THE IMPACT OF AUDITOR-CLIENT RANGE ON AUDIT QUALITY AND TIMELY AUDITOR REPORT

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Abstract

This study delves into the dynamic relationship between auditor-client proximity and its effect on audit quality and the punctuality of auditor reports within companies trading on the Tehran Stock Exchange (TSE). A comprehensive analysis was conducted on a sample of 108 businesses, spanning the years 2013 to 2019. Employing an innovative methodology, our findings reveal that the geographical distance between auditors and clients fails to exhibit statistically significant correlations with audit quality (Almagsoosi et al., 2022). Instead, our research emphasizes the crucial role of proximity in fostering productive conversations between auditors and clients, leading to more punctual audit reports. Notably, this study pioneers the investigation of the spatial interval between auditors and clients, marking a significant contribution to the field. By elucidating the implications of engaging nonlocal auditors, our research not only contributes to innovation but also introduces novel insights into the realm of audit quality and timely reporting practices, expanding the horizons of auditing research.

Keywords: Local Auditor, Audit Quality, Timeliness of Auditor Report

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1. INTRODUCTION

Some local investors, analysts, banks, fund managers (investment, cooperative), and market practitioners can profit from the information presented in the financial geography literature. It is possible that providing a sufficient reason could lower the cost associated with presenting information to local

shareholders. The auditing industry can also benefit from making use of geographical advantages. Most auditing work is done on-site at the client's business, where the client can better oversee the process. A local auditor's connection with a local client may need less time and travel than an out-of-state auditor's connection with a client. Long-term investments (Khalbas et al., 2018; Thammasiri, 2014; Jensen et al., 2013; Choi et al., 2012) have also become the primary topic of publications in the financial literature. According to these articles, lenders and local investors profit from loan and investment interest because information providers give benefits such as enhanced monitoring, corporate data observation, information access, cheaper costs, and access to insider knowledge. Where the demands of the region and location apply, the firm and the auditor should choose a local auditor-client connection over a distant one in the audit services market. Many firms, on the other hand, hire international auditors.

Companies may favor audit quality over audit costs which is why international auditors are prioritized over local auditors. They have three justifications for their actions:

1) the number of auditors should be limited;

2) local auditors can be hesitant to consider high-risk clients and therefore avoid performing certain tasks;

3) audit fees charged by foreign auditors may be less than those charged by local auditors of comparable caliber.

According to Thammasiri (2014), there are three situations in which the auditor-client distance negatively impacts the quality of the audit. To begin, local auditors will have an advantage in expertise over the company because they will have access to inside information that auditors from out of town might not. Secondly, local auditors can collect information about businesses with less time and money than would be required by auditors from outside the area. Czerney et al. (2019) claim that local auditors have an advantage in terms of expertise because of their established networks of contacts with company management. There could be concerns regarding auditor independence if local auditors have close relationships with the company's executives, giving them an edge in terms of specifics. To rephrase, an auditor's capacity to provide an objective assessment is impaired if he or she has personal relationships with the client that could be perceived as friendly (Chen et al., 2020).

Hasan et al. (2021) claim that two assumptions meant that local auditors were unable to approve high-risk businesses' financial statements. To begin, auditors charge more money for audits when there is a larger risk of fraud in the financial statements. Second, because of their familiarity with the area, local auditors are better able to identify risks than their out-of-town counterparts, who tend to exaggerate the potential consequences. Internal risk, control risk, and non-detection risk are all types of audit risk. That's why some small towns have started turning away risky businesses. According to research, audited financial statements are often the sole reputable source of information (Al-Taee & Flayyih, 2023; Haroon & Zaka, 2023; Hegazy & Ebrahim, 2022; Elbahar et al., 2021).

The purpose of this study is to acquire a better knowledge of the geographical advantages that may exist in the audit industry. This is accomplished by attempting to examine the geographical advantages.

This study addresses a significant need in the existing body of research by investigating how the proximity of auditors to their customers influences the quality of audits and the speed with which auditors communicate their findings to companies that are traded on the Tehran Stock Exchange (TSE). This research is significant because it offers insights into the auditing process, particularly in relation to the idiosyncrasies of the Iranian financial industry. These insights are the reason for the research's value. First and foremost, the purpose of this research is to provide answers to the following questions:

RQ1: Is there a correlation between auditors' and customers' distances and the results of the audit?

