NETWORK GOVERNANCE AND AUDIT PRICING: EVIDENCE IN MALAYSIA

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ABSTRACT

The aim of this study was to examine the relationship between network governance represented by senior government officers of the audit committee (SGOAC) and audit fee. Knowledge distribution, economic returns, effective enforcement and compliance with environmental regulations can be acquired based on the social network theory. Hence, lower audit fees may be charged by the auditors to the company with the presence of a higher SGOAC as the information and knowledge gathered are based on their good network government connection. Analyses were conducted using data from 690 listed companies in the Bursa Malaysia in 2014. The Ordinary Least Square (OLS) regression method was applied to estimate the relationships between SGOAC and audit fee. The result shows that SGOAC has significant negative relationships with audit fee. Further analyses of the Big 4 auditor also show that lower audit fee charged in the number of SGOAC. It shows that it is not because of lower audit quality that resulted in the negative relationship between the SGOAC and audit fee. The evidence suggests that lower audit fees were charged by the auditor due to network governance, thus, network governance has a good impact on the company. Hence, the results provide initial evidence on the relationship between SGOAC and audit fees in business prospects in Malaysia.

Keywords: Senior Government Officers of the Audit Committee (SGOAC), audit fee, social network theory and Malaysia.

ABSTRAK

Tujuan kajian ini dijalankan adalah untuk mengenalpasti hubungan antara rangkaian tadbir urus korporat yang diwakili oleh Pegawai Kanan Kerajaan bagi Jawatankuasa Audit (SGOAC) dan yuran audit. Pengedaran pengetahuan, pulangan ekonomi, keberkesanan penguatkuasaan dan pematuhan kepada peraturan alam sekitar boleh diperolehi melalui Teori Rangkaian Sosial. Oleh itu, yuran audit yang lebih rendah mungkin dicaj oleh juruaudit kepada syarikat dengan kehadiran SGOAC yang lebih ramai sebagai maklumat dan pengetahuan yang diperolehi melalui hubungan baik mereka dengan pihak kerajaan. Analisis yang telah dijalankan dengan menggunakan data daripada 690 buah syarikat yang tersenarai di Bursa Malaysia pada tahun 2014. Kaedah regresi *Ordinary Least Square* (OLS) telah digunakan untuk menganggar hubungan antara SGOAC dan yuran audit. Keputusan menunjukkan bahawa SGOAC mempunyai hubungan negatif yang signifikan dengan yuran audit. Analisis tambahan pada sampel juruaudit Big 4 juga menunjukkan bahawa yuran audit yang lebih rendah dicaj dengan bilangan SGOAC yang ramai. Hal ini menunjukkan bahawa ia bukan disebabkan oleh kualiti audit yang rendah yang mengakibatkan hubungan negatif antara SGOAC dan yuran audit. Penemuan ini mencadangkan agar yuran audit yang rendah akan dicaj oleh juruaudit kepada tadbir urus rangkaian, hal ini kerana ia memberi kesan yang baik kepada syarikat. Justeru, dapatan ini menunjukan bukti awal tentang hubungan antara SGOAC dan yuran audit dalam prospek perniagaan di Malaysia.

Kata kunci: Pegawai Kanan Kerajaan bagi Jawatankuasa Audit (SGOAC), yuran audit, Teori Agensi, Teori Rangkaian Sosial dan Malaysia.

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TABLE OF CONTENTS

CHAPTER 3: HYPOTHESIS DEVELOPMENT AND METHODOLOGY

CHAPTER 4: FINDINGS AND DISCUSSIONS

List of Appendix

List of Tables

List of Figure

List of Abbreviations

GLCs	Government Linked Companies
Non-GLCs	Non-Government Linked Companies
OLS	Ordinary Least Square
SGO	Senior Government Officers
SGOAC	Senior Government Officers of the Audit Committee
SPSS	Statistical Package for Social Science
UUM	Universiti Utara Malaysia
VIF	Value inflation Factor

CHAPTER 1

INTRODUCTION

This chapter discussed the research interest, background, problem statement, research question and research objectives, significance and organisation of the study.

1.1 Research Interest

A distinctive feature of Malaysia includes the close bond between big company and government. Senior government Officers (SGO) represents the characteristics of network governance (Hamid, 2011), which argued implement a critical agenda that drives the economic growth of the nation. Their appointment as directors in many Malaysian public listed companies, whether in GLCs and Non-GLCs signifies those characteristics. Their close connection with regulators such as lawmakers or government influenced network governance characteristics.

On the other hand, Malaysia is a country that different from most other countries where there is intertwining between multicultural ethnicities and economic interest in Malaysia landscape. Gomez and Jomo (1999) stated that close relationships between economic function and racial have shaped the capital market in Malaysia. Stenson (1980) found that the Chinese monopolise on the business sector, although the Malays dominated the political context in the country. In another point of view, the Chinese led Malaysian economic wealth, though the political influence is distributed collectively amongst ethnic groups (Abdul-Wahab, Mat Zain & James, 2011). This inequality of capital distribution has driven by the introduction of the New Economic Policy (NEP) in 1970 and government link companies later in 1980's. Earlier, from the time of race riot in May 1969, the government has supported certain Chinese and

Malay companies through providing investment capital at favoured rates and channelling contracts to these companies (Bliss, Gul & Majid, 2011).

Social network theory explained the influence of the board establishment and structure in a company (Lynall, Golden & Hillman, 2003). Based on pre-existing relationships, social network theory reflects the expected route to obtain company resources. Granovetter (1985) found that stable and preferential social link influenced and support a company degree in economic activities. Through social network, a company can resolve problems in terms of poor entrepreneurial organisation resources by forming a network exchange structure through critical resource suppliers.

Currently, there are many senior government officers appointed as the board of director in Malaysia public listed companies. Nevertheless, it is not known whether their nomination as board members would help in reduce the audit works and lower down the audit pricing due to limited studies conducted related to senior government officers of the audit committee (SGOAC) and audit fees.

1.2 Background of the Study

Network governance relationship with audit pricing in public listed companies in Malaysia has become the main focus of the study. Powell (1990) found that intercompany coordination or known as network governance involved with "distinct of the form of coordinating economic activity" which opposite with markets and hierarchies. Hence, network governance was considered as coordination of the informal social system instead of bureaucratic arrangements within companies and formal contractual relationships between them (Jones, Hesterly & Borgatti, 1997) due to uncertain and competitive environments for complicated products coordination and service.

Distribution and acquisition of diverse types of knowledge and information system in the company increase the collaborative control process through the social network (Schuler & Decker, 2003; Crona & Bodin, 2006; Issac, Erickson, Quashie-Sam & Timmer, 2007). For example, senior government Officers (SGO) can acquire critical information resources for companies economic benefits through the social network established on prior relationships.

In addition, Dedeurwaerdere (2007) argued that network governance led to efficiency for an organisation through knowledge acquirement and decentralised problem solving where the existence of collective solutions for global problems in diverse self-regulated sector activities improved the effectiveness. In contrast view, Hamid (2011) stated that development and application of unique agenda are part of network governance in purpose to realise certain objectives.

Overall, it can be concluded that individuals, organisation and company using network governance in order to compete and retain in current challenging and competitive environment. Focusing on the company, board of directors specifically will exchange information among themselves to achieve certain goals.

1.3 Problem Statement

In the study, senior government Officers of the audit committee (SGOAC) is defined as a person who is retired or currently serving as the senior officers in government division and also hold a position as audit committee member of a particular company. Nowadays, there are many senior government officers appointed as board members in the public listed companies (PLCs). Their appointment as board members may be influenced by their close connection with the government and legislators.

The example of appointment senior government officers as the board of director includes the nomination of former Inspector General Police Malaysia as the board of director and Vice Chairman of Genting Berhad, an entertainment and gaming company (Hamid, 2011). Besides, another example includes the former Chief Defence in Malaysia Armed Forces also selected as Directors cum Chairman and audit committee member in Ajinomoto, a food producer company. Moreover, under the context of performance, Hamid (2011) suggested that network governance represents by senior government officers also improves the company performance. However, it is not known whether their appointment as board members would contribute to the reduction of audit works and lower down the audit fees as there is no specific study conducted related to SGOAC and audit fees.

The study expected that the presence of SGOAC as the board member would reduce the audit fee due to the knowledge distribution and information gathered by network governance through social networks. Consistently, Liebeskind, Oliver, Zucker and Brewer (1996) mentioned that social networks under network governance are a group of individuals that exchanges based on shared norms caused by trustworthy behaviour.

In addition, Jaffee (1995) mentioned that audit fee is categorised as monitoring cost under transaction cost. Furthermore, Jones et al. (1997) found that transaction cost reduces through a social mechanism in network governance. This has triggered the issue of whether network governance plays by SGOAC helps auditor works, thus, reducing the audit fee.

While there are numerous studies related to the audit committee and audit fee, there are limited studies that particularly examined the association between senior government officers of the audit committee (SGOAC) and audit pricing. Feng, Sun

and Tong (2004) had conducted the performance of government linked companies (GLCs) and Non-Government Linked Companies (Non-GLCs) in Singapore environment. Similarly, Ang and Ding (2006) also conducted Singapore GLCs and Non-GLCs performance. Meanwhile, only Hamid (2011), reviewed the network governance of GLCs and Non-GLCs in Malaysia. Both earlier studies conducted similar research with the latter study but with different context. Hence, the study investigates the effect of network governance represented specifically by the SGOAC and its effect on audit pricing in Malaysia. Therefore, further insight on the association of network governance represented by the SGOAC and audit pricing is expected to be derived from the study.

1.4 Research Questions

A research question is formulated based on the research problem. The research question is as follows:

1. Is there any significant relationship between senior government officers of the audit committee and audit pricing in Malaysia public listed companies?

1.5 Research Objectives

The main purpose of the study is to examine the effect of network governance on audit pricing in public listed companies in Malaysia. Hence, the study specifically investigates:

1. The relationship between senior government officers of the audit committee and audit pricing.

1.6 Significance of the Study

Based on prior literature, the study can be considered as the first study to investigate the relationships between senior government officers of the audit committee (SGOAC) and audit pricing. Prior studies showed that there is limited understanding of network governance. Jones et al. (1997), stated that network governance is poorly understood although it is progressively significant.

In Malaysia, previous studies related to government and audit fees mostly focused on the political connection, corporate governance and audit fees. However, there is no studies have been carried out on SGOAC and its relationships with audit pricing in Malaysia. However, there was a study that investigated the link between senior government officers (SGO) and performance in Malaysia. The study by Hamid (2011) examined the link between senior government officers with performance particularly in GLCs and Non-GLCs in Malaysia.

Moreover, there are few studies examined senior government officers related to company performance in Singapore. Thillainathan (1999) stated that before the two countries split in 1965, Singapore was once part of Malaysia. Therefore, a social pattern such as three main races comprised of Malays, Chinese and Indians exist in both countries. Besides, both countries also have their GLCs represented by the SGO. A research conducted by Ang and Ding (2006), found that GLCs in Singapore perform greater than Non-GLCs under Singapore Exchange's main board. Likewise, Feng et al. (2004) investigated GLCs and Non-GLCs in Singapore provide the same results in the year between periods from 1964 up to 1998.

