

Audit Report Lags of Federal Statutory Bodies in Malaysia

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Abstract—This study examines the determinants of audit report lag (ARL) for Federal Statutory Bodies (FSBs) in Malaysia. Final samples of 92 FSBs during the period 2006 to 2010 are used in this study. This study examines firm size, leverage, profitability and auditor's comment to determine the ARL and four hypothesis have been constructed in this study. The regression analysis was conducted to identify the relationship between firm size, leverage, profitability, auditor's comments and ARL. The findings suggest that auditor's comment highly influence ARL of FSBs. Firm size and profitability of the FSBs show a negative relationship towards ARL. This study also shown there is an improvement of audit delay in year 2009 and 2010. This aligned with culture of precision value which has been introduced by Malaysia Prime Minister, Datuk Seri Najib Tun Razak in Government Transformation Programme. Due to limited information disclose in the financial statements, future researcher can extend this study by looking at qualitative aspect.

Keywords—Federal Statutory Bodies, Malaysia, Audit Report Lags

I. INTRODUCTION

Public sector is an organization and they are authorized by the public to manage their resources efficiently. In order to determine whether the public resources have been managed properly, Auditor General (AG) is appointed by the government to examine all their activities. Due to this, public sector organizations are required to keep proper and faithful accounting records. Federal Statutory Bodies (FSBs) which are corporations formed to carry out certain government duties are

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also required to keep proper and faithful accounting records. Similar to public and private sectors, FSBs must prepare proper financial reports about their organizations as this statement is a key instrument by which stakeholders can obtain information thus maintaining their trust in the organization.

Financial statements are instruments that provide information about financial position, performance and adaptability of an enterprise. Users such as investors will use the financial statements to assess the stewardship and decision making capabilities of management. According to Prime Minister of Malaysia, Dato' Sri Najib Bin Tun Abdul Razak, in this challenging world both private sectors and public sectors are required to play an important part in determining the growth of the economy (Economic Transformation Programme Update, July 2011).

As the public is one of the contributors to the government fund, they have a right to timely information about the company in making a decision. In the process of administering the transformation programmes, the timeliness of information is important and it will determine the quality of the decision made by the users. It is also an important area that the users of accounting information are concerned about (Afify, 2009). Lengthy reporting lag may relate to lower quality of information (Knechel and Payne, 2001). Research done by Abdulla (1996) revealed that greater benefit can be derived from the financial statement when the time lag between the end of accounting year and the publication date is shorter.

II. OBJECTIVES OF THE STUDY

Due to the issues being discussed earlier, this study is designed to meet two objectives.

1. To identify the trend of audit report lag of Federal Statutory Bodies.
2. To examine the factors that determine audit report lag of Federal Statutory Bodies.

Besides the public, government may have potential interest on this issue as they are responsible for monitoring the FSBs performance throughout the year. Sometimes problems in the

organization can be detected by using timely audit report (Law P, 2009) and as a result, management can rectify the problems immediately. This will increase the performance of the organization and enhance public confidence towards the organization. Hence, quality information can be spread to the users in evaluating the FSBs' performance.

Since large organizations are expected to have good management, it is important for the users to determine the determinants of audit report lag (ARL). Therefore, period of audit lag has to be reduced. As such this study also aims to raise the issues on the determinants of ARL of FSBs.

FSB are formed to carry out government task in order to achieve government's mission and goals and it is independent of the government. However, government is still responsible to ensure that funds from the taxpayer are being used in efficient, effective and economic manner by FSB in carrying their operation. As clearly stated in the FSB legislation or according to Ministerial Function Act 1969 each FSB is controlled by Minister. The Minister is responsible to Parliament for the operation of all Government Boards and agencies. According to Retirement Fund (Incorporated) also known as 'KWAP' 2009, there are 118 corporations listed as FSB in Malaysia. Inland Revenue Board (IRB), Employee Provident Fund (EPF), Social Security Organization (SOCISO), local universities such as University Utara Malaysia, University Technology Mara and etc are examples of statutory bodies under the federal government.

Although FSB govern under its own Act, they are also required to have effective board of directors to monitor FSB's management and administration. Boards of directors under FSB are appointed by the Minister of Finance which the appointment is based on the proven track records of integrity, ability and reliability to undertake their responsibility. The board of directors under FSB consists of representatives from various stakeholders. These representatives consist of members who represent government, employers, employees and professional members from various backgrounds. The combination of these directors will lead to competence and a strong ability of the directors in discharging their duties effectively. The appointment and termination of the board's members are controlled by respective Minister.

