

# DETERMINANTS OF AUDIT FEES ACROSS CENTRAL AND EASTERN EUROPEAN COMPANIES BEFORE AND DURING COVID-19

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## Abstract

Relevant and faithfully represented financial information stands as the key determinant of efficient capital allocation in financial markets. The primary function of an audit is to diligently investigate financial information provided by a company, assuring users that it is relevant and faithfully represented, offering a true and fair view about the company's financial health. Central to this assurance is the determination of audit fees, which extends beyond mere monetary transactions. These fees, shaped by market conditions and audited company-specific characteristics, serve as a barometer reflecting the accounting quality of the audited company. Influenced by factors such as the company's size, complexity, industry risk, and market competition among audit firms, audit fees capture the intricacy of a comprehensive audit process. During periods of disruption, such as the recent COVID-19 pandemic, businesses encounter distinct challenges that reflect on audit process. This leads to fluctuations in the pricing of audit services, as auditors respond and adapt to the evolving market conditions. However, despite of vital role of audit fee as a measure of accounting quality, there is a gap in literature concerning audit fees in Central and Eastern Europe (Rewczuk & Modzelewski, 2020; Groff et al.,

2017), especially in the times of market turbulences, such as COVID-19 pandemic (Hategan et al., 2022; Al-Qadasi et al., 2023). To bridge this gap, this study was taken aiming to identify the determinants of the audit fee of companies in this region. Additionally, it incorporated COVID-19 effects comparing audit fees and their determinants in periods before and during COVID-19.

The research sample comprised company-level data for the years 2019 and 2021, collected from the Bloomberg database. Based on the availability of data, a total of 101 Central and Eastern European companies were examined in year 2019 and in 2021 this number increased to 203. The dependent variable in this study was the size of the audit fee, while independent variables included audited company-specific variables, such as size of the auditee, its number of employees, ratio of foreign revenue, net profitability, size of receivables, size of inventory, net debt, book-to-market ratio, current ration, return on assets, type of auditor's opinion, industry risk, and size of auditor, representing audit company characteristics. The econometrical research employed a modified model of Hribar et al. (2014), tailored to the situation and available data on Central and Eastern European companies. Ordinary least squares (OLS) regression was performed to determine audit fee variables for the pre-COVID-19 and COVID-19 periods. Descriptive statistics revealed that, on average, companies in the 2021 sample paid almost 270,000 euros in audit fees compared to 213,000 euros in 2019. In the pre-COVID-19 period, the significant positive variables affecting audit fees were the total assets of auditee and auditors belonging to Big4 companies, while the current ratio was a significant negative variable. Analysis of the year 2021 data indicated that the total assets of the auditee, ratio of the auditee's foreign revenue, auditee's number of employees and auditor's belonging to Big4 companies were significant positive determinants of audit fees. The significance of variables outlines that the increase in the auditee's size determined by total assets, increases the audit fee. Both the size of the auditee and auditor affiliation to Big4 were identified as key variables determining audit fees in previous studies (Lawal & Ibrahim, 2022; Kanakriyah, 2020). Similarly, the same two variables proved to be the key determinants in the pre-COVID-19 and COVID-19 periods in the study of Al-Qadasi et al. (2023). It highlighted that the size of the auditee (belonging to Big4) is the most significant determinant in both pre-COVID-19 and COVID-19 models and, therefore, has the largest effect on audit fees. This study brings new evidence to audit fee research, representing the findings on audit fee determinants in Central and Eastern European countries during times of market turbulences.

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