Past empirical studies mostly explored on political connection and audit fee. For instance, Blis et al. (2011) stated that the independence of audit committee that

demands a higher quality audit and led to higher audit fee is found weaker for companies with a political connection. In addition, Abdul-Wahab et.al (2011) found that there are positive relationships between audit fees and politically connected companies in Malaysia. Hence, it is expected that the findings of the study on the association between SGOAC and audit pricing can contribute to the current understanding of network governance and audit fee.

Furthermore, the findings of the study also expected to provide more evidence or be used as the reference to the body of knowledge, regulators, government and practitioners on network governance understanding and its relationship with audit pricing.

1.7 Scope and Limitation of the Study

The investigation on the relationship of senior government officers of the audit committee (SGOAC) and audit pricing is the main scope of the study. Hence, the independent variable of the study is SGOAC whereas audit pricing signifies as the dependent variable. There is a methodological limitation to the design used in the study, as the study only employ a one-year data of companies listed on Bursa Malaysia (which is the year of 2014) as a cross-sectional data.

The year 2014 is chosen as a sample in order to get the latest number of companies after the election year in 2013 since SGO (senior government officers) close relationship with government and they might relate with government party election.

1.8 Conclusion

This chapter summarised the background of the study, where there is limited study been developed related to network governance and audit pricing. Overall, only several studies highlighted senior government officers and its association with the

performance which only took place in Malaysia and Singapore since both countries are quite similar in terms social form such as ethnicity. The chapter further clarified that there are limited studies conducted on senior government officers that also hold as part of the audit committee and its association with audit pricing, though many government officers been appointed as the board of directors in Malaysia public listed companies. Likewise, the objective and research question of the study discussion related to network governance and audit pricing. In addition, this chapter also includes the scope and significant provided by the study.

1.9 Organization of Remaining Chapter

The remainder of the study is organised as follows. The second chapter discussed the background of the study, theoretical framework and hypothesis development. The third chapter provided the research methodology, followed by the fourth chapter where the study discussed the results. The last chapter concluded the study by summarised the main findings including their implications and limitation.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

This chapter described the relevant literature on network governance, audit committee and audit fees which emphasized on determining the factor of audit pricing.

2.2 Network Governance

There are few definitions provided by scholars on network governance. Some scholars provided different terms for network governance with partial meaning. Among the terms included "network form of organisation" (Powell, 1990), "alliance capitalism" (Gerlach & Lincon, 1992), "business group" (Granavetter, 1995) and "social networks" (Liebenskind et al., 1996). In another point of view, network governance signified as natural or informal social mechanism that led to intercompany coordination which totally opposite with company that applied bureaucratic structures and official contractual relationships between them (Gerlach, 1992; Nohria, 1992).

Overall, a complete definition of network governance is provided by Jones et al. (1997), where it comprised terms such as "persistent", "select", "structured", "implicit and open-ended contracts" which can be referred to Table 2.1. The term "select" defined that network members usually exchange among each other but not often with other members. Thus, the network members do not comprise the whole industry. Meanwhile, the "persistent" clarified that repeatedly, the network members worked with each other over time, hence, instead of a static unit, network governance is an active process unit. In addition, the term "structured" described that exchanges among network members are designed rather than random or constant. Finally, the "implicit

and open-ended contract" referred that adapting, coordinating and safeguarding exchanges do not derive from authority or legal contracts, yet, formal contracts might emerged between some members but not apply to all members. Table 2.1 exhibits some terms and partial definitions of network governance suggested by scholars.

Table 2.1 Different Terms and Explanation on Network Governance

Scholars	**Terms**	**Explanation on Network Governance**
Powell (1990)	Network forms of organisation	Independent flow of resources, mutual lines of communication
Dubini & Alrich (1991)	Networks	Relationships between a person, groups and organisation
Larson (1992)	Network organisational forms	Long term recurrent exchanges that generate interdependencies rely on combinations of obligations, expectations, reputations and reciprocal interest
Liebeskind, Oliver, Zucker & Brewer (1996)	Social networks	A group of individuals that exchanges only through common norms of trustworthy manners
Jones, Hesterly & Borgatti (1997)	Network Governance	Select, persistent and structured set of autonomous companies and non-profit agencies engaged to create product or services based on implicit and open-ended contract for environmental uncertainty adaptation and to safeguard exchanges

Source*: A General Theory of Network Governance: Exchange Conditions and Social Mechanism (Jones et al., 1997)*

Establishment of network governance further explained by Jones et al. (1997) which mentioned that network governance is important as it utilised social network theory and transaction cost economics (TCE). Three exchange conditions under TCE perspective comprised of uncertainty, asset specify and frequency, determined which governance form is more efficient. However, complications of adaptation, managing and safeguarding need to be highlighted effectively for a governance system to occur and develop (Williamson, 1991). Therefore, Jones et al. (1997) move beyond TCE by added complex task conditions that triggered the emergence of network governance. Thus, the existence of network governance thrive by four exchange conditions consist of 1) environment uncertainty, 2) task complexity, 3) frequency and 4) asset specify, determined the most effective governance form.

Environment uncertainty further described by Williamson (1991) which explained that because there is uncommonly stable and unpredictable environment, adaptation emerged due to environmental uncertainty which is the "central problem of economic organisation. Similarly, Miliken (1987) argued that the inability of individual or company to predict future events indicated "environmental uncertainty". Understanding the source of uncertainty is very crucial, as these can decide types of governance need to be used in purpose to manage and safeguard exchanges. Suppliers, customers, competitors, regulatory agencies, financial markets caused this uncertainty (Miles & Snow, 1978).

In addition, tax complexity comprised of the level of difficulty in identifying and manage tasks which already embedded in a company and struggle in acquire outside resources. Likewise, a number of different specialised inputs need to be completed for a product or service referred to "tax complexity". Increased scope of activities, the

number of business functions needed, the number of product produced, or number of differ market served led to differing specialist and input (Killing,1988).

Furthermore, the frequency is also significant for several reasons (Williamson, 1985). First, frequency help in transmitting tacit knowledge in customised exchanges mainly for specialised process or knowledge. Second, the foundation for a social mechanism to adapt, manage and safeguard exchanges happened efficiently if the interactions in established conditions for relational and influenced structural done frequently. Third, cost efficiency emerged in using specialised network governance structure through frequent interactions. The unique social environment and uncertainty of the Bumiputra business agenda resulted to the implementation of New Economic Policy (NEP) in 1971, Industrial Coordination Act (ICA) in 1975 and followed by formation of government linked companies (GLCs) reflected in Malaysia (Hamid, 2011). The enactment of NEP, ICA and GLCs that in purpose to assist Bumiputra in business, triggered the formation of network governance in Malaysia.

2.2.1 Senior Government Officers (SGO)

The appointment of senior government officers (SGO) as the director explained the characteristic of network governance based on their close connection with government or regulators. As mentioned earlier in Section 1.3, the former Inspector General Police in Malaysia has been appointed as the board of director and Vice Chairman of Genting Berhad, an entertainment and gaming company (Hamid, 2011). Another examples, include the former Chief Defence in Malaysia Armed Forces also appointed as Directors cum Chairman in Ajinomoto, a food producer company.

Currently, limited studies been made on SGO. Only Feng et al. (2004), Ang and Ding (2006) examined the relationships of GLCs (represented by SGO) and performance in

Singapore since the country GLCSs are alike with Malaysian GLCSs which included SGO as representative (Hamid , 2011). Both studies concluded that GLCs performed better than Non-GLCs in that region. Meanwhile, in Malaysia, only Hamid (2011) investigated the relationships between SGO and performance where the result showed that SGO contribution enhances more in Non-GLCs performance than in GLCs. The study goes further by investigated SGO who also hold as the member of the audit committee in companies and its relationships with audit pricing. As audit committee represents as part of governance control in companies, it is interesting to know how SGO as audit committee gives effect to audit pricing.

2.3 Audit Committee

To date, there is no prior study conducted specifically on senior government officers of the audit committee (SGOAC). Hence, the study only provided information on the common roles done by audit committee member in the company.

Audit committee plays a major mechanism among management and auditor in terms of communication and negotiation of terms for audit conduct purposes. Similarly, audit committee acts as a communication link between governing body, auditor and management (Salleh & Haat, 2014). Hossain and Khan (2006) defined audit committee as subcommittee in representing the board of directors that provided arrangements for the audit. Basically, three main responsibilities of audit committee fall under audit, internal control and financial reporting. Audit committee needs to ensure that there is sufficient business risk addressed by the company's internal and external audit. Under internal control, audit committee needs to guarantee that the internal controls are suitable to addressed business risk. Meanwhile, audit committee also needs to review company financial reports (Vanasco, 1994). Similarly, audit committee needs to meet

with internal financial managers and outside auditors of a company to oversee the financial statement, audit process and internal accounting controls of the company (Woidtke & Yeh, 2013).

Vanasco (1994) found that audit committee rapidly gaining acceptance, yet, are not widespread practice in Malaysia during 1990's. However, the revised of the Malaysian Code on Corporate Governance (MCCG) in 2007 has strengthened the regulations on audit committee role in ensuring that audit committee has an effective check on company management (Salleh & Haat, 2014).

As a monitoring role, tremendously regulators has highlighted the importance role of the audit committee. Audit committee represents as one of the reliable custodian of the public interest through competent, committed, independent and tough-minded characteristic (Levvit, 2000). Another important characteristic that needs to be possessed by audit committee is financial expertise. In this context, all public companies in the United States are required to disclose whether they have a financial expert on their audit committee which has been highlighted as most controversial provisions in Sarbanes-Oxley (Defond, Hann & Hu, 2005). In addition, the audit committee is regarded as financial expertise if their biographical information encompasses of accounting experience, experience in preparing financial statements and as financial statement expert utilise (Badolato, Donelson, & Ege, 2014).

2.4 Audit Pricing (Supply versus Demand Perspectives)

Simunic (1980) have started the study on audit pricing by creating a model which includes factors such as client size, complexities and risk to describe the variation in audit pricing. The cost associated with audit service which demanded by the client is defined as audit fee (Simunic, 1984). Similarly, Solatni (2007) described audit pricing

as the cost implies on the audit to address an opinion on the conformity of the financial statements.

Supply and demand side perspective provide a clearer picture on audit pricing. Carcello et al. (2002), argued that auditors are expected to "minimise total cost by balancing their resource cost (cost of performing more audit work) and their expected future losses from legal liability. These represent supply side perspective where audit fees are seen as a function of an auditor assessment of the overall audit risk. Tsui, Jaggi and Gul (2006), explained that auditor has a tendency to view corporate governance as the main internal control mechanism that influences nature and range of audit test under supply side perspective. High-quality accounting information achieved resulted from strong corporate governance mechanism. Hence, strong corporate governance reduces auditor's evaluation of audit risk and consequently results to less audit test and less audit pricing. Similarly, Yatim, Kent and Clarkson (2006) found that reduction of the audit effort from auditor resulted from strong corporate governance that reduces control and inherent risk. If good corporate governance can become a substitute to external auditing, a negative relationship between audit fees and governance mechanism is expected, hence, led to the reduction in audit pricing (Hay, Knechel & Wong, 2006). Thus, these supply side perspective and the nonappearance of strong demand side effect provide the prediction of a negative relationship between corporate governance and audit fee (Abdul-Wahab et al., 2011).

In contrast, demand side perspective of audit pricing suggested that the existence of corporate governance provide higher audit pricing (Johl, Subramaniam & Zain, 2012). Hence, demand side resulted from a positive relationship between corporate governance and audit fee (Hay et al., 2006). Usually, companies with strong corporate

governance mechanism comprised of independent, quality and expert board requested a higher quality audit and led to higher audit fee.

2.5 Determinants of Audit Pricing

There are various attributes that determine the audit pricing. Among them includes the auditor background and qualification, the company size in terms of total assets, the complexity of the client and also the business risk. Customer size, the complexity of the client, customer profitability, audit risk in overall and market share degree competition specified the audit fee charged to a company (Hay et al., 2006). Thus, higher audit fee charged to a company with a higher specification. Audit pricing is mainly been derived by the number of direct, billing rate adjusted labour hours devoted to the audit (Davis, Ricchiute & Trompeter ,1993).

2.5.1 Size

Simunic (1980) argued that size expected to have positive relationships with audit pricing. The size is usually measured by total assets and some studies use the revenue to determine size. The natural logarithm on the raw data is used to transform the size measure to develop linear relationships with audit fee. Any model of audit fees expected to indicate that size is an extremely crucial explanatory variable. Simunic (1980) and Francis (1984), found that more audit test needed for the larger company, in turn, led to higher audit pricing.

2.5.2 Complexity

According to Hackenbrack and Knechel (1997), time consume and more workload is expected from an audit if a client or a company is more complex. There are numerous ways on how to measure complexity. Among the most common indicator for complexity includes the number of subsidiaries, the number of foreign subsidiaries and

proportion of foreign assets (Hay et al., 2006). Thus, the more time and manpower required to complete the audit engagement, the higher audit pricing will be charged.

2.5.3 Leverage

The risk of a client failing also measured by leverage, which possibly exposed the auditor to loss (Simunic, 1980). Two most typical proxies for leverage included debt to total assets ratio and quick ratio (Hay et al., 2006). Positive association emerged between debt ratio and audit fee. Meanwhile, quick ratio and audit fee also seemed led to negative relationships. Similarly, Low, Tan & Koh (1990) claimed that audit fee and debt ratio provide positive relationships.

2.5.4 Auditor size

Big Four's auditor comprised of Ernst & Young, PriceWaterhouseCoopers, KPMG and Deloitte. A higher audit fee is expected when the auditor is known in terms of the brand name such as Big Four's company with higher audit quality. In addition, Big Four's are the biggest audit company in the world, hence, their expertise and financial strength gave them the opportunity to deliver higher quality audit (Che-Ahmad, Shafie & Yusof, 2006). Prior studies provide positive relationships between Big Four's company and audit fee (Rose, 1999; Che-Ahmad & Houghton, 2001).

2.5.5 Ethnicity

Yatim et al. (2006) and Gul (2006) found that Bumiputra CEO in Malaysia usually lacks in monitoring which led to greater scrutiny, hence, more time-consuming in audit works compare to Non-Bumiputra CEO companies. In contrast, Chinese business company might influence the different level of agency problems and risk. Chinese business structures and practice are quite diverse than Bumiputra and foreign controlled company. Lower audit fee paid by the Chinese-controlled company due to

less agency conflict, thus, less operational risk and lower extension audit. In addition, higher audit fees paid by foreign-controlled companies as high audit quality is needed due to the high level of monitoring demand and to diminish the problem of parent companies located far away (Che-Ahmad & Houghton, 2001).

2.6 Audit Committee and Audit Pricing

At the moment, there is no prior research conducted on senior government officers of the audit committee (SGOAC) as mentioned earlier in Chapter 1. Therefore, the study intended to bridge the gap by providing the link between the audit committee and audit pricing as well as to provide more insight to previous research.

Collier and Gregory (1996) found that two possible relationships between the audit committee and audit fee. Additional work might require by the audit committee in order to satisfy their own requirement in the case of the audit committee are likely to demand a higher quality of the audit. An example includes when audit committee set a lower level of materiality limits which led to further audit testing or increase in auditor hours. Higher audit fee also emerged due to the prevention of low balling or fee cutting by audit committee which lower audit fee offered by another auditor than current auditor been rejected.

Besides, the relationships between the audit committee and audit fee might be negative. Effective systems resulted from audit committee roles which to review the internal control contributed to lower audit fees. Basically, deteriorate of effective internal control system increased the planned audit hours (Kaplan, 1985). Thus, audit fees increase due to failed in the internal control system which supposed to be held by

the audit committee. Hence, improve in internal control reduced audit hours and audit pricing. Wild (1994) found that after the formation of the audit committee, the earnings is significantly more informative. Reduce in audit fee happened from the rise of audit efficiency which resulted from less disagreement between auditor and directors. Higher quality financial reporting directed to lower audit risk possibility and lower sample size, thus, provide higher audit efficiency.

2.7 Conclusion

This chapter has provided a summary of relevant studies conducted by the prior researcher on network governance, audit committee and determinant in audit pricing. The studies on audit pricing have been conducted extensively by the previous researcher but there are fewer studies on network governance and limited published studies conducted on senior government officers of the audit committee and its association with audit pricing. The following chapter provided discussion on method use and hypothesis development in the study.

CHAPTER 3

HYPOTHESIS DEVELOPMENT AND METHODOLOGY

This chapter outlines and presents the hypothesis development that is eventually tested and focus in detail on the senior government of the audit committee (SGOAC) and audit pricing. The first section of the chapter discussed a social network theory and a theoretical framework developed. Finally, the chapter provided the method used in the study with the conclusion.

3.1 Social Network Theory

Brass, Butterfield and Skaggs (1998) found that a social network is a set of actor and the set of ties represented by some relationships or lack of relationships between the actors. Dunn (1983) defined social network theory as the nature of knowledge process which knowledge is acquired through social relation. Tichy, Tushman and Fombrum (1979) stated that organisations in social network approach are seen as a system of the object that includes people, groups and organisations linked together through a variety of relationships in a society. Burt (2000) found that network connections that include social capital which provides values such as economic returns are among the principle of the social network. Hence, it is assumed that social network is some sort of relationships between the actors such as people, group and organisation in a society which provides values such as economic or knowledge returns.

Under the context of governance, Scholz and Wang (2006) claimed that social network provides effective enforcement and compliance with environmental regulations than the existence of formal institutions. Effective enforcement and compliance with environmental regulations than the existence of formal institutions emerge through

social networks. Collaborative governance process can be improved through the assistance to the generation, acquisition and distribution of different types of knowledge and information from the management through the social network (Crona & Bodin, 2006; Issac, Erickson, Quashie-Sam & Timmer, 2007; Schuler & Decker, 2003).

In addition, Birley (1986) and Khurana (2001) revealed that social network plays a significant role in the formation of the board in the company. This is supported by Granovetter (1985) that there is an influence of social networks in economic actions such as how the economics action been informed, embeddedness and enables by the stable and social relations preference network. Besides, individual with known reputation trusted informants that have dealt with another party which is believed trustworthy and depends on ones' owns past information to deal with a specific person, preferred by the managers on board formation and composition (Gulati & Gargiulo, 1999). Social network theory is found to consider the predictable path (based on pre-existing relationships) to acquire resources (Lynall, Golden & Hillman, 2003) such as knowledge and information from the government. Consistently, Larson (1992) stressed that the importance of network formation on reputation, trustworthy, mutuality and reciprocity interdependence emphasises by social network theory.

Through strategic benefits required from enhancing network exchange structures with outsiders that recognised as important resources dealers, the resource poor in the company would able to be improved. Thus, relationships from social network can provide new company in its target market. In the study, senior government officers are reflected as outsiders who have critical resources of information on the board through their connection that may improve the company's opportunity in terms of lower down

the audit fee and also act as the representative of the government to ensure compliance with environmental regulation. In addition, since senior government officers of the audit committee (SGOAC) have an easy access to top officers in the government, the knowledge and information can be distributed to the company to reduce the auditor work which led to lower audit fee. Hence, it is predicted that the presence of senior government officers that hold the position as audit committee might lower down the audit fee. This is due to the fact that they are chosen and appointed as board member cause by their merit and seniority with a good reputation previously in the government as well as been offered with higher remuneration (Hamid,2011).

Increasing in strong governance mechanism would lower down the audit fees since SGOAC were handpicked instead of felt that they been appointed as director and offered with good remuneration. SGOAC social network with the government may lead to the reduction in audit fees charged to company cause by their critical resources such as knowledge and information. This is consistent with the supply-side perspective of audit fee which through strong governance mechanism, audit risk reduces and lowers down the audit fees.

3.2 Theoretical Framework

Further explanation on the theoretical framework developed in the study describes by network governance.

3.2.1 Network Governance

New Economy Policy (NEP), Industrial Coordination Act (ICA) 1975 and the formation of government-linked companies (GLCs) by Malaysian government best described the concept of network governance in Malaysia. NEP has been established in 1971 to restructure society through eradicate the identification of race with the

economic role and to eliminate poverty. Bowie (1988) stated that to reach NEP's goal, the government establish the public enterprise and joint public-private companies to advance Bumiputra's business. In another hand, Hensley and White (1993) argued that the function of NEP is to equally allocate wealth distribution among Malaysia society.

In addition, Industrial Coordination Act that was presented in 1975 delivers a mechanism for the enhancement of Bumiputra's equity ownership in public listed companies (PLCs). Industrial Coordination Act requires Companies with equity exceeded a specific limit that listed in Kuala Lumpur Stock Exchange, to sell 30 percent of their shares to Bumiputra. Then, the government institutional investor or other Bumiputra trust funds normally bought the 30 percent stakes on behalf of the Bumiputra. Until the Bumiputra is ready to purchase, the agencies would hold the shares.

In early 1980's, government-linked companies (GLCs) were formed based on the enormous government involvement in corporate sectors such as wholly owned government enterprise and joint ventures in private sectors. The New Economic Policy (NEP) objectives and spur in Malaysia economic activities were seen to be accomplished through the establishment of GLCs. However, Non-Bumiputra seemed to be left alone struggle for their survival in terms of structuring their companies, concreating shareholdings and cross-shareholding, yet, Bumiputra are protected under NEP umbrella.

Hence, the enforcement of law and order might be impaired by NEP as the ownerships delivered to a particular group of shareholders rather than competitively realised (Porta, Lopez-de-Silanes & Shleifer, 1999). Network governance also seems emerged in Non-GLCs as they also seemed to appoint senior government officers as part of

their directors to sustain in the business. These selected directors would act as individuals that supply external resources for the companies.

The application of NEP and GLCs establishment were view as network governance form as the government need to pool all of its resources for networking to encourage the accomplishment of NEP objectives. The process includes redistribution, corporatisation and privatisation the NEP policies and the government control all critical decision on all matters. It is noticed that network governance not only helpful in the NEP and ICA related with GLCs but in Non-GLCs as well. Hence, it can be concluded that network governance supports and might emerge in all Malaysian public listed companies.

Hamid (2011) proposed that network governance comprised of selecting, joint collaborating and appointment directors and top officers is with the aim to assist the company in adjusting with environmental possibilities and to directs and protect exchanges so that desired objectives can be realised. "Selecting" means that the network company only exchanges sources among each other and rarely with others. Network members repeatedly work with each other over time reflects "joint collaboration" terms. "Appointment of directors and top officers" define the appointment a group of people such as directors and managers that are connected with GLCs group. Generally, it can be summarised that network governance in Malaysian public listed companies comprised of directors and managers appointment that connected with GLCs cluster which in purpose to channel external resources for survival in challenging and unpredictable business environment.

3.3 Hypothesis Development

Following hypothesis is developed in order to answer the research question provided in Chapter 1. The structure of the hypothesis represented as follows:

3.3.1 Senior Government Officers of the Audit Committee (SGOAC) and Audit Fees

Senior government officers (SGO) preferred been appointed as directors and managers in companies as they have influence and access to regulators. SGO influence and access to regulators are seen as a crucial strategy for a company survival as their connection and status involved required resources into their companies. The resources include favourable contracts, business prospects, knowledge and information might be delivered by the SGO into the company. Consistently, Hamid (2011) found that SGO has an easy accessed to the top officers in the government. Hence, there may be an opportunity for the company to improve under the context of business performance through this network and the study expected that the network led to audit fee reduction.

Besides, Provan (1980) claimed that the connection and resources acquired could improve company legitimacy in public and assist the company in achieving its goals. For instance, SGO can help the companies as "door opener" in business prospects and resources from the government. The study interprets SGOAC as a person who's retired or presently serving as a senior officers in government departments and at the same time hold as an audit committee members in companies. It is suggested that SGOAC might use their connection with the government to reduce the transaction cost (audit fee).

As mentioned earlier, some of the SGO were handpicked for their appointment as board member based on their good merit and seniority reputation previously in the

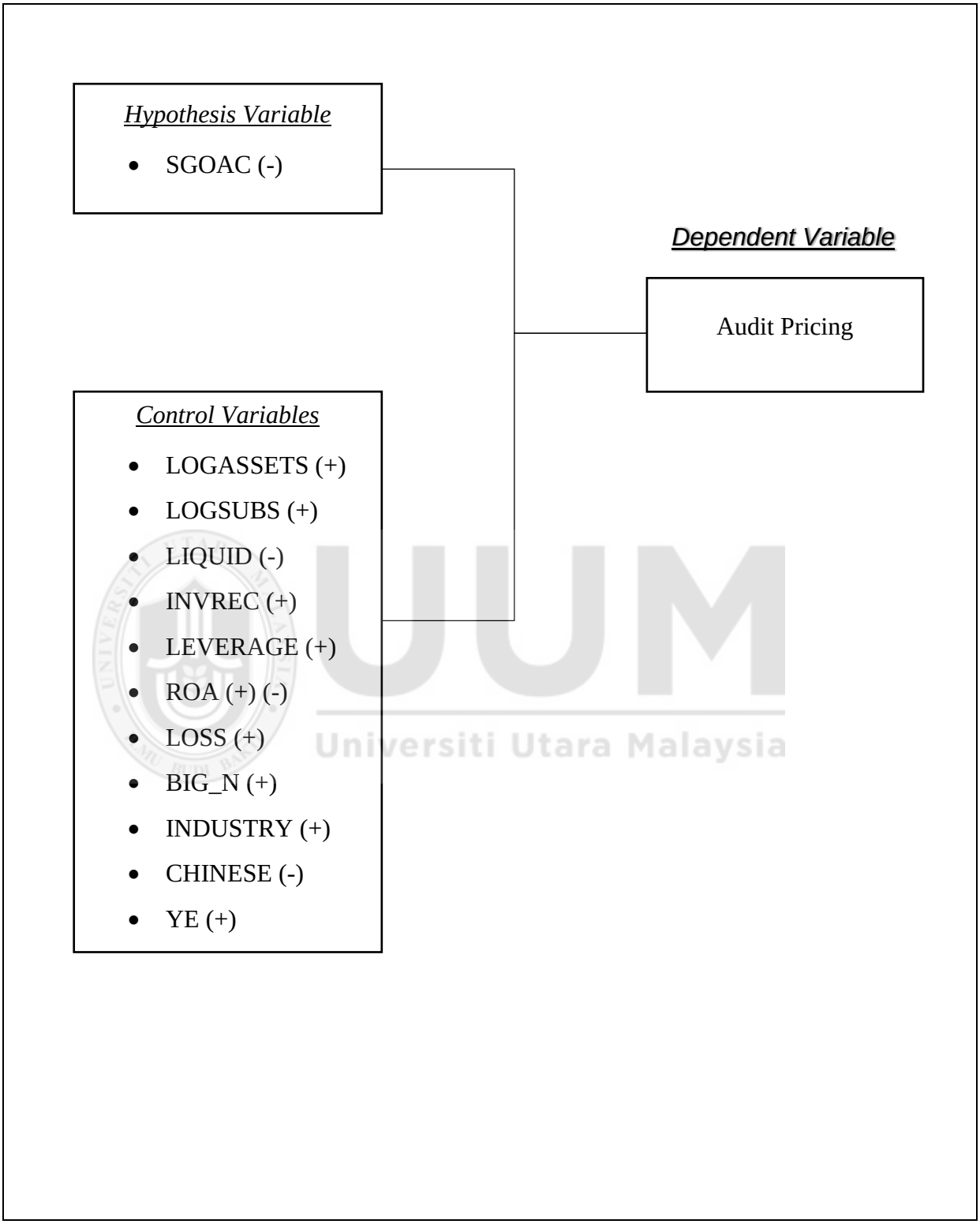
government department (Hamid, 2011). SGO plays major roles as they are actually representing the government to ensure that the company comply with the environmental regulations, instead of they been appointed as they have served the government well. Hence, it can be concluded that senior government officers of the audit committee (SGOAC) represent the government through their strong monitoring governance and their good networks with the government top officers.

Overall, the study expected that the existence of senior government officers of the audit committee (SGOAC) provides knowledge and information to the auditor and ensures the compliance with regulation by the company has contributed to the reduction in audit assessment and suggested lower audit fee.

Based on this statement, the following hypothesis is developed (in alternate form):

H_1: There is a negative significant relationship between senior government officers of the audit committee and audit pricing.

Figure 3.1 Theoretical Framework



3.4 Methodology

This chapter comprises of sample selection and data collection process. The discussion of the model and the measurement of the variable used in the model will be discussed at the end of the chapter.

3.4.1 Sample and Data

The association between senior government officers of the audit committee (SGOAC) and audit fee was examined using the population of companies listed on Bursa Malaysia in the year 2014. Table 3.1 clearly describes the sample selection of the companies in 2014.

The year 2014 was chosen a year after the General Election (GE) in 2013. Thus, the study would like to access the sample that includes SGO after the election. As mentioned earlier, SGO has a close connection with the government, thus, some of them might be effected during or after the election. On purpose to get a clear sample, the study collects the sample data after the election, namely 2014.

Table 3.1

Sample selection of Companies for the year 2014

	TOTAL
Total companies listed on Bursa Malaysia 2014	906
(-) Finance or Banking companies	(26)
(-) Companies with incomplete financial data and unavailable annual report (current or prior year)	(190)
TOTAL SAMPLE	**690**
Companies with Senior Government Officers of Audit Committee	**349**
Companies without Senior Government Officers of Audit Committee that disclose it in annual report	341
TOTAL SAMPLE	**690**

Table 3.1 above present the sample selection of the companies. Based on Table 3.1, the study includes all public listed companies in Malaysia, totalling 906 companies. Companies listed under banking and financial industry (26 companies) are left out from the study as the regulation and nature of these companies are significantly different from the non-financial companies and this consistent with prior studies (see for example Bliss et al., 2011; and Johl et al., 2012). Besides, 190 companies were also excluded due to incomplete financial data and unavailable annual report from the study. The total amount of 690 companies is the final sample of the study.

Table 3.2

Industry classification of overall sample population companies for the year 2014.

	2014	
Industry	**Frequency**	**%**
Construction	91	13.2
Consumer	78	11.3
Food Producers	72	10.4
Technology	63	9.1
Real estate	57	8.3
Engineering	44	6.4
Electric and electronics	28	4.1
Mining	28	4.1
Chemical	27	3.9
Support service	26	3.8
Transport	26	3.8
General Industrial	24	3.5
Oil	20	2.9
Travel and leisure	20	2.9
Retailer	18	2.6
Automobiles	16	2.3
Media	10	1.4
Forestry Paper	9	1.3
Telecommunication	9	1.3
Gas and Water	8	1.2
Beverages	6	0.9
Electricity	4	0.6
Pharmaceuticals	4	0.6
Tobacco	1	0.1
Aerospace Defense	1	0.1
Total Sample	**690**	**100**

Table 3.2 shows the industry classification for the year 2014. The highest percentage of companies that includes as part of the sample in the study is construction industries by 13.2 percent, followed by consumer industry by 11.3 percent and food produces 10.4 percent. This explanation is specific to a total sample of overall 690 companies.

Table 3.3

Industry classification of Senior Government Audit Committee in Companies for the year 2014

	2014	
Industries	**Frequency**	**%**
Construction	50	14.3
Consumer	34	9.7
Food Producers	32	9.2
Real Estate	32	9.2
Technology	29	8.3
Engineering	20	5.7
Transport	19	5.4
Support Service	16	4.6
Mining	14	4.0
Oil	13	3.7
Electric and Electronic	12	3.4
General Industries	11	3.2
Retailer	11	3.2
Chemical	10	2.9
Travel and Leisure	10	2.9
Automobile	7	2.0
Forestry Paper	7	2.0
Gas and Water	6	1.7
Media	4	1.1
Beverages	3	0.9
Pharmaceutical	3	0.9
Telecommunication	3	0.9
Electricity	2	0.6
Aerospace	1	0.3
Total	**349**	**100**

Table 3.3 provides further specification on the industrial sector for senior government officers of the audit committee (SGOAC) for the year 2014 which deliver to the amount of 349 companies. The highest amount of industries of a company that have SGOAC is construction by 50 companies with 14.3 percent, followed by consumer companies by 34 companies with 9.7 percent. High technology industries companies with SGOAC only represented by 29 companies with 8.3 percent. From the total

sample of 690 companies that manage to be collected, most of the companies industries do have SGOAC and only tobacco industries that do not have SGOAC. It may due to the reasons that the sample is small which only one tobacco companies.

Hence, it can be summarised that most companies do have senior government officers (SGO) as their audit committee, which according to Hamid (2011), senior government officers was selected as board due to easy access and good relationships with top officers in the government. Their selection as the board of directors might due to their good merits and seniority or their appointment was given to them as *golden handshakes* by the government caused by their past contribution.

3.4.2 Data Analysis and Model Specification

The total sample comprised of 690 companies and the study examines the relationships between SGOAC and audit pricing of the observed company for the particular period 2014. Based on the hypothesis, a regression model was used to test the relationship between senior government officers of the audit committee and audit pricing.

In testing the hypothesis, the study extended and imitate the well-established audit pricing model from (see for example Simunic, 1980; Che-Ahmad et. al, 2006; Abdul-Wahab, Mat Zain, James & Haron, 2009; and Abdul-Wahab et al., 2011). The ordinary least square (OLS) was used to analyse the data as it has been used extensively in audit pricing literature (see for example Simunic, 1984; Palmrose, 1986; Francis & Stoke, 1986; Francis & Simon, 1987; Che-Ahmad et al., 2006; and Abdul-Wahab et al., 2011). SGOAC is introduced as a hypothesis variable in the study.

The research model used for testing is as follows:

$$LOGFEE = \beta_0 + \beta_1 SGOAC + \beta_2 LOGASSETS + \beta_3 LOGSUBS + \beta_4 LIQUID + \beta_5 INVREC + \beta_6 LEVERAGE + \beta_7 ROA + \beta_8 LOSS + \beta_9 INDUSTRY + \beta_{10} BIG\_N + \beta_{11} CHINESE + \beta_{12} YE + \varepsilon$$

The measurement of the variables set out below, the specification of the measures follow later in this chapter.

Dependent Variable

LOGFEE	=	Natural log of audit fees services fee of group level

Hypothesis Variable

SGOAC	=	Total senior government officers as audit committee to total audit committee

Control Variable

LOGASSETS=		Natural log of total assets
LOGSUBS	=	Natural log of the number of consolidated subsidiaries
LIQUID	=	Current assets to current liabilities
INVREC	=	Total inventories and account receivables to total assets
LEVERAGE	=	Total debt to total assets
ROA	=	Net profit before tax to total assets
LOSS	=	Dummy variable, 1 for loss in the last year
INDUSTRY	=	Dummy variable that takes a value of 1 for companies belonging to (construction),(consumer), high technology and 0 for otherwise
BIG_N	=	Dummy variable that takes a value of 1 if the auditor is the Big Four company and 0 if otherwise
CHINESE	=	Total ethnic Chinese directors to total directors
YE	=	Dummy variable that takes a value of 1 for fiscal year end in December
ε	=	Error term

βi - constant (i = 0), regression coefficients (i = 1,2,3…12)

3.4.3 Explanation and Measurement of Variables

The following variables explanation and measurement is developed based on the research model used for testing in the study. The explanation and measurement of the variables organised as follows:

3.4.3 (i) Dependent Variable for the Audit Fee Model

The dependent variable in the study, audit fee, is measured through the logarithmic transformation of Ringgit Malaysia value of the audit fee paid to the auditor, to correct the non-normality in the distribution of the data. This is consistent with Abdul-Wahab et al. (2011) that audit fee model was utilised to test the hypothesis. Prior studies also stated that logarithmic transformation in the purpose of test normality is applied to audit fee (Francis, 1984; and Francis & Simon, 1987). In addition, higher audit fee resulted from additional audit test that led to more audit hours and more procedure used to specialised audit staff (O' Sullivan, 2000). Consistently, Wild (1994) highlighted that the formation of audit committee provides informative earnings which give rise to a lower investigation on audit risk and fewer disagreement between auditor and director that enhance audit efficiency and reduce audit fee.

3.4.3 (ii) Hypothesis Variable

Senior government officers of the audit committee (SGOAC) can be identified as retired or currently serving as the senior officers in government division and also hold a position as audit committee member of a particular company. The SGOAC data were extracted from the annual report which was obtainable from Bursa Malaysia's website. In the study, SGOAC is measured through the proportion of senior government officers that hold a position as the audit committee to the total audit committee.

3.4.3 (iii) Control Variables

The standard control variables that are used in the study are commonly utilised in audit fee studies. Though, the objective of the study is to examine the relationship between SGOAC and audit fee, other variables related to audit fee need to be included in the model as they have been stated and resulted in having significant effect on the model from prior studies (refer to Che-Ahmad et al., 2006; and Abdul-Wahab et al., 2011). The control variable comprised of total assets/company size, total subsidiaries, liquidity, inventory and receivable, leverage, return on assets (ROA), loss, industry, auditor, Chinese ethnicity and fiscal year end.

(i) Company Size (LOGASSETS)

Regarded as a proxy for company size (Hay et al., 2006) the natural logarithm of total assets are included in the study to control the non-linear relationships between audit fee and company size. According to Simunic (1980) and Francis (1984), higher audit fees is expected from a larger company as it is more complex, thus, need more audit assessment. Besides, higher risk and higher difficulty in monitoring the executive's management due to increase in company size led to the independent auditor to rely upon. Hence, it is suggested that there is a positive association between company size and audit fees.

(ii) Total Subsidiaries (LOGSUBS)

The number of subsidiaries in the company (LOGSUBS) measured the audit complexity by using the logarithm transformation. More time consuming the audit tend to be and the harder it is to audit is predicted from a more complex client (Simunic, 1980; and Hackenbrack & Knechel, 1997). Positive association is found between audit fee and the number of subsidiaries (Yatim et al., 2006). Similarly, the

number of subsidiaries, as well as the number of industrial classification, determine the complexity of the company (Hay et al., 2006). A huge number of subsidiaries led to higher audit fees due to the larger scope of auditing that need to assess more complex business operation. Thus, a positive relationship is expected from the association of LOGSUBS and audit fee.

(iii) Liquidity (LIQUID)

Uyar (2009) defined liquidity as an ability of a company collecting cash from the customer in time to prevent cash shortages, difficulty in paying short term debts and its obligations. In the study, the proportion of current assets to current liability represents the liquidity variable. Hay et al. (2006) stated that the association between quick ratio and audit fee is found to be negative which quick ratio represented by current assets minus inventories to the current liability. Consistently, Whisenant, Sankaraguruswamy and Raghunandan (2003) stated that audit fee decreasing in liquidity. To support, Hogan and Wilkins (2008) also found that audit fee is a decreasing function of liquidity.

(iv) Inventory and Receivable (INVREC)

Generally, the most difficult area to audit is inventory and receivables, hence, specialised audit procedures needed to control the higher risk of error of that area (Simunic, 1980; and Newton & Ashton, 1989). The combination of inventory and receivables divided by total assets represents the INVREC receivables. Hay et al. (2006) suggest that INVREC has positive relationships with audit fee. To support, additional assessment needed from auditor for a huge amount of inventories and receivables inspection (Antle, Gordon, Narayanaorthy & Zhou, 2006).

(v) Leverage (LEVERAGE)

Another proxy for audit risk is leverage. In the study, leverage represented by total debt to total assets. Hay et al. (2006) argued that leverage measures a risk of a client failing, which in turn provide loss to the auditor. The expected association between leverage and audit fee is a positive relationship. There is a higher amount of audit fee charged to the company with high leverage due to more risk for business which demands high audit quality. In other words, the higher the leverage, the higher the agency cost and business risk which resulted in higher audit fee.

(vi) Return on Assets (ROA)

Return on assets (ROA) acts as a proxy for client profitability (Abdul-Wahab et al., 2011) and represented as net income to total assets in the study. The prediction relationships between ROA and audit fee is negative as well as positive. In the event where the client is not financially stable, the auditor might be exposed to loss (Simunic, 1980). Thus, if there is a higher return on assets or great performance by the company, lower audit risk assessment which contributes to lower audit fee being charged. In another point of view, higher profitability company usually need extensive audit test for revenue and expenses validity that led towards higher audit fees as profitability is related to effective use of assets and other resources (Joshi & Al-Bastaki, 2000). Consistently, the previous study also provides the similar finding as a positive relationship was found between profitability and audit pricing (see Simunic, 1980; and Wallace, 1984).

(vii) Loss (LOSS)

Another attributes to profitability in the study is LOSS variable. The assumption relationship between loss and audit fee is positive. In the study, LOSS variable

reflected as a value of one if a loss in last year and zero, if otherwise. Pong and Whittington (1994), stated that this attributes represented as financial distress in prior year where a positive association is expected. Consistently, Abdul-Wahab et al. (2011) argued that LOSS variable control for the financial distress across the company. It can be concluded that the worse the performance of a company (LOSS), the higher audit fee is expected due to business risk and financially insecure.

(viii) Industry (INDUSTRY)

Dummy variable represented for INDUSTRY where a value of one for company belongs to construction, high technology, consumer and value in zero if otherwise. This is on purpose to control the variation of audit pricing across the industries (Abdul-Wahab et al., 2011). The financial institution is the common industries that normally been placed out from audit fee research due to the fact that it is more labour intensive and difficult to audit (Simunic, 1980). Financial institution industry has quite large assets, yet, it is easier to audit financial institution as other companies such as in manufacturing industry have a huge amount of inventories, receivables and knowledge-based assets (Hay et al., 2006). Hence, the audit fee for the financial institution is significantly lesser than other industry when dummy variable is used to test for financial institution industry.

(ix) Auditor (BIG_N)

A dummy variable is used to control on the differences in audit quality. The value of one represented that Big Four is the company auditor while zero if otherwise. It is reported that when the auditor is recognised of a high-quality audit, higher audit fee will be charged (Hay et al., 2006). Among the Big Four auditor (and affiliates) includes Deloitte and Touche (Kassim Chan and Co.), PWC (Jaafar Hussein), KPMG Peat

Marwick (KPMG Desa Megat) and Ernst and Young (Hanafiah Raslan Mohamad or HRM, Lim Ali and Co.). Ji-hong (2007) and Firth (2002), both argued that Big Four charged premium audit fee or higher cost due to high audit quality and audit engagement. Hence, a positive association existed between Big Four audit companies and audit fee (Che-Ahmad & Houghton, 2001) cause by Big Four great reputation effect.

(x) Chinese Ethnicity (CHINESE)

In the study, Chinese ethnicity measured by examining the number of Chinese board of director sitting on the board. The audit fee is affected by ethnic that controlled or own the board (Che-Ahmad & Houghton, 2001). Similarly, ethnic business practice gives impact to audit pricing in the auditee company as local Chinese is reported to paid lower audit fee than Bumiputra or foreign owned company due to the diverse level of agency conflict and risks related cause by higher quality audit demanded (Che-Ahmad et al., 2006). Hence, a negative relationship is expected for Chinese local controlled and/or owned companies with audit fee.

(xi) Fiscal Year End (YE)

Hay et al. (2006) found that auditor "busy season" is consistent with the time when the companies have their fiscal year end. December 31 is known as the most common fiscal year end of the auditor's busy season followed by January and February. Discounted audit fee might be offered by audit firm for work performed outside the "busy season". During the busy season which is fiscal year end at 31 Dec, an audit conducted might be charged costly as the audit co-workers need to work over time. In short, positive relationships is expected from the association between fiscal year end and audit fee.

3.5 Conclusion

This chapter discussed the research framework that leads to the hypothesis development. The presence of senior government officers of the audit committee (SGOAC) is expected to have an impact on audit fee charged to the company. The hypothesis variable is expected to have negative relationships with the audit fee due to network governance plays by SGOAC through knowledge and information gathered from close connection with the government which contributed to the reduction in auditor works and subsequently lower down the audit fee. This is consistent with Jones et al. (1997) that reduction in transaction cost (audit fee) and gaining in comparative advantage over market and hierarchies achieved due to the social mechanism in network governance.

Besides, SGOAC would able to lower the transaction cost (audit fee) based on their social network with lawmaker and government division. Through their reputation and power as well able to assess to resources such as information business opportunities, the lower audit fee expected to be charged. Consistently, Hamid (2011) stated that the appointment of senior government officers was mainly influenced by their close relationship with the government and regulators. Overall, it can be concluded that network governance plays by SGOAC contribute to lower audit fee charged by the auditor, hence, support the supply-side of audit perspectives.

Table 3.4 Summary variables, measures and data sources

No	Variables Name	Variable Type	Expected Sign	Measurement	Data Sources	Data Needed
1	Audit Fee	Dependent	NA	Logarithmic transformation of Ringgit Malaysia value of audit fees paid to the auditor	Annual reports of sample companies downloaded from Bursa Malaysia websites	Income Statement, Notes to the Financial statement
2	Senior Government Officers of Audit Committee	Independent	Negative (-)	Proportion of total senior government officers as audit committee over total audit committee	Annual reports of sample companies, in the section of: Board Members biography and background	Total number of senior government officers as audit committee member
3	Auditee Size	Control	Positive (+)	The natural logarithmic of total assets	Annual reports of sample companies, downloaded from Bursa Malaysia websites	Balance sheet
4	Auditee Complexity	Control	Positive (+)	The natural logarithmic of the number of consolidated subsidiaries	Annual reports of sample companies downloaded from Bursa Malaysia websites	Notes to the Financial statement
5	Liquidity	Control	Negative (-)	Proportion of total current assets to total current liabilities	Annual reports of sample companies downloaded from Bursa	Balance sheet

Table 3.4 (Continued)

6	Inherent Risk	Control	Positive (+)	Proportion of total account receivables and inventories over total assets	Annual reports of sample companies downloaded from Bursa Malaysia websites	Balance sheet
7	Leverage	Control	Positive (+)	Proportion of total debt over total assets	Annual reports of sample affected, downloaded from Bursa Malaysia websites	Balance sheet
8	Profitability	Control	Negative (-) Positive (+)	Proportion of net profit before tax over total assets, Dummy variable, coded as 1 for loss in last year and 0, if otherwise	Annual reports of sample companies downloaded from Bursa Malaysia websites	Balance sheet, Net income
9	Industry	Control	Negative (-) or Positive (+)	Dummy variable, coded as 1 for company belongs to construction, consumer and high technology and 0, if otherwise	Annual reports of sample companies downloaded from Bursa Malaysia websites	Corporate information, DataStream
10	Auditor	Control	Positive (+)	Dummy variable, coded as 1 for Big Four auditor and 0, if otherwise	Annual reports of sample companies downloaded from Bursa Malaysia websites	Corporate information
11	Ethnicity	Control	Negative (-)	Proportion of total ethnic Chinese director to total directors	Annual reports of sample companies downloaded from Bursa Malaysia websites	Corporate information

Table 3.4(Continued)

12	Busy season	Control	Positive (+)	Dummy variable, coded as 1 for fiscal year end in December and 0, if otherwise	Annual reports of sample companies downloaded from Bursa Malaysia websites	Balance sheet

CHAPTER 4

FINDINGS AND DISCUSSIONS

4.1 Introduction

This chapter provided analyses of the results from the model identified in the previous chapter. The results are provided in two subsections comprised of main analysis and further analyses. The descriptive analysis presented in the beginning of this chapter followed by analysis on multicollinearity, heteroscedasticity, autocorrelation and Ordinary Least Square (OLS) analyses in the next chapter. Further analyses results are presented later in this chapter. The conclusion of the discussion for the results model is presented at the end of the chapter.

4.2 Descriptive Analysis

The sample of the study consist of all companies listed on Bursa Malaysia for the year 2014, excluding the banking and financial industry resulted to 880 companies which have been discussed earlier in the previous chapter. After excluding companies without annual report and incomplete financial data, the total sample selected for the study comprises of 690 companies.

Table 4.1 provide the descriptive statistics for the continuous variable that explains the minimum, maximum, mean and standard deviation of the variables in the model and Table 4.2 provide the descriptive statistic on the dummy variable for the entire sample.

Table 4.1

Descriptive Statistic on Continuous Data, N = 690

Variable	Minimum	Maximum	Mean	Std.Deviation
LOGFEE	4.173	7.531	5.337	0.451
AUDITFEE (RM)	**14,902**	**34,000,000**	**5,21,678.54**	**1,747,466.573**
SGOAC	0.000	1.000	0.202	0.235
LOGASSETS	6.797	11.044	8.562	0.688
TOTALASSETS (RM,000)	**6,259**	**110,650,200**	**1,885,961.88**	**7282155.859**
LOGSUBS	0.000	2.688	1.043	0.439
SUBSIDIARY(NUMBER)	**1**	**487**	**19.72**	**35.062**
LIQUID	0.001	99.789	3.502	6.288
INVREC	0.001	0.915	0.334	0.195
LEVERAGE	0.005	0.936	0.364	0.192
ROA	0.010	69.590	7.536	7.672
LOSS	*0.000*	*1.000*	*0.220*	*0.412*
INDUSTRY	*0.000*	*1.000*	*0.330*	*0.472*
BIG_N	*0.000*	*1.000*	*0.440*	*0.497*
CHINESE	0.000	1.000	0.609	0.286
YE	*0.000*	*1.000*	*0.580*	*0.494*

Notes: [a]The three (3) variables in **Bold** are not variable of interest (i.e. they not included in the models) but addressed here to deliver further insight on Malaysian business practice; four (4) variables in *Italic* represents as dummy variables; LOGFEE is natural logarithm of audit fees; SGOAC is total senior government officers as audit committee to total audit committee; LOGASSETS is natural logarithm of total assets; LOGSUBS is natural logarithm of the number of consolidated subsidiaries; LIQUID is current assets to current liabilities; INVREC is total inventories and account receivables to total assets; LEVERAGE is total debt to total assets; ROA is net profit before tax to total assets; LOSS takes the values of 1 for loss in the last year and 0 otherwise; INDUSTRY takes the value of 1 for companies belonging to (construction), (consumer), (high technology) and 0 for otherwise; BIG_N takes the value of 1 if the auditor is the Big Four company and 0 if otherwise; CHINESE is total ethnic Chinese directors to total directors; YE takes the value of 1 for fiscal year end is 31 December and 0 otherwise

Based on Table 4.1, the mean value for senior government officers of the audit committee (SGOAC) is 0.202 with a minimum of 0 and maximum of 1 with standard deviation 0.235 overall for the year 2014. The Higher amount of leverage comes from Lion Diversified. Meanwhile, Inch Kenneth Kajang present the minimum amount of leverage. The amount of audit fee charged from RM 14,902 to RM 34,000,000 represented by Chuan Huat Resources and the latter by Sime Darby Berhad with an average RM 521,679. The average of audit fee found in the study is much higher than the amount of audit fee reported by Yatim et al. (2006) which is reported as RM 191,975. A number of total assets from the sample range from RM 6,259,000 to RM 110,650,200 000. The mean asset size is RM 1,885,961.88 with standard deviation of RM 7,282,155.859. The mean value for a number of subsidiaries is 19.72 with the maximum number of 487 subsidiaries and standard deviation 35.062.

Table 4.2

Descriptive statistic on Dummy Data N = 690

Variable		Frequency	Percentage
LOSS	Lost in last year	149	21.6
	Profit in last year	541	78.4
INDUSTRY	Companies belongs to Consumer/Construction /High Technology industries	231	33.5
	Companies belongs to other industries	459	66.5
BIG_N	Big4	303	43.9
	Non-Big 4	387	56.1
YE	Fiscal year end 31 Dec	398	57.7
	Fiscal year end Otherwise	292	42.3

Meanwhile, Table 4.2 provides the specific explanation on the dummy variable. Consistent with Abdul-Wahab et al. (2009) and Abdul-Wahab et al. (2011), the same measurement is used for LOSS variables. 22 percent out of 690 total sample derived with lost in last year while 78.4 percent acquired profit. In terms of industry, 34 percent of the sample belong to consumer, construction or high technology field. From the sample of 690, 58 percent have the fiscal year ending 31 December while another 42 percent year ends otherwise. Overall, only 303 companies have employed brand name auditors and larger percentage of companies employed non-brand name auditor (387 companies).

4.3 Multicollinearity Test

According to Hair, Anderson, Tatham and Black (1992), multicollinearity test describes the level by which one variable's effect could be managed by other variables. Besides that, Pearson Correlation and Variance Inflation Factor (VIF) are utilised to test the multicollinearity problem.

4.3.1 Pearson Correlations Analysis

Correlation measures the strength of a relationship between two metric variables through statistical technique. A correlation that equals as +1, signify as perfectly positive relationships while a perfect negative relationship indicates from correlations that equal to -1. Besides that, the correlation between variables equals to 0 if those specific variable do not have any relationships with each other (Pallant, 2010). Overall, correlation analysis has been utilised to describe the association between one variable with another (Asteriou & Hall, 2007). The matrix correlation between the variables of the study for audit fees model is reflected in Table 4.3 below. Among all the independent variables, correlation is found to be less than 0.5 except for correlation between LOGASSETS and LOGSUB (0.561).

Abidin, Kamal and Jusoff, (2009) predicted possible multicollinearity using 0.8 as a threshold. In addition, Firth (1997) also provide the same opinion. Generally, it can be concluded that there is no serious multicollinearity problem in the regression of the study as all the correlation are found less than 0.8 as shown in Table 4.3.

Table 4.3: Correlation Matrix for Dependant and Independent variable

Pearson Correlation Coefficient of Variables (Sample = 690)

	SGOAC	LOG ASSETS	LOG SUBS	LIQUID	INVREC	LEVERAGE	ROA	LOSS	INDUSTRY	BIG_N	CHINESE	YE
SGOAC	1.00	.124**	.092*	-.060	-.003	.140**	-.007	-.032	-.048	.079*	-.255**	-.042
LOG ASSETS		1.00	.561**	-.097*	-.251**	.306**	-.141**	-.105**	-.254**	.442**	-.257**	.054
LOG SUBS			1.00	-.198**	-.100**	.254**	-.157**	-.017	-.106*	.201**	-.094*	-.035
LIQUID				1.00	-.143**	-.429**	.021	.020	.008	-.058	0.11	-.028
INVREC					1.00	.219**	-.028	-.043	.229**	-.190**	.164**	-.045
LEVERAGE						1.00	-.122**	-.052	-.024	.119**	-.102**	-.010
ROA							1.00	.007	.034	-.016	-.056	.007
LOSS								1.00	.001	-.074	-.035	-.007
INDUSTRY									1.00	-.201**	.135**	-.008
BIG_N										1.00	-.227**	-.005
CHINESE											1.00	-.162**
YE												1.00

**.Correlation is significant at the 0.01 level (2-tailed) *.Correlation is significant at the 0.05 level (2 tailed)

4.3.2 Variance Inflation Factor (VIF)

Highly collinearity exists when VIF is larger than 10 and the tolerance value is lower than 0.10 and hence, need to be highlighted (Healy, 2002). Through Variation Inflation Factor (VIF) test, it ensures whether independent variables includes high collinearity or not.

Based on Table 4.4 as shown below, there is no serious multicollinearity problem emerge in the study as all the VIF are less than 10 and the tolerance value variable is more than 0.10.

Table 4.4

Collinearity Statistics

Variables	Tolerance	VIF
SGOAC	0.912	1.096
LOGASSETS	0.481	2.079
LOGSUBS	0.647	1.546
LIQUID	0.790	1.265
INVREC	0.798	1.253
LEVERAGE	0.675	1.481
ROA	0.953	1.049
LOSS	0.974	1.027
INDUSTRY	0.895	1.117
BIG_N	0.773	1.294
CHINESE	0.817	1.224
YE	0.954	1.048

[a]See Table 3.4 for the definition of the variables.

4.4 Heteroskedasticity

Breush-Pagan test is used in this analysis to test whether heteroskedasticity exists or not in the model. If the Chi-Square value is significant with the p-value below an appropriate threshold, the null hypothesis is rejected and heteroskedasticity is assumed (Breush & Pagan, 1979). Hayes and Cai (2007) also consistently provide the same opinion on the Breush-Pagan test. The presence of heteroskedasticity is shown through Breush-Pagan test with a probability value of (0.0000) that represents at one percent level. Hence, using the OLS-robust regression, the results have been corrected due to the problem of heteroskedasticity together with other results for further analysis.

4.5 Autocorrelation

In purpose to ensure that autocorrelation does not exist in the analysis, the Durbin-Watson test is used to test for serial correlation between errors. A value closer to 2 is acceptable and provides a result that autocorrelation problem does not exist in the study. There is no serious autocorrelation problem exist as the Durbin-Watson test for the study is close to 2 which is 2.036.

4.6 Ordinary Least Square (OLS)

The Ordinary Least Square (OLS) analysis was carried out in purpose to test the hypothesis on the relationship between the variables of the study. The regression analysis was conducted after the cross checking on the multicollinearity, heteroskedasticity and autocorrelation of the data. Table 4.5 presents the regression results in testing the hypothesis.

Table 4.5

Multiple Regression Analysis for Audit Service Fee model (N=690)

Variables	Expected Sign	Coefficient	t-value	Sig.
SGOAC	-	-0.625	-1.42	0.078*
LOGASSETS	+	0.373	14.60	0.000***
LOGSUBS	+	0.300	9.11	0.000***
LIQUID	+	-0.001	-0.43	0.335
INVREC	+	0.037	0.72	0.237
LEVERAGE	+	0.048	0.83	0.204
ROA	+	0.003	2.40	0.009***
LOSS	+	0.033	1.45	0.075*
INDUSTRY	+	0.019	1.05	0.146
BIG_N	+	0.121	5.60	0.000***
CHINESE	-	-0.160	-4.14	0.000***
YE	+	0.011	0.58	0.282
Constant		1.816	8.72	0.000
Adjusted R^2			0.7260	
F-value			101.98	
P-value			0.0000	

Notes: Significant at: *10, **5 and ***1 per cent levels; LOGFEE is natural logarithm of audit fees; SGOAC is total senior government officers of the audit committee to total audit committee; LOGASSETS is natural logarithm of total assets; LOGSUBS is natural logarithm of the number of consolidated subsidiaries; LIQUID is current assets to current liabilities; INVREC is total inventories and account receivables to total assets; LEVERAGE is total debt to total assets; ROA is net profit before tax to total assets; LOSS takes the values of 1 for loss in the last year and 0 otherwise; INDUSTRY takes the value of 1 for companies belonging to (construction), (consumer), (high technology) and 0 for otherwise; BIG_N takes the value of 1 if the auditor is the Big Four company and 0 if otherwise; CHINESE is total ethnic Chinese directors to total directors; YE takes the value of 1 for fiscal year end is 31 December and 0 otherwise

Based on Table 4.5, the model study comprised of audit fees as the dependent variable, senior government officers of the audit committee (SGOAC) as the independent variable, with several control variables (LOGASSETS, LOGSUBS, LIQUID, INVREC, LEVERAGE, ROA, LOSS, INDUSTRY, BIG_N, CHINESE and YE).

The results showed that the model is significant at one percent significance level. The adjusted R-squared of the model is 0.726 which is a slightly higher than prior studies by Che-Ahmad et al. (2006) of 0.720 and Yatim et al. (2006) of 0.699 percent. As expected, the result shows the coefficients for variables SGOAC is negatively significant (at 10 percent significant level).

For the hypothesis variable of senior government officers of the audit committee (SGOAC) that represent the number of the senior government officers, which sits on the audit committee, the result found a negative relationship with audit fee. Thus, their existence in companies as audit committee that have good relationships with lawmaker would lower down the audit fee. As mentioned earlier, audit fee is considered as monitoring cost under transaction cost (Jafee, 1995). Consequently, Jones et al. (1997) stressed that the reduction of transaction cost is due to the social mechanism in network governance.

Besides, the social network provides effective enforcement and compliance with environmental regulations than the existence of formal institutions (Scholz & Wang, 2006). This is consistent with supply audit fee perspective by Johl et al. (2012) that in existence of strong governance, auditors are less obligated to pursue additional audit efforts which resulted in lowering audit fees. Therefore, it can be concluded that network governance plays by SGOAC through good connection with the government which led to knowledge and information acquired as well as representative as strong

governance to ensure compliance with regulations contribute to the reduction in the audit assessment and resulted in lowering audit fee.

For the control variable, all results show consistencies with prior studies conducted in Malaysia and others (see eg. Che-Ahmad et al., 2006; Yatim., et al., 2006; Abdul-Wahab et al., 2009 and Abdul-Wahab et al., 2011). Six (6) variables as expected are found to provide significant relationships with audit fee, such as LOGASSETS, LOGSUBS, ROA, LOSS, BIG_N and CHINESE (ethnicity). The significant and positive coefficient LOGASSETS and LOGSUBS indicate that the larger the company (based on asset size) and the higher number of subsidiaries led to complexity matter which led to higher audit fee.

Che-Ahmad et al. (2006) supported the finding by stated that higher audit fees may be charged on a more complex company where more audit assessment acquired. Besides, positive coefficient and significant BIG_N show that higher quality audit from brand name auditor led to higher audit fee. Hence, higher audit fee is charged due to higher quality workers and advanced audit procedures in able to detect wrongs and errors. Higher audit fee caused by brand name auditor reputation is based on the positive relationship between brand name auditor and audit fee is shown in Malaysian market (Rose, 1999; Che-Ahmad & Houghton, 2001).

Another positive relationship is found between ROA and audit fee with one (1) percent significant level and 0.05 beta coefficient. This applies that the higher profitability of the company, the higher the audit fee. According to Joshi and Al-Bastaki (2000), profitability related to efficient use of assets and other resources and higher profitability company normally acquire extensive audit testing of revenue and expenses validity which led to higher audit fee. Consistently, the prior studies also

provide the same finding as a positive association was found between profitability and audit fee (see Simunic, 1980; Wallace, 1984). In addition, a positive relationship is found between LOSS and audit fee by ten (10) percent significant level and 0.03 level of the coefficient.

This described that in the existence of company loss, higher audit fee charged by the auditor. Consistently, Hay et al. (2006) explained that higher audit fee is expected when the performance of the company is worse which led to more risk upon the auditor.

All variable are found provide positive significant relationships with audit fee while CHINESE (ethnicity) have a significant negative association with audit fee. As proposed by Che-Ahmad and Houghton (2001), the Chinese controlled company provided low agency problem and lower audit fee resulted from a lower audit assessment caused by lower agency problem. The result of the study implies that the higher the number of caused Chinese board of director, the lower the audit fee.

Several control variables are found to have a positive relationship with audit fee but not significant. The variables include LIQUID, INVREC, LEVERAGE, INDUSTRY and YE. This might be due to small sample size used in the study.

4.7 Further Analyses

Further analyses were conducted in purpose to examine the sensitivity of the results by using different measurement for the hypothesis variable and the audit fee. The results are provided in Table 4.6, Table 4.7, 4.8, Table 4.9 and Table 4.10.

4.7.1 Senior Government Officers (SGO) and Audit Fee

This further test is quite consistent with the main test in terms of the control variable. Only several tests using different hypothesis variable such as SGO instead of SGOAC (senior government officers of the audit committee) and all control variable remain the same in this further test. Based on Table 4.6, the results shown is consistent with the main findings.

Table 4.6

Further Analysis on the Audit Fee model (Senior Government Officers as hypothesis variable, N = 690).

Variables	Expected Sign	Coefficient	t-value	Sig.
SGO	-	-0.122	-1.84	0.033**.
LOGASSETS	+	0.373	14.70	0.000***
LOGSUBS	+	0.303	9.20	0.000***
LIQUID	-	-0.006	-0.43	0.334
INVREC	+	0.030	0.59	0.279
LEVERAGE	+	0.050	0.86	0.195
ROA	+	0.003	2.32	0.011***
LOSS	+	0.032	1.39	0.083*
INDUSTRY	+	0.020	1.10	0.135
BIG_N	+	0.120	5.55	0.000***
CHINESE	-	-0.175	-4.36	0.000***
YE	+	0.010	0.55	0.293
Constant		1.834	8.82	0.000
Adjusted R^2			0.7266	
F-value			102.57	
P-value			0.000	

Notes: Significant at: *10, **5 and ***1 per cent levels; LOGFEE is natural logarithm of audit fees; SGO is total senior government officers to total board of director; LOGASSETS is natural logarithm of total assets; LOGSUBS is natural logarithm of the number of consolidated subsidiaries; LIQUID is current assets to current liabilities; INVREC is total inventories and account receivables to total assets; LEVERAGE is total debt to total assets; ROA is net profit before tax to total assets; LOSS takes the values of 1 for loss in the last year and 0 otherwise; INDUSTRY takes the value of 1 for companies belonging to (construction), (consumer), (high technology) and 0 for otherwise; BIG_N takes the value of 1 if the auditor is the Big Four company and 0 if otherwise; CHINESE is total ethnic Chinese directors to total directors; YE takes the value of 1 for fiscal year end is 31 December and 0 otherwise

Based on Table 4.6, the Ordinary Least Square (OLS) regression results show that the model is significant with one percent level and adjusted R-squared of 0.722. From the results in Table 4.6 below, the only hypothesis variable, SGO have five (5) percent significant negative relationships with audit fee. The control variables such as LOGASSETS, LOGSUBS, ROA and BIG_N shows a positive significant relationship with one (1) percent significance level.

Meanwhile, CHINESE control variable provides significant negative relationships with audit fee by one (1) percent significant level as well. Another positive relationship with audit fee includes LOSS control variable with ten (10) percent positive significant level. Other control variables such as LIQUID, INVREC, LEVERAGE, INDUSTRY and YE provide insignificant results with audit fee. In addition, Table 4.7 provides the regression results with a combination sample of GLCs and Non-GLCs of 68 companies.

4.7.2 Senior Government Officers of the Audit Committee (SGOAC) in Government Linked Companies (GLCs) and Non-Government Linked Companies (Non-GLCs)

Table 4.7
Further Analysis on the Audit Fees Model (Government Link Companies and Non-Government Link Companies (N=68)

Variables	Expected Sign	Coefficient	t-value	Sig.
SGOAC	-	-0.626	-2.86	0.003***
GLCs	-	-0.078	-0.80	0.214
SGOAC X GLCs	+	0.496	1.93	0.030**
LOGASSETS	+	0.432	4.61	0.000***
LOGSUBS	+	0.324	3.96	0.000***
LIQUID	-	-0.019	-0.82	0.209
INVREC	+	-0.017	-0.08	0.467
LEVERAGE	+	0.439	2.03	0.024**
ROA	-	-0.014	-1.67	0.051*
LOSS	+	0.014	0.17	0.434
INDUSTRY	+	0.123	1.25	0.109
BIG_N	+	-0.033	-0.33	0.372
CHINESE	-	-0.410	-2.51	0.008***
YE	+	-0.041	-0.54	0.298
CONSTANT		1.660	1.90	0.032
Adjusted R^2			0.8295	
F-value			20.91	
P-value			0.000	

Notes: Significant at: *10, **5 and ***1 per cent levels; LOGFEE is natural logarithm of audit fees; SGOAC is total senior government officers as audit committee to total audit committee; GLCs takes the value of 1 if Government Linked Companies and 0 otherwise; LOGASSETS is natural logarithm of total assets; LOGSUBS is natural logarithm of the number of consolidated subsidiaries; LIQUID is current assets to current liabilities; INVREC is total inventories and account receivables to total assets; LEVERAGE is total debt to total assets; ROA is net profit before tax to total assets; LOSS takes the values of 1 for loss in the last year and 0 otherwise; INDUSTRY takes the value of 1 for companies belonging to (construction), (consumer), (high technology) and 0 otherwise; BIG_N takes the value of 1 if the auditor is the Big Four company and 0 otherwise; CHINESE is total ethnic Chinese directors to total directors; YE takes the value of 1 for fiscal year end is 31 December and 0 otherwise

Based on Table 4.7, the hypothesis variable represented by SGOAC and all control variable remain the same with additional of GLCs as a dummy variable. The results show that the model provides five (5) percent significant results with adjusted R-square 0.8295. The hypothesis variables show one (1) percent negative significant results with audit fee. The coefficient for the interaction in terms SGOAC with the presence of GLCs, SGOAC* GLCs, is positive and significant (0.030, $t = 1.93$, $p < 0.05$).

The result shows that higher audit fee charged in the presence of SGOAC and GLCs. This indicates that SGOAC acts as monitors and demand more audit work to be applied especially in GLCs than Non-GLCs. According to Hay et.al (2006), client attributes comprised of size, complexities and inherent risk provide a positive relationship with audit pricing. Hence, due to the fact that GLCS is much more complex, bigger and riskier than Non-GLCs based on its size, number of subsidiaries, number of inventories and receivables, more audit assessment conducted and led to higher audit fee being charged. Therefore, it can be concluded that in the presence of GLCs, senior government officers of the audit committee (SGOAC) act as a monitor by demand more audit assessment and higher audit fee charged due to GLCs size, complexity and inherent risk.

In terms of control variables, LOGASSETS and LOGSUBS provide one (1) percent positive significant relationships with audit fee, while one (1) percent caused significant relationships are found between CHINESE and audit fee. LEVERAGE provide five (5) percent positive relationship with audit fee followed by ROA with ten (10) percent negative relationship with audit fee while other control variables provide an insignificant relationship with audit fee. Meanwhile, Table 4.8 provides the regression results for the partition analysis between the GLCs and Non-GLCs.

Table 4.8

Further Analysis on the Audit Fees Model for the Partition (Government Link Companies (GLCs, N=34) and Non-Government Link Companies (Non-GLCs, N=34)

		Non-Government Link Companies (Non-GLCs), (N=34)		**Government Link Companies (GLCs), (N=34)**	
Variables	**Expected Sign**	**Coefficient (t-value)**	**Sig.**	**Coefficient (t-value)**	**Sig.**
SGOAC	-	-0.693 (-3.42)	0.002***	0.042 (0.22)	0.416
LOGASSETS	+	0.141 (1.33)	0.100*	0.560 (5.24)	0.000***
LOGSUBS	+	0.442 (5.29)	0.000***	0.308 (2.00)	0.030**
LIQUID	-	0.003 (0.07)	0.472	-0.021 (-0.58)	0.283
INVREC	+	0.038 (0.18)	0.430	-0.109 (-0.24)	0.406
LEVERAGE	+	0.950 (2.75)	0.006***	0.395 (1.06)	0.151
ROA	+	-0.025 (-2.25)	0.018**	-0.001 (-0.05)	0.480
LOSS	+	-0.165 (-1.57)	0.066*	-0.008 (-0.05)	0.482
INDUSTRY	+	-0.094 (-1.10)	0.141	0.219 (1.23)	0.116
BIG_N	+	0.085 (0.96)	0.175	-0.089 (-0.45)	0.328
CHINESE	-	-0.716 (-4.95)	0.000***	-0.122 (-0.61)	0.274
YE	+	0.0451 (0.49)	0.313	-0.080 (-0.57)	0.287
Constant		4.513 (4.29)	0.000	0.235 (0.22)	0.414
Adjusted R^2		0.8770		0.8385	
F-value		29.52		12.08	
P-value		0.000		0.000	

Notes: Significant at: *10, **5 and ***1 per cent levels; LOGFEE is natural logarithm of audit fees; SGOAC is total senior government officers as audit committee to total audit committee; LOGASSETS is natural logarithm of total assets; LOGSUBS is natural logarithm of the number of consolidated subsidiaries; LIQUID is current assets to current liabilities; INVREC is total inventories and account receivables to total assets; LEVERAGE is total debt to total assets; ROA is net profit before tax to total assets; LOSS takes the values of 1 for loss in the last year; INDUSTRY takes the value of 1 for companies belonging to construction, consumer, high technology; BIG_N takes the value of 1 if the auditor is the Big Four company; CHINESE is total ethnic Chinese directors to total directors; YE takes the value of 1 for fiscal year end is 31 December and 0 otherwise

Table 4.8 provides the result for a population sample of 34 companies each for GLCs and Non-GLCs. In this test, hypothesis variable is represented by SGOAC and all others variable remains the same. Between GLCs and Non-GLCs result, the Non-GLCs provide a significant result compared to GLCs. The Non-GLCs results show the model is significant by one (1) percent level with the adjusted R - square of 0.8770. There are significant negative relationships between the hypothesis variable and audit fee by one (1) percent significant level. LOGSUBS, LEVERAGE and CHINESE control variable provide a significant result by one (1) percent and ROA with five (5) percent significant results followed by LOGASSETS and LOSS by ten (10) percent significant results while others control variables provide insignificant results.

For GLCs sample, the results show the model is insignificant with adjusted R- square of 0.8385. The hypothesis variable and audit fee in GLCs provide insignificant results compare to Non-GLCs. Only control variables of LOGASSETS provide one (1) percent significant relationship followed by LOGSUBS by five (5) significant relationships while others control variable provide insignificant results. The results might be insignificant for ensure GLCs due to the small population, which is only 34 companies that managed to be selected.

4.7.3 Senior Government Officers of the Audit Committee (SGOAC) and Big 4 Auditor

Table 4.9

Further Analysis on the Audit Fee Model (t-test analysis of SGOAC and Big 4 or Non-Big 4 Auditor, N= 690)

	Big 4	Non-Big 4	t-value	Sig.
Means	0.223	0.186	2.066	0.039
(Standard Deviation)	(0.238)	(0.231)		

A comparison of the mean senior government officers of the audit committee (SGOAC) between Big 4 auditor and Non-Big 4 auditor is provided in Tables 4.9. The t-test results in Table 4.9 indicates that there is a statistically significant difference between the mean SGOAC of Big 4 and Non-Big 4 auditor as the p-value is less than 0.05. Besides, the group statistic box revealed that the mean number of SGOAC for the Big 4 auditor was greater than the mean number of SGOAC for the Non-Big 4 auditor. Therefore, it can be concluded that SGOAC mean is more for Big 4 auditor than Non- Big 4 auditor and has a significant different.

Table 4.10
Further Analysis on the Audit Fee Model for the Partition (Big 4 Auditor, N=303) and (Non-Big 4 Auditor, N=387)

		Big 4 Auditor, N=303		**Non-Big 4 Auditor, N= 387**	
Variables	**Expected Sign**	**Coefficient (t-value)**	**Sig.**	**Coefficient (t-value)**	**Sig.**
SGOAC	-	-0.132 (-2.00)	0.024**	-0.013 (-0.22)	0.414
LOGASSETS	+	0.385 (10.61)	0.000***	0.343 (8.82)	0.000***
LOGSUBS	+	0.347 (7.51)	0.000***	0.248 (5.39)	0.000***
LIQUID	-	-0.011 (-0.92)	0.180	0.001 (0.55)	0.292
INVREC	+	0.027 (0.32)	0.376	0.044 (0.69)	0.245
LEVERAGE	+	0.057 (0.62)	0.270	0.061 (0.85)	0.198
ROA	-	0.002 (1.20)	0.167	0.003 (1.72)	0.044**
LOSS	+	-0.031 (-0.80)	0.213	0.064 (2.31)	0.011**
INDUSTRY	+	0.045 (1.41)	0.081*	0.004 (0.20)	0.422
CHINESE	-	-0.248 (-3.90)	0.000***	-0.074 (-1.54)	0.062*
YE	+	-0.003 (-0.09)	0.463	0.014 (0.64)	0.262
Constant		1.868 (5.98)	0.000	2.029 (6.64)	0.000
Adjusted R^2		0.7323		0.556	
F-value		61.41		32.84	
P-value		0.000		0.000	

Notes: Significant at: *10, **5 and ***1 per cent levels; LOGFEE is natural logarithm of audit fees; SGOAC is total senior government officers as audit committee to total audit committee; GLCs takes the value of 1 if Government Linked Companies and 0 otherwise; LOGASSETS is natural logarithm of total assets; LOGSUBS is natural logarithm of the number of consolidated subsidiaries; LIQUID is current assets to current liabilities; INVREC is total inventories and account receivables to total assets; LEVERAGE is total debt to total assets; ROA is net profit before tax to total assets; LOSS takes the values of 1 for loss in the last year and 0 otherwise; INDUSTRY takes the value of 1 for companies belonging to (construction), (consumer), (high technology) and 0 otherwise; BIG_N takes the value of 1 if the auditor is the Big Four company and 0 otherwise; CHINESE is total ethnic Chinese directors to total directors; YE takes the value of 1 for fiscal year end is 31 December and 0 otherwise

In addition, Table 4.10 provides the regression result for the partition analysis between the Big 4 auditor and Non-Big 4 auditor. As expected, the results present in Table 4.10 shows that senior government officers of the audit committee (SGOAC) have a negative significant result of five (5) percent with audit fee under Big 4 auditor sample. The result consistent with Tsui et.al (2001), good corporate governance led to lower audit test and audit pricing. In contrast, SGOAC shows insignificant result towards Non- Big 4 auditor. The result provides that in the sample of Big 4 auditor, SGOAC has a negative relationship with audit fee. This indicates that even in Big 4 auditor charge lower audit fee in the presence of higher SGOAC. It shows that it is not because of lower audit quality that resulted in a negative relationship between SGOAC and audit fee. Thus, it can be concluded that network governance represented by SGOAC contