achieve the requirement of applying the panel data method. Within the study period, our sample companies have at least three years' worth of

data with the majority having seven years' worth of data. Thus, 676 observations for our empirical evidence were considered. Our sample period selection is based on the fact that it is for the period of five years after the introduction of the Malaysian Code on Corporate Governance and extends four years after its first revision. This period of time can ensure more compliance and effective implementation of the provisions in the code by Malaysian companies. Data were collected for the sample companies from Malaysian capital market websites, company annual reports and the OSIRIS database.

ESTIMATION METHOD

This study first examined the direct association between audit committee financial expertise and audit report lag, and then examines the association after considering the interaction between audit committee financial expertise and independence. We used the fixed effects panel data method to provide the empirical results. Prior literature has documented that panel data methods are effective in controlling for omitted time invariant and specific time variables, in general (Baltagi 2008), and in analyzing audit report lag, in particular (Henderson & Kaplan 2000). Furthermore, we employed two proxies—audit report lag and industry-adjusted audit report lag—for audit report lag. These proxies (audit report lag) are consistent with most prior literature (e.g. Ashton et al. 1987; Bamber et al. 1993) and perform (industry-adjusted audit report lag) more effectively in controlling industry influence on audit report lag (Baatwah, Salleh, & Ahmad 2015a). Based on this method, we ran the following models:

$$ARL_{it} \text{ (or } IAARL_{it}) = \beta_i + \beta_1 ACAEX_{it} + \beta_2 ACID_{it} \text{ (or } FACID_{it}) + \beta_3 ACSZ_{it} + \beta_4 ACM_{it} + \beta_5 BID_{it} + \beta_6 BSZ_{it} + \beta_7 BOM_{it} + \beta_8 FNCOND_{it} + \beta_9 OWCO_{it} + \beta_{10} SUB_{it} + \beta_{11} INVRCEV_{it} + \beta_{12} EXTORD_{it} + \beta_{13} LOSS_{it} + \beta_{14} COSZ_{it} + \beta_{15} NEWS_{it} + \beta_{16} LNCOAG_{it} + \beta_{17} OPINION_{it} + \beta_{18} ADFSZ_{it} + \beta_{19} ADFT_{it} + \beta_{20} ADFEE_{it} + \beta_{21} NADFEE_{it} + \beta_{22\text{-}27} YEARDUM_{it} + \varepsilon_{it} \quad (1)$$

$$ARL_{it} \text{ (or } IAARL_{it}) = \beta_i + \beta_1 ACAEX_{it} + \beta_2 ACID_{it} \text{ (or } FACID_{it}) + \beta_3 ACAEX_{it} * ACID_{it} \text{ (or } FACID_{it}) + \beta_4 ACSZ_{it} + \beta_5 ACM_{it} + \beta_6 BID_{it} + \beta_7 BSZ_{it} + \beta_8 BOM_{it} + \beta_9 FNCOND_{it} + \beta_{10} OWCO_{it} + \beta_{11} SUB_{it} + \beta_{12} INVRCEV_{it} + \beta_{13} EXTORD_{it} + \beta_{14} LOSS_{it} + + \beta_{15} LNCOSZ_{it} + \beta_{16} NEWS_{it} + \beta_{17} LNCOAG_{it} + \beta_{18} OPINION_{it} + \beta_{19} ADFSZ_{it} + \beta_{20} ADFT_{it} + \beta_{21} ADFEE_{it} + \beta_{22} NADFEE_{it} + \beta_{23\text{-}28} YEARDUM_{it} + \varepsilon_{it} \quad (2)$$

We define our interested variables as follows. For the dependent variables, audit report lag (ARL) is the number of days between the year-end and the date of the auditor report signature, while industry-adjustment audit report lag (IAARL) is the difference between the median of audit report lag for a given industry and audit report lag for a focal company from the same industry. As for audit committee financial expertise (ACAEX), we adhered to the definition provided by Bursa Malaysia and the most recent audit committee financial expertise literature (e.g. Dhaliwal et al. 2010; Sharma & Iselin 2012) that considers a director with a qualification and experience in accounting as the only relevant financial expertise to the audit committee. We operationalized this variable as the proportion of accounting expertise on the audit committee. For audit committee independence, we used the proportion of independent directors on the audit committee (ACID) and full audit committee independence (FACID).