RQ2: Is the promptness of audit reports may be affected by the distance between the auditor and the customer?

The answers to these questions are what this study is all about, as they provide light on the function auditor-client relationships play in guaranteeing accurate and timely financial reporting. Not only do the results shed light on the dynamics between auditors and clients in worldwide financial markets, but they also have the potential to influence auditing procedures and legislation in Iran.

This study is structured as follows. Section 2 — a comprehensive literature review — synthesizes prior research and highlights existing knowledge gaps. Section 3 elaborates on the research methodology, offering insights into the analytical processes applied to the results. Section 4 presents the findings and engages in discussions regarding their implications. Finally, Section 5 draws the conclusions and recommendations for further research are presented.

2. LITERATURE REVIEW

There are a variety of considerations that go into selecting an objective auditor. According to Dickins et al. (2018), Czerney et al. (2019), Chen et al. (2020), Duh et al. (2020) and Sun et al. (2020), the right to appoint a competent auditor as a volunteer for the annual meeting rises in proportion to the company's size, debt, and payroll expenses. Thus, we take a look at what makes people pick an auditor from beyond their own area. Several studies have examined the correlation between auditor-client distance and audit effectiveness, including Khalbas et al. (2018), Jensen et al. (2013), and Choi et al. (2012). The results of the studies by Jabbar et al. (2021) and Kadhim et al. (2020) The presence of a local auditor, regardless of their position, significantly decreased the likelihood of a contract being signed with an auditor from outside the area. In addition, businesses whose reports are more accurate are less likely to use an auditor from outside the country, and those that do pay less (Abd Mohammed et al., 2022). Finally, selecting a local auditor has a positive and statistically significant effect on how quickly you receive your audit report.

In addition, the study's results show that neither the auditor's location nor the client's location has any appreciable effect on the quality of the audit.

Thammasiri's (2014) study results are included as well. Prove that it will be difficult to employ external auditors due to the presence of local BIG4 audit firms and industry-specific certified auditors. firms that are losing money, businesses that are receiving a continuous corporate audit report, firms that have lower earnings, and companies that have challenges with their internal controls are more likely to seek an auditor from outside the area. The entirety of the data points to the conclusion that businesses that face a greater potential for audit failure are more inclined to seek auditors who are based in distant locations. Finally, Duh et al. (2020) ruled that the costs of hiring an auditor from outside the area exceed those of using a local firm. This demonstrates that businesses that hire auditors from outside the region will not be able to save money on the audit. There may be a price difference between a non-local auditor and their client because of the auditor's lack of familiarity with the local market. However, academics are less likely to characterize the knowledge advantages of local auditors in terms of increased supervisory competence, reduced supervision costs, and high availability. The study's major goal is to evaluate the advantages of distance with respect to the accessibility of information. Multiple studies, including those by and have found a negative correlation between auditor and client proximity and audit quality.

Compared to their international counterparts, local auditors may have a leg up on the competition thanks to superior control abilities, the ability to observe subtle nuances within organizations, lower acquisition costs, or access to secret information. In addition, the work they do may lead to reduced fees for local auditors. However, auditor independence might be compromised by developing too close of a relationship with management. Companies are more likely to choose local auditors who can provide a knowledge advantage, and auditors may provide preference to local clients over those in other locations. Additionally, auditors should charge a higher audit price to clients based outside of the country. They should also be cognizant of the fact that auditor-client distance negatively correlates with audit efficiency. If the auditor's independence suffers due to physical separation from their clients, and if such factors lessen the auditor's knowledge advantage on the job. According to Alyaseri (2021), there is a correlation between an increase in audit tenure and an increase in the number of report failures. In addition, discovered that the first three years of a relationship between an auditor and a customer are the most susceptible to dishonesty. It would appear that worries regarding the independence of auditors have no effect on the effectiveness of audits.

The information contained in financial statements can be put to use in decision-making regarding matters pertaining to both the economy and finances. Users need to have access to such information to analyze the company's efficiency and financial health. According to research, audited financial statements are often the sole reputable source of information.

Because of their precision and timeliness, these two fundamental indicators are useful for corporate reporting. As the time for completion of the audit process (submission of the audit report) grows, the value of the information contained in the yearly report decreases.

With only temporary financial data accessible, one of the most significant qualities of information is timeliness, which means consumers may make a choice, assess, and explain prompt action on the connected concerns. In other words, before squandering the chance, financial records should be made available to consumers so that they may examine and make judgments. As a result, the data is older the closer it is to the time of the incidence.

As a result, we estimate that the auditor-client gap will be connected to the availability of timely reports and that the gap will grow as the audit report is delayed. This prediction is based on prior research (Khalbas et al., 2018; Thammasiri, 2014; Jensen et al., 2013; Choi et al., 2012). According to the study, local auditors may have a knowledge advantage over commercial businesses since they know the company's secret information, whereas non-local auditors may not have complete information about the company. Furthermore, whereas non-local auditors may invest more effort and time in gathering knowledge about the organization, local auditors may expend less effort and time. Local auditors also have the advantage of maintaining excellent ties with firm management. Local auditors will gain from information advantage if they have close contact with business management.

Thus, the hypotheses are as follows:

H1: There is a large inverse relationship between the distance between the auditor and the customer and the quality of the audit.

H2: There is a large inverse relationship between the distance between the auditor and the customer and the timely report.

3. RESEARCH METHODOLOGY

The research's goals are realistic, and its methods and quality standards are up to par. Methods of inductive inquiry are employed. Gather theoretical concepts and supporting documentation from print and online sources; apply inductive reasoning and appropriate statistical methods to either reject or confirm research hypotheses.

3.1. Data set and representative sample

Companies meeting the following criteria that were listed on the TSE between 2013 and 2019 make up the statistical population under examination.

A company's eligibility for inclusion in the study was contingent on its:

– being listed on the TSE prior to 2013;
– having a fiscal year end of March 20 and not changing it during the research;
– not being affiliated with financial intermediaries like banks and investment firms;
– having shares traded at least once during the year;
– having data available.

The data for this inquiry was gathered using a library-based strategy. This method relied on a random selection of documents for analysis.

Financial statements from selected members were retrieved from the TSE website and Rah Avaran-e Novin software and included in the sample papers for the current study.

In this study, several regression and logic operations are carried out with the help of the EViews 9 software. This software was utilized due to its appropriateness in econometrics, accounting, and financial analysis.

$$AQ = \beta_0 + \beta_1 Local + \beta_2 Size + \beta_3 Leverage + \beta_4 BookMK + \beta_5 ROA + \beta_6 InstOwner + \beta_7 BigN + \varepsilon \qquad (1)$$

$$ART = \beta_0 + \beta_1 Local + \beta_2 Size + \beta_3 Leverage + \beta_4 BookMK + \beta_5 ROA + \beta_6 InstOwner + \beta_7 IndepentDT + \beta_8 BigN + \beta_9 Officenatexp + \varepsilon \qquad (2)$$

3.3. Research variables

In this study, we focus on the audit quality and timeliness of the audit report as the dependent variable, and we use the following for the calculation.

A timely audit report (*ART*) is one that was completed before the end of the fiscal year.

In this study, the independent variable is the local auditor (*Local*), who is calculated in the following way: if the auditor and the client are physically located within 100 miles (161 km) of each other, then the value of the local variable will be 1.

Managed variables:
• *Size* equals the natural logarithm of the product of the company's size and its annual revenue.
• The ratio of total debts to total assets is the definition of *Leverage*.
• *BookMK* evaluates dividends at book value versus market value.
• Return on assets (*ROA*) is the profit ratio before deducting total assets for interest and taxes.
• The percentage of ownership held by institutional investors is denoted by *InstOwner* and

3.2. Study models

Model 1 is estimated to test *H1* in accordance with the studies by Khalbas et al. (2018) and Thammasiri (2014), in the current study auditor industry specialization and the audit quality requirements are financial restatements. Model 2 is used for testing *H2*. The equations of both models are presented below.

is calculated by dividing the number of shares held by institutional investors by the total number of outstanding shares.
• The percentage of the board that is unconstrained, shown by *IndepentDT* is the same as the total number of board members.
• If the auditor is a rank-and-file employee, then *BigN* = 1. Official Accountants Association member or A-rated auditor, otherwise 0.

4. RESULTS

This section will examine the proposed variables and study hypotheses. The *H1* is tested using logic regression, whereas the *H2* is tested using multiple regression.

4.1. Data description

Table 1 depicts the research variables' descriptive statistics. There were 108 businesses assessed in all. The time frame for this analysis is from 2013 to 2019.

Table 1. Descriptive statistics of the study variables are provided

Variable	Average	Median	Max.	Min.	Std. dev.	Skewness	Kurtosis	Normality
ART	74.946	74.000	155.000	17.000	28.382	0.002	1.848	0.000
Officenatexp	0.456	0.000	1.000	0.000	0.499	0.175	1.031	0.000
Restatement	0.786	1.000	1.000	0.000	0.411	-1.394	2.943	0.000
Local	0.676	1.000	1.000	0.000	0.469	-0.752	1.566	0.000
BigN	0.814	1.000	1.000	0.000	0.390	-1.615	3.607	0.000
BookMK	0.303	0.350	7.785	-9.997	1.102	-3.767	40.127	0.000
IndepentDT	0.654	0.667	1.000	0.000	0.208	-0.773	4.066	0.000
InstOwner	28.879	14.320	146.120	0.000	33.269	0.921	2.541	0.000
Leverage	0.650	0.613	3.060	0.145	0.321	3.074	19.311	0.000
ROA	0.100	0.096	0.629	-0.492	0.161	-0.090	4.055	0.000
Size	13.665	13.576	19.809	8.900	1.727	0.662	4.351	0.000

4.2. Investigating the initial hypothesis

The *H1* is tested using Model 1 of the investigation. The findings of Model 1's estimate of the study data

are presented in Table 2, with the dependent variable of auditor industry specialty serving as the focus of the analysis.

Table 2. Outcomes of Model 1 estimation on the research variables (Part 1)

Panel A: Main variables				
Variable	Coefficient	Std. error	z-statistic	Prob.
C	-146.516	67.622	-2.167	0.030
Local	0.161	0.199	0.808	0.419
Size	-0.708	0.100	-7.064	0.000
Leverage	-0.988	0.497	-1.988	0.047
BookMK	-0.317	0.135	-2.354	0.019
ROA	-0.571	0.832	-0.686	0.493
BigN	-0.577	0.214	-2.690	0.007
InstOwner	0.001	0.003	0.258	0.796
Fixed effects of year and industry	Controlled			

Table 2. Outcomes of Model 1 estimation on the research variables (Part 2)

Panel B: Statistical analysis			
LR statistic Prob. (LR statistic)	*Pseudo R²*	*Hosmer-Lemeshow (HL) statistic*	*HL significance*
193.175 (0.000)	0.209	16.579	0.035

Table 2 shows that both the Prob. (LR statistic) and the HL significance levels are lower than the critical value of 0.05.

It's a marker of the standard of the model. This shows that the model is valid, and the results may be trusted. This indicates that the auditor's industry focus is significantly correlated with the study's independent variables. The probability value for the independent variable, "use of the local auditor", is greater than 0.05, coming in at 0.419, according to the statistical study. Therefore, the *H1* is not supported; using a local auditor has no effect on the quality of the audit (the auditor's specialization in the industry). Results from a model for estimation in Table 3 display the results of the study's dependent variable financial restatement and Model 1 estimate.

Table 3. Results of the study's dependent variable

Panel A: Main variables				
Variable	*Coefficient*	*Std. error*	*z-statistic*	*Prob.*
C	136.721	71.673	1.908	0.056
Local	0.372	0.200	1.856	0.063
Size	0.162	0.060	2.697	0.007
Leverage	-0.168	0.460	-0.365	0.715
BookMK	-0.245	0.175	-1.404	0.160
ROA	-0.476	0.773	-0.616	0.538
BigN	-0.428	0.258	-1.661	0.097
InstOwner	0.000	0.003	0.067	0.947
Fixed effects of year and industry	Controlled			
Panel B: Statistical analysis				
LR statistic Prob. (LR statistic)	*Pseudo R²*	*HL statistic*		*HL significance*
20.574 (0.015)	0.029	5.614		0.690

From Table 3, it is clear that both the Prob. (LR) statistic and the HL significance are smaller than 0.05. This is a sign that the model is reliable. This shows that the model is valid, and the results may be trusted. The auditor's field of expertise correlates significantly with the study's independent variables.

The results of the statistical analysis show that the independent variable, using a local auditor, has a probability greater than 0.05 at 0.419. This result indicates that the hypothesis is not supported and that there is no correlation between using a local auditor and audit quality (as measured by the revised financial statements).

4.3. Investigating the auditor-client range on audit quality report

Model 2 is utilized to put the hypothesis to the test. The results of the Model 2 estimate using research data are shown in Table 4.

Table 4. Outcomes of Model 2 estimation on the research variables

Panel A: Main variables				
Variable	*Coefficient*	*Std. error*	*t-statistic*	*Prob.*
C	35.790	46.853	0.764	0.446
Local	-4.950	1.303	-3.798	0.000
Size	2.798	3.162	0.885	0.378
Leverage	10.110	5.405	1.871	0.063
BookMK	-1.623	0.621	-2.611	0.010
ROA	-21.838	6.468	-3.376	0.001
BigN	-3.807	1.912	-1.992	0.048
Officenatexp	-3.933	4.074	-0.965	0.336
IndepentDT	4.514	4.896	0.922	0.358
InstOwner	0.051	0.057	0.905	0.367
Fixed effects of year and industry	Controlled			
Panel B: Statistical analysis				
F-statistic	*F significance*	*Durbin-Watson stat.*	*R²*	*Adjusted R²*
9.763	0.000	2.115	0.774	0.862

5. DISCUSSION

The model is suitable for testing, and the findings may be believed because the value of Prob. (F-statistic) is now less than 0.05, whereas it was 0.000 earlier. Table 4, which shows the results of the statistical study, has these observations.

The value of the Durbin-Watson test was 2.115, and this number is considered to be an optimum value because it falls between the ranges of 1.5–2.5. This suggests that the time series values for this hypothesis sample do not suffer from the issue of autocorrelation. The value of the coefficient of determination, R^2, was 0.862, which indicates that the independent variable can explain 86.2% of the variation in the dependent variable. The value of the adjusted R^2 was 0.774, which indicates that the independent variable affects the variable that is being studied by 77.4%.

According to the findings of the statistical analysis, the value of Prob. for the independent variable, which is the utilization of the local auditor, is lower than 0.05, reaching 0.000. This indicates that the hypothesis is accepted, which denotes that there is a connection between the utilization of the local auditor and the delay in the issuance of the auditor's report. As a result of the fact that the value of the Coefficient is negative, we can conclude that this relationship is an inverse relationship. This indicates that the issuance of the auditor's report will be delayed further the more frequently the local auditor is called upon to perform auditing duties.

6. CONCLUSION

The purpose of this research is to measure the distance between auditors and their clients at companies trading on the TSE and to analyze how that distance affects audit quality and report timeliness. In sum, the findings highlight the significance of choosing a local auditor for producing an on-time audit report. The distance between the auditor and the customer does not appear to have any bearing on the quality of the audit. In contrast to Choi et al. (2012), our results are in line with those of Khalbas et al. (2018), Thammasiri (2014), and Jensen et al. (2013). There are significant differences between the two countries' financial systems and legislation, as well as the auditing standards used to evaluate firms' practices. The findings are consistent with those of Khalbas et al. (2018). Future research in this field should consider the incorporation of additional variables, such as industry-specific factors and regulatory changes, to gain a more comprehensive understanding of the relationships between auditor-client proximity, audit quality, and timeliness. Qualitative analysis and cross-cultural comparisons can provide deeper insights, while the effects of auditor specialization, client size, and technological advancements are promising avenues for further investigation. Longitudinal studies and industry-specific research would enhance our understanding of these dynamics. By addressing these areas, future research can contribute to a broader and more nuanced understanding of the intricate factors influencing audit quality and timely reporting.

Future recommendations focus on further understanding the connections between auditor-client closeness, audit quality, and the timely delivery of auditor reports, future research in this area should take into account the inclusion of additional variables, such as industry-specific characteristics and legislative changes. Understanding how the dynamics of various sectors are affected by regulatory shifts might yield useful information. Further, the qualitative features of auditor-client interactions and the impact of cultural variables on these relationships may be uncovered through qualitative analysis and cross-cultural comparisons, both of which provide prospective pathways for greater knowledge. There is promise in exploring how auditor specialty, client size, and technology developments affect auditing processes. The best way to get a handle on these intricate dynamics is to conduct longitudinal studies that monitor these factors across time, in addition to sector-specific studies. Future research can help shed light on the complex aspects that affect audit quality. As well as the future viewpoint of the current research that discusses the effects of the auditor client range on the quality of the audit might be used for the same approach with additional variables such as the gender of the client or auditor, and this would have an effect on the quality of the audit. The current strategy may be utilized along with a certain year for any period that was desired.

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