The annual reports of FSBs were gathered from Parlimen. Besides annual report, the auditor's certificate issued to FSBs also has been selected in order to determine the ARL.

III. AUDIT REPORT

A. Audit Report Lag (ARL)

Financial statements are the products of financial reporting which are being used by the corporation to deliver information to the users. These enable users to better infer the reality of a corporation's financial performance and position. This indicates that it is important for corporations to provide quality financial report to the users. The quality of disclosure in corporate annual report and account has been represented in the literature by several construct including adequacy (Buzby, 1974), comprehensiveness (Barrett, 1976) and informativeness

(Alford et al, 1993). Another characteristic of quality disclosure is timeliness. Henderson and Kaplan (2000), gap between financial year end and date of auditor's report is referred to as the 'audit report lag'.

In a public sector, government servants play an important role in carrying their duties for their superior. These include their duties in communicating economic events of the government to the users including public in order to determine the effectiveness and efficiency of the individual in performing their duties. This is different from Public Listed Companies (PLC) as public servants are responsible to the public as a whole. In certain countries, concept of accountability is very important in the organization including public sector. Recent study by World Bank indicates there is strong relationship between good governance and good government performance. This requires the government to have high standards for governance and accountability.

However, this accountability differs depending on the organization whereby the public sector has been criticized for inefficiency, ineffective accountability and poor performance. To overcome these problems, National Audit Department (NAD) requires their staff to comply with quality standard MS ISO 9001: 2008 in carrying their duties. This standard requires auditor to carry out their duties within four months. Audit report is an auditor's opinion about the accuracy of government financial statements.

According to Governmental Accounting Standards Board's (GASB) 1987, Financial reporting should be able to assist users in determining the level of services that can be provided by the government organization and its ability to pay its liabilities as they become due.

IV. THEORY

A. Shareholder Theory

1Malaysia campaign which was launched by Prime Minister, Y.A.B Dato' Sri Najib Tun Abdul Razak on 3 April 2009 revealed that government tries to create better value to their stakeholders. By having good governance in FSB, stakeholders' interest can be protected. This can be explained by stakeholder's theory. Phillip and Freeman, (2003) discussed the stakeholder theory as:

"a theory of organizational management and business ethics that address the morals and values applicable to managing an organization."

B. Agency and Accountability Theory (Stewardship)

In a recent year, there is great pressure towards better accountability within public sector entities since it shows the effectiveness and efficiency of the organization in managing public resources. According to Rohaimi (2011); Hughes (2003); Chapman (2000) public sector is accountable to their superiors, political leadership and public at large in managing public fund and maximizing their wealth. It is public sector responsibility to report their activities to the public and provide justification on what they have done. Accountability

of public sector in carrying their duties is communicated to the public through financial statement. This is stated clearly in the Concept Statement No 1 of Governmental Accounting Standards Board's (GASB).

Agency theory also suggests that agency costs arise when there is conflict of interests between principal and agent. In public sector, agency cost arises when public sector fails to fulfil public's demand. It shows agency cost is an expense to the public. Many researchers have been done on accountability and agency theory in private sector and this study attempts to apply accountability practices and agency theory perspective in the FSB.

V. MEASUREMENT OF INDEPENDENT VARIABLES

Figure 1. Theoretical Framework for Determinants of Audit Report Lags of Federal Statutory Bodies in Malaysia

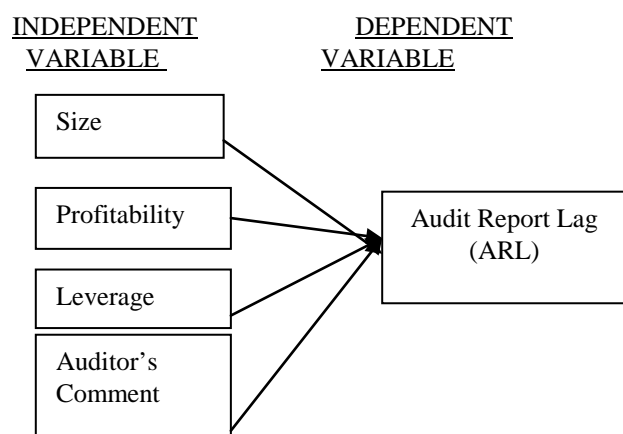


Figure 2. Sample Selection

List of FSB at the end of 2010	118
<i>Less</i>	
FSB where annual reports not available in the Parliament's record	(13)
<i>Less</i>	
FSB which does not meet the criteria	(13)
Final sample	92

A. Size

For local authorities', Rubin (1992) found that special interest group exists in the larger cities may give high pressure to government officers to provide timely reports. Municipal financial statements are the only information available for the public to determine municipal's financial position. Therefore, shorter ARL is expected. Prior investigation by Payne and Jensen (2002); McLelland and Giroux (2000) shows municipal size also has an influence on audit delay. Positive relationship is predicted for size of population and ARL (Bamber et al, 1993).

H1 – There is a negative association between ARL and FSB size.

B. Profitability

The importance of LA financial reporting as a medium to provide information to public users has been discussed by many researchers (Collin et al, 1991; Tayib, 1994). A study by Tayib, Hugh and Ameen (1999) revealed that Malaysian taxpayers has an interest in reading annual report especially on statement of income and expenditure as it discloses relevant information on the disbursement of taxpayer money. Declining income for LA is a signal of management conflict in managing taxpayer money. This requires AG to increase audit effort and perform their audit carefully in order to maintain public confidence towards government in managing their money. However study by Annaert et al (2002) found that no relationship exists between profitability and ARL.

H2 - There is negative relationship between ARL and FSBs' profitability.

C. Leverage

As PLCs, FSBs also can incur large debt in building and maintaining their infrastructure and provide service to public. FSBs with high leverage are expected to have high agency cost. Thus, a high quality audit service is required to satisfy the need of users especially public as a whole. Information on financial positions of the government is important to government bondholders in determining the ability of LA to pay the debt. This requires LA to provide quality information by increasing their monitoring on municipal performance. Increase in audit efforts will lead to lengthy audit engagement (Jensen and Meckling, 1976).

H3 – ARL is significantly and positively associated with level of FSBs' leverage.

D. Auditor's Comment

According to Lys and Watts (1994), auditor's remarks also may lead to increase in ARL because auditors might try to protect themselves from any potential legal action by taking more time to audit the errors. Remarks or comment by auditor is expected to convey bad news about the organization (Whittred, 1980). In the case of FSBs, bad news will have a huge impact on the public as they are a contributor to the Malaysia's economy. Based on the above discussion, this study argues that the auditor's comments are likely to increase audit delay. Therefore the following hypothesis is proposed:

H4 – ARL is significant and positively associated with auditor's comment.

VI. REGRESSION MODEL

Based on previous model employed by Ashton (1989) and Carlsaw and Kaplan (1991) a model of audit delay is

developed. The regression model is used to test the association between dependent variables and ARL. The model is as follows:-

$$\text{ARL} = \beta_0 + \beta_1 (\text{SZ}) + \beta_2 (\text{PROF}) + \beta_3 (\text{LEV}) + \beta_4 (\text{ADCMNT}) + \epsilon$$

Where β_0 , the constraint coefficient of regression; $\beta_1 - \beta_4$, regression coefficient of independent variables; ϵ , random error term.

ANALYSIS OF FINDINGS

Table 1. Summarize the descriptive result for Audit Delay for 2006-2010

	2006	2007	2008	2009	2010
N	92	92	92	92	92
Mean	181.15	187.33	189.23	179.88	179.10
Median	196.00	206.00	207.00	186.50	185.50
Std. Deviation	51.214	49.942	50.808	51.963	51.435
Skewness	-.980	-1.220	-1.276	-.602	-1.063
Minimum	29	25	23	21	18
Maximum	284	278	241	332	237

Table2. Descriptive Statistics: Independent Variables

	SZ	PROF	LEV
Mean	8.0147	.3195	7.0368
Median	8.0550	.3100	7.0850
Std. Deviation	.88689	.14600	1.05225
Skewness	-.189	.266	.003
Kurtosis	.460	-.439	.550
Minimum	5.35	.00	3.75
Maximum	10.39	.74	10.36

Before conducting the Pearson Correlation analysis, the independent variables are examined to ensure normal distribution of data that need to be performed. Data is said to be normal if the standard Skewness is within the range of 1 and -1, while for standard Kurtosis data has to be less than 3 (Pallant, 2003). Based on Table 1 and Table 2 above, all data are normally distributed according to each variable. Relationship between variables in this study is tested using Pearson's correlation. A positive value in the correlation implies a positive association while negative value implies negative association. This analysis is important in describing

the strength and direction of the linear relationship between two variables (Pallant, 2003).

Table 3. Pearson's Correlation between Dependent and Independent Variables

	DAYS	SIZE	LEVERAGE	PROFIT	AC
DAYS	1	-0.56	-.048	-.057	.115*
SIZE	-.056	1	-.002	.742**	-.031
LEVERAGE	-.048	-.002	1	-.018	.122* *
PROFIT	-.057	.742* *	-.018	1	.000
AC	.115*	-.031	.000	.000	1

*Correlation is significant at the 0.05 level (2-tailed)

**Correlation is significant at the 0.01 level (2-tailed)

Notes:

DAYS is measured by number of days between the date of financial statement and the date of auditor's report.

SIZE is measured by natural logarithm of year-end total asset.

LEV is measured by proportion of total debts to total assets.

PROFIT is measured by natural logarithm of the net income for the year.

AC is measured by using dichotomous variable of (with auditor's comment) and 0 (no auditor's comment).

Table 3 above shows the Pearson correlation analysis result between the variables for this study. The result indicates that there is a positive linear correlation between auditor's comment (AC) with audit report lag (DAYS) and this supports hypothesis (H4). It shows that auditor's comments on FSBs' financial statements are significant against the delay of auditor's report. According to Lys and Watt (1994); Houghton and Jubb (1999) errors or irregularities found in the financial statements require auditor to spend more time and effort in performing additional audit procedures in order to provide true and fair view reports to the users. These results also support agency and accountability theory where auditor spends more time to investigate the weaknesses in the FSBs' financial statements. This leads to an increase in the ARL.

However, result of correlation between DAYS and firm size (SIZE) indicates that there is negative linear correlation. This relationship also can be proven through the study done by Carslaw and Kaplan (1991); Henderson and Kaplan (2000); Wermer et al (2000); Ahmed (2003); Ku Ismail and Chandler (2004) and El Banany (2006). Larger FSB tends to report quickly than other FSB due to good governance and strong internal control. Since FSBs are responsible for managing public fund, therefore FSB may receive high pressure from public and this will lead FSBs to provide timely reports. This finding supports hypothesis (H1) which has been discussed in the previous chapter.

Table 3 above also shows there is negative relationship between DAYS and leverage (LEV). This finding shows the FSBs with higher leverage tend to provide timely report

to the users. However, this finding is contrary to hypothesis (H3) and prior study by Carslaw and Kaplan (1991); Owusu-Ansah (2000); Boonlert-U-Thai et al (2002) and Conover et al (2007) where they found there is positive relationship between leverage and timeliness. On the other hand, negative relationship between DAYS and profitability (PROF) supports hypothesis (H2). According to Curtis (1976) and Kinney and McDaniel (1993) company with declining profit tend to have longer ARL. The same goes for FSBs where Malaysian taxpayers are more interested in reading FSBs' annual report as it discloses relevant information on disbursement of taxpayers' money (Tayib, Hugh and Ameen, 1999). Declining income of FSBs is a signal of management conflict in managing taxpayers' money and this requires AG to spend more time to conduct audit in order to maintain public confidence towards FSBs.

Furthermore, based on the correlation analysis above there is a negative linear correlation between SIZE and LEV, but positive linear correlation between LEV and AC. The result indicates when SIZE increases, LEV of the FSBs shall increase. Table above also shows there is no relationship between PROFIT and AC.

VII. CONCLUSION OF STUDY

Timeliness of financial reporting is important because it provides valuable information to the public. Since public is the main contributor to the government fund, they have right to access quality and timely information. Relevancy of the information will reduce due to increase in reporting lag. Thus the decision made by users might not be of superlative quality. This study extends prior research by examining whether size of statutory body, leverage, profitability and auditor's comment affect ARL of FSBs. The findings of this study provide new insight into the determination of FSBs audit delay. To conduct this study, a total of 92 FSBs have been selected. Result of the study indicates that range of ARL for FSBs from a minimum interval of 18 days to a maximum interval of 332 days. This study also shows there is an improvement of audit delay from 2008 to 2009. Finding from this study also agrees with prior research where auditor's comments affect the ARL (Lys and Watts, 1994). Furthermore, annual report of FSBs will be tabled in Parliament by respective Minister and public gives more attention to auditor's report because it reflects the government accountability. Thus, to provide quality information to the users, the auditor is required to carry additional audit procedures (Houghton and Jubb, 1999). FSBs size and profitability of the FSBs show negative relationship with ARL. This is due to strong internal control and good corporate governance (Carslaw and Kaplan, 1991).

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