For the control variables, we controlled for a set of variables relating to corporate governance, audit risk, audit complicity, timely reporting incentives and auditor characteristics. These factors have been shown to influence the audit report lag (e.g. Ashton et al. 1987; Bamber et al. 1993; Carslaw & Kaplan 1991; Knechel et al. 2012; Leventis et al. 2005; Wan-Hussin & Bamahros 2013). Thus, controlling these variables can eliminate the threat of omitting important variables and enhance the productivity of our models. Indeed, most of this literature have predicted a positive association between audit risk, audit complexity variables and audit report lag. On the other hand, it has also assumed a negative relationship between corporate governance, timely reporting incentives and auditor characteristics, and audit report lag.

The definition of all the variables included in our analysis is shown in Table 1[1].

EMPIRICAL RESULTS

DESCRIPTIVE ANALYSIS

Table 2 shows a comprehensive descriptive statistics for the study sample and variables of interest. Panel A of this Table shows that our sample includes companies with different industry classification, and that companies from the manufacturing and finance industries represent the largest number in our sample, which are 29% and 22%, respectively. It also shows that, on average, most industries have an audit report lag (ARL) of between 65 and 89 days, thereby indicating that introducing a reduction in the timeframe of the audited financial statement would not burden most industries. As for the variables of interest, it is shown that wholesale trade industry is ranked as the highest in terms of financial expertise and independent directors on the audit committee, followed by financial industry in terms of audit committee financial expertise, and construction industry in terms of audit committee independence. In this Table, Panel B shows the means of interested variables for each year and suggests an improvement in ARL, ACAEX, ACID and FACID from year to year indicating that it is possible to observe a difficulty in complying with any reforms in the initial years.

Panel C of Table 2 shows the descriptive statistics for the study variables over a sample period (i.e. 2005-

TABLE 1. Definition of variables

Variable	Measurement of variable
ARL	The number of days between the company year-end and the audit report date.
IAARL	The difference between ARL and the median of ARL for a given industry.
ACAEX	The proportion of directors on the AC with accounting expertise.
ACID	The proportion of independent directors on the AC.
FACID	1 if the AC has full independent directors, 0 otherwise.
ACSZ	The number of directors on the AC.
ACM	The number of meetings held by the AC during the year.
BID	The proportion of independent directors on the board.
BSZ	The number of directors on the board.
BOM	The number of meetings held by the board during the year.
FNCOND	The Zmijewski model for financial distressed companies.
OWCO	The percentage of company shares held by substantial shareholders (>=5%).
SUB	The number of company principle subsidiaries.
INVRCEV	The proportion of the inventory and receivable accounting to total assets.
EXTORD	1 if the company reported extraordinary items, 0 otherwise.
LOSS	1 if the company reported a loss for the current year, 0 otherwise.
COSZ	The natural log of total assets.
NEWS	The difference between current EPS and prior EPS scaled by prior EPS.
LNCOAG	The natural log of the number of years since the company was incorporated.
OPINION	1 if the auditor issued qualified audit report, 0 otherwise.
ADFSZ	1 if the audit firm is Big 4, 0 otherwise.
ADFT	The number of consecutive years that the external auditor is appointed as the external auditor for the company.
ADFEE	The natural log of statuary audit fees.
NADFEE	The natural log of non-audit fees paid to the external auditor.

2011). Our descriptive discussion focuses on the variables of interest. Thus, the descriptive statistics for the other variables can be seen in Panel C. It reports that the mean (median) of ARL is 77 (74) days. This result is contrary to most Malaysian evidence (e.g. Nelson & Shukeri 2011; Wan-Hussin & Bamahros 2013) that shows that, on average, Malaysian auditors take more than 100 days to finalize the year-end audit function, which suggests that a large number of Malaysian companies are prepared for a greater reduction in the timeframe for disclosure. This result is comparable with US empirical evidence (e.g. Abbott et al. 2012; Ettredge et al. 2006). As for IAARL, the average is 3 (0) days, which suggests that Malaysian companies deviate from the industry audit report lag by an additional 3 days. As for interested audit committee variables, it is shown that ACAEX is, on average, 39% (33%). The mean (median) for ACID is found to be 85% (80%). As for FACID, it is reported that 48% of our sample has formed an audit committee with full independence.

Table 3 is the results gauging the effect of multicollinearity on our estimations. We observe that none of the variables in our analysis has a variance inflation factor (VIF) exceeding the normal value indicating that a multicollinearity problem does not threaten our empirical analysis Untabulated results of correlation matrix also indicate no. univariate correlation between two variables higher than 0.80 suggesting that multicollinearity is not a concern (Gujarati 2009). We wish to highlight that COSZ and ADFEE have VIF around 5.5 which is higher than other variables. However, we ran our models after excluding one of these variables, and found that the results for our interested variables are quantitatively similar to the main results.

Regression Results

Table 3 and Table 4 present the results for Equations (1) and (2), with ARL (columns 4 and 5) and IAARL (columns 6 and 7) as the dependent variables. To ensure the efficiency of our estimations, we winsorized all the continuous variables at the level 1% percentile and 99% percentile to reduce the effect of outliers, and we used robust standard error to reduce the effect of heteroscedasticity and autocorrelation problems since Modified Wald test and Wooldridge test indicate the presence of these problems. The results for the control variables are largely consistent with prior studies, except for ADFSZ and ADFT which have a significant and positive association with ARL and IAARL. [2] Our concern is the association between audit committee financial expertise and audit report lag. Thus, we only discuss and deliberate the results related to this concern.

The results indicate that the coefficients of ACAEX are insignificantly associated with ARL and IAARL (p>.10), which is consistent with prior Malaysian evidence (Mohamad-Nor et al. 2010; Wan-Hussin & Bamahros 2013). This further supports our contention suggesting that, by itself, Malaysian audit committee financial expertise is unable to ensure timely audit reports, and

TABLE 2. Descriptive statistics

Panel A: Sample distribution and means for interested variables for each industry						
Variable	No.Obs	%	ARL	ACAEX	ACID	FACID
Agriculture, Forestry, and Fishing	81	12%	73.82	0.38	0.86	0.49
Mining	30	4%	106.70	0.30	0.92	0.70
Construction	47	7%	85.38	0.38	0.93	0.77
Manufacturing	199	29%	81.23	0.34	0.86	0.51
Transportation and Utilities	86	13%	65.67	0.43	0.81	0.33
Wholesale Trade	7	1%	114.29	0.48	1.00	1.00
Retail Trade	28	4%	65.86	0.36	0.79	0.29
Finance, Insurance, and Real Estate	146	22%	68.84	0.46	0.82	0.39
Services	52	8%	88.65	0.40	0.85	0.50
Total	676	100%	77.38	0.39	0.85	0.48

Panel B: Means for interested variables for each year							
Variable	2005	2006	2007	2008	2009	2010	2011
ARL	79.01	77.93	76.64	77.01	76.71	77.47	77.04
ACAEX	0.35	0.37	0.37	0.39	0.41	0.41	0.43
ACID	0.77	0.78	0.81	0.87	0.88	0.91	0.91
FACID	0.22	0.23	0.36	0.54	0.60	0.69	0.67

Panel C: Descriptive statistics					
Variable	Mean	S.D.	0.25	0.50	0.75
ARL	77.38	26.02	56.00	74.00	102.0
IAARL	2.760	24.49	-10.75	0.000	20.00
ACAEX	0.390	0.190	0.250	0.330	0.500
ACID	0.850	0.150	0.750	0.800	1.000
FACID	0.480	0.500	0.000	0.000	1.000
ACSZ	3.630	0.760	3.000	3.000	4.000
ACM	5.590	2.530	4.000	5.000	6.000
BID	0.500	0.140	0.400	0.500	0.570
BSZ	8.180	1.940	7.000	8.000	9.000
BOM	6.790	3.370	4.000	6.000	8.000
FNCOND	-2.050	1.510	-3.060	-2.190	-1.210
OWCO (%)	52.15	19.38	37.82	54.74	67.03
SUB	35.98	44.06	7.000	24.50	47.00
INVRCEV	0.230	0.170	0.080	0.190	0.330
EXTORD	0.520	0.500	0.000	1.000	1.000
LOSS	0.040	0.200	0.000	0.000	0.000
COSZ (RM000)	16000000	45000000	81000000	190000000	670000000
COSZ	21.65	1.761	20.51	21.36	22.62
NEWS	1.540	31.96	-4.150	2.000	8.770
LNCOAG	3.250	0.740	2.830	3.430	3.740
OPINION	0.010	0.080	0.000	0.000	0.000
ADFSZ	0.900	0.300	1.000	1.000	1.000
ADFT	6.720	2.970	5.000	7.000	9.00
ADFEE (RM000)	990.0	2000	180.0	350.0	9300
ADFEE	12.96	1.218	12.08	12.75	13.74
NADFEE (RM000)	450.0	1100	21.00	97.00	300.0
NADFEE	10.78	3.439	9.952	11.48	12.63

COSZ (RM000), ADFEE (RM000) and NADFEE (RM000) are total assets, total audit fees and total non-audit services measured in amounts. See Table 1 for definition of variables.

TABLE 3. Regression results

Variable	VIF	Exp. Sign	ARL	ARL	IAARL	IAARL
			Coef/ t.stat	Coef/ t.stat	Coef/ t.stat	Coef/ t.stat
ACAEX	1.20	?	5.521	5.465	6.035	5.961
ACID	1.44	-	-3.224		-2.102	
FACID	1.46	-	-1.181***	-1.469		-1.212
ACSZ	1.34	-	-0.443	-1.377***	-1.120***	-1.317***
ACM	1.98	-	1.393	-0.449	-0.403	-0.411
BID	1.56	-	0.170	1.789	1.458	2.014
BSZ	1.44	-	0.198	0.181	0.174	0.191
BOM	2.41	-	0.891***	0.194	0.166	0.161
FNCOND	2.27	+	-0.184***	0.871***	0.695***	0.679***
OWCO	1.20	-	0.034**	-0.185***	-0.148***	-0.149***
SUB	2.49	+	-1.846	0.036**	0.036**	0.037**
INVRCEV	1.21	+	4.166***	-2.087	0.250	0.001
EXTORD	1.20	+	4.642***	4.138***	4.633***	4.600***
LOSS	1.15	+	0.391	4.592***	5.052***	4.993***
COSZ	5.49	-	-0.001	0.433	0.311	0.363
NEWS	1.08	-	-10.722**	-0.001	-0.001	-0.001
LNCOAG	1.40	-	6.145**	-10.808**	-15.311***	-15.346***
OPINION	1.01	+	5.399**	6.295**	5.978**	6.115**
ADFSZ	1.19	-	0.324*	5.487**	5.541***	5.608***
ADFT	1.28	-	0.743	0.327*	0.313*	0.315*
ADFEE	5.53	?	-0.419***	0.678	1.213	1.148
NADFEE	1.30	_		-0.422***	-0.426***	-0.428***
YEARDUM				Included		
_cons			104.9***	103.4***	36.10***	56.19***
N			676	676	676	676
R^2			0.089	0.091	0.096	0.097
Adj R^2			0.050	0.053	0.055	0.056
T-stat			0.000	0.000	0.000	0.000

*p<.10; **p<.05; ***p<.01
See Table 1 for definition of variables

that it needs more support to ensure the contribution of audit committee financial expertise. Thus, we contend that audit committee independence can enhance the role of financial expertise in attaining a short audit report lag. In this regard, we report and discuss the results for the audit committee independence and audit report timeliness proxies. We should report that the coefficient of ACAEX is positive which is contradictory to previous Malaysian evidence (e.g. Mohamad-Nor et al. 2010; Wan-Hussin & Bamahros 2013). One possible explanation for such result is that in our sample, audit committee financial expertise is highly exposed to risk in accounting irregularities cases since our sample includes the largest listed companies in Malaysian Bursa. As such these directors are concerned more with the risk than other directors are (Krishnan & Visvanathan 2008) and so have greater incentivies to reduce this risk by conducting a more detailed review and investigation of accounting irregularties and discussing different accounting issues in detail with the auditor and other related parties. Such process may lead to a longer period required to prepare the annual reports for auditing and time has been extended for the auditor to complete the audit.

Using the proportion and full audit committee independence, it is reported that ACID and FACID are negatively but insignificantly associated with ARL and IAARL (p>.10). This result is contradictory to Wan-Hussin and Bamahros (2013) who found a negative and significant association. We believe that our results are reliable because the sample of this study has allowed us to control the effect of recent revisions in the code on corporate governance that had brought a significant improvement to the Malaysian corporate governance practices, particularly audit committee independence. Thus, it suggests that the results of prior research relating to audit committee independence and audit report lag are endogenously determined by a time specific effect.

Having reported no significant association between audit committee financial expertise and audit report timeliness, we tested whether including more independent directors on the audit committee enhances the role of audit committee financial expertise. We employed the interaction approach to examine this interest by multiplying ACAEX with ACID and FACID. After standardizing the components of the interaction terms ACAEX, ACID and FACID, it is shown that the interaction terms of ACAEX*ACID and ACAEX*FACID

TABLE 4. Interaction analysis

Variable	Exp. Sign	ARL	ARL	IAARL	IAARL
		Coef/t.stat	Coef/t.stat	Coef/t.stat	Coef/t.stat
ACAEX	?	1.059	0.563	1.158	0.634
ACID	-	-0.513		-0.346	
FACID			-1.389		-1.233
ACAEX*ACID	-	0.651		0.664	
ACAEX*FACID	-		1.025		1.075
ACSZ	-	-1.247***	-1.437***	-1.189***	-1.381***
ACM	-	-0.438	-0.446	-0.398	-0.407
BID	-	1.827	2.057	1.902	2.294
BSZ	-	0.139	0.168	0.142	0.177
BOM	-	0.219	0.199	0.188	0.167
FNCOND	+	0.924***	0.895***	0.729***	0.705***
OWCO	-	-0.188***	-0.179***	-0.142***	-0.144***
SUB	+	0.034**	0.035**	0.036**	0.036**
INVRCEV	+	-1.342	-1.712	0.764	0.399
EXTORD	+	4.003***	4.038***	4.466***	4.496***
LOSS	+	4.713***	4.672***	5.124***	5.076***
COSZ	-	0.346	0.401	0.266	0.329
NEWS	-	-0.001	-0.001	-0.001	-0.001
LNCOAG	-	-10.655**	-10.817**	-15.242**	-15.355***
OPINION	+	6.181**	6.257**	6.015**	6.075**
ADFSZ	-	5.393**	5.532**	5.534***	5.654***
ADFT	-	0.346**	0.349**	0.335**	0.338**
ADFEE	?	0.979	0.871	1.454	1.350
NADFEE	-	-0.444***	-0.440***	-0.451***	-0.447***
YEARDUM			Included		
_cons		102.0***	103.7***	34.30***	35.40***
N		676	676	676	676
R^2		0.091	0.091	0.098	0.098
Adj R^2		0.051	0.051	0.058	0.058
T.stat		0.000	0.000	0.000	0.000

*p<.10; **p<.05; ***p<.01
See Table 1 for definition of variables.

are positively and insignificantly correlated with ARL and IAARL, thereby suggesting that our hypothesis is not supported.

The result is explained as follows. First, audit committees in Malaysia are not given sufficient support by the board. It has been reported that boards with a high proportion of independent directors and expertise are more likely to have a more effective audit committee (Rainsbury et al. 2008) but this is not the case. More insights into our data reveal that Malaysian boards are dominated by executive directors, and that, in most cases, independent and financial expert directors on the audit committee are the only independent and financial expert directors on the board. Second, given their status as a minority on the board and the long timeframe requirements for disclosing audited reports, these directors are more concerned about the accuracy and reliability of accounting numbers than the relevancy of these numbers. This is because their reputation is more likely to be significantly threatened in cases such as accounting numbers manipulation, than it is for timely disclosure. Therefore, they might conduct a more detailed review and discussion with the internal auditors, CFO and CEO. In addition, they might ask the auditor to delay the issue of an audit report to further examine whether the suggestions of auditors reflect an independent auditor and how managers address these suggestions.

ADDITIONAL ANALYSIS

BOARD INDEPENDENCE

As we have suggested, audit committee independence enhances the role of financial expertise in audit report lag and that board independence is considered as a major element for ensuring overall effective monitoring. In Malaysia, there is evidence indicating that only independent directors on the board perform greater monitoring (Ameer et al. 2009). Using subsample analysis, we tested equation (1) and (2) by grouping our sample into two groups based on board independence. According to prior literature (e.g. Krishnan & Visvanathan 2008), companies with a board independence of 60% and above are considered as having

a more independent board (H_BID), whilst companies with less than this proportion are considered as having a less independent board (L_BID). We conducted all these tests using ARL, as it is the measure that is mostly used for audit report timeliness and for the purpose of brevity. Furthermore, we only considered the proportion of independent directors to measure audit committee independence.

Table 5 shows the results of this analysis, and it indicates that ACAEX and ACID are negatively and significantly associated with ARL for boards dominated by independent directors. On the other hand, for boards with a high proportion of non-independent directors, ACAEX is significantly and positively associated with ARL, while ACID is insignificantly associated. These results suggest that audit committee financial expertise and independence are hindered by the lack of independent boards in reducing the lag of the audit report. However, ACAEX*ACID is positively and insignificantly associated with ARL for H_BID (L_BID) group indicating that if the board is dominated by independent directors, financial expertise director can effectively contribute to short audit report lag regardless of the proportion of independent directors in the committee. Furthermore, we observed that ACSZ and ACM have a significant and negative association with ARL for boards with more independent directors, but that they are insignificant for boards with fewer independent directors, thereby indicating that board independence is crucial to ensure the effectiveness of the role of the audit committee on the timeliness of audit reports.

COMPANY SUBSIDIARIES

One claim advanced by Bursa Malaysia for reducing the timeframe of the audited financial statement (60 days) is that the auditors of companies with a large number of subsidiaries will face difficulty in complying with any reduction in the current timeframe. In most of the literature, as well as our empirical evidence, it is suggested that companies with a large number of subsidiaries have a longer audit report lag. We empirically examined this

TABLE 5. Additional analysis

Variable	ARL					RESTMT
	H_BID		L_BID		LNSUB	
	Coef/ t.stat	Coef/ t.stat	Coef/ t.stat	Coef/ t.stat	Coef/ t.stat	Coef/ t.stat
ACAEX	-17.385***	-3.129***	10.429***	2.002***	5.907	2.066
ACID	-12.215**	-1.899**	-1.822	-0.299	-2.908	-1.040
LNSUB					-1.318	
ARL_S						-0.481
ACAEX*ACID		1.472		0.380		
ACSZ	-2.829***	-2.735***	-1.835	-1.878	-1.229***	-0.599
ACM	-1.127**	-1.112*	-0.163	-0.158	-0.444	0.071
BID					1.419	-2.584
BSZ	1.040	0.906	0.783	0.749	0.174	0.283
BOM	0.515	0.551	0.084	0.099	0.203	-0.039
FNCOND	0.418	0.338	1.141***	1.157***	0.788***	0.307
OWCO	-0.291***	-0.281***	-0.147**	-0.144**	-0.181***	-0.002
SUB	0.214**	0.225**	-0.013	-0.013	-	0.036*
INVRCEV	53.986***	54.049***	-16.140***	-15.832***	-2.259	6.708**
EXTORD	5.272**	4.191	3.637**	3.565**	4.240***	-0.799
LOSS	-0.321	-0.039	5.363***	5.435***	4.684***	-0.101
COSZ	-0.781	-0.764	-1.676**	-1.658**	0.827	1.108*
NEWS	0.0119***	0.011***	0.004	0.004	-0.001	-0.006
LNCOPAGE	-1.248	-1.671	-13.964**	-13.943**	-10.418**	2.283
OPINION	8.914***	8.273***	5.986*	6.065*	5.972**	0.474
ADFSZ	-1.523	-1.968	6.233**	6.255**	5.345**	0.292
ADFT	-0.555	-0.330	0.558***	0.569***	0.351*	-0.204
ADFEE	2.312**	2.432**	1.892***	2.038***	1.363	-1.074
NADFEE	-0.091	-0.091	-0.459***	-0.475***	-0.424***	-0.015
YEARDUM	Included					
_cons	89.49*	71.769	140.44***	140.89***	87.87***	-
R^2	0.441	0.449	0.106	0.107	0.088	0.187
T.stat	0.000	0.000	0.000	0.000	0.000	0.000
N	159	159	517	517	676	399

*p<.10; **p<.05; ***p<.01

H_BID is indicator for subsample with high proportion of board independence; L_BID is indicator for subsample with low proportion of board independence; LNSUB is indicator variable equals 1 if the number of subsidiaries is equal or greater than sample median, 0 otherwise; ARL_S is indicator variable equals 1 if the ARL is smaller than sample median, 0 otherwise; RESTMT is indicator variable equals 1 if the company restates its annual report, 0 otherwise; See Table 1 for definition of other variables.

claim by creating a dummy variable (LNSUB) that reflects companies with a number of subsidiaries equal to or more than the median of our sample (25).

In Table 5, we provide an estimation of equation (1) after replacing SUB with LNSUB, and found that LNSUB is insignificantly related to ARL, which suggests that the presence of a large number of subsidiaries does not hinder the auditors in expressing their opinion more quickly. Furthermore, we replaced LNSUB by using the number of foreign subsidies and rerun equation (1). The unreported results support the preceding conclusion.

SHORT AUDIT REPORT LAG AND QUALITY OF FINANCIAL REPORTING

We also tested another claim by Bursa Malaysia in that introducing a new reduction relating to the timeframe of audited financial statements will threaten the quality of these statements. Using US data, Knechel and Sharma (2012) showed that short audit report lag is not associated with a decrease in the quality of financial reports. Accordingly, we tested this claim by using financial reporting restatement (RESTMNT) as a proxy for financial reporting quality, and companies with an audit report lag less than the sample median as a proxy for short audit report lag (ARL_S). In our full sample, 18% of companies restated their annual financial reports. However, using logistic regression for panel data, Table 5 shows that ARL_S is negatively and insignificantly associated with ARL, thereby indicating that a short audit report lag does not lead to lower quality financial reporting.

CONCLUSION

This study is a timely response to the recent requirements made by Bursa Malaysia relating to the timeframe for disclosure, and to the Malaysian empirical evidence relating to the association between audit committee financial expertise and audit report lag. We find that Malaysian companies are able to provide more timely financial reports that are compatible with more developed countries, such as the US. Furthermore, we find that audit committee financial expertise is not associated with audit report lag. Thus, we propose that audit committee independence enhances audit committee financial expertise in providing timely financial reports. Using the interaction approach, we documented the association between audit committee financial expertise and independence with audit report lag, are either separately or jointly significant.

Consequently, we explained that these two significant monitoring mechanisms receive insufficient support from the board of directors. Empirical evidence testing this explanation suggests that audit committee financial expertise and independence are associated with a short audit report lag if the board of directors is dominated by independent directors. We also found no empirical evidence supporting that a large number of subsidiaries hinders the ability of auditors to provide a timely audit report, and that reducing the timeframe of audited financial reports will dilute the quality of such reports.

Our findings suggest crucial implications for the audit report timeliness literature and Malaysian policymakers. We have contributed to prior literature by examining whether the interaction between audit committee financial expertise and its independence enhances the timeliness of audit reports. With respect to the contribution to the Malaysian audit report lag literature, we believe that audit committee financial expertise is a relevant factor in explaining audit report lag when the effect of board independence is included as a contributing factor. As for policymakers, we have evidence suggesting that Bursa Malaysia regulators have missed an opportunity to further enhance the timeliness of financial reporting since a large number of companies have an audit report lag of no more than 77 days. In addition, our findings support the latest reforms in relation to the composition of the audit committee, and suggest that Malaysian regulators should pay further attention to the composition of the board.

We acknowledge that our results should be interpreted with caution due to some methodological limitations. First, the data come from companies of a relatively large size in terms of their capitalization. Thus, the generalizability of our results is constrained by this limitation. Second, although our results are more reliable because we have control over most of the variables in the audit report lag model and we have considered company and time specific effects, this reliability could be threatened if the audit report lag is dynamic. Thus, we suggest that future research considers these limitations.

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NOTES

1. We did not control the recent findings in relation to internal audit function because of the high number of missing data for internal audit investment over the study period and the fact that the majority of our sample has an in-house internal audit function.
2. We could explain the unexpected results for ADFSZ and ADFT as follows: Big 4 audit firms in Malaysia are currently exposed to greater reputation and financial risks as a result for discovering many cases of accounting irregularities in 2007 (e.g. Megan Media, Transmile Bhd, Maxbiz Corp Bhd) and establishing Audit Oversight Board (AOB) in 2010 for monitoring and inspecting audit firms registered in Malaysia. Confirming our claim, most Malaysian evidence on the association between big 4 audit firms and audit report lag that uses data after 2005 have positive or not economically significant association (e.g. Ishak, Sidek

& Rashid 2010; Ismail et al. 2012; Mohamad-Nor et al. 2010; Nelson & Shukeri 2011; Yaacob & Che-Ahmad 2012; Wan-Hussin & Bamahros 2013). Alternatively, big 4 audit firms in Malaysia are concerned with the quality of reports more than any other type of auditors. Therefore, they conduct more detailed audit and exert large amount of efforts, which in turn is associated with the longer period of time required to complete the audit. As for audit firm tenure, it is possible that auditors in Malaysia in the initial years are more motivated to prove themselves to shareholders as efficient in providing timely accounting information, but after a few years this motivation decreases as they become more powerful or non-independent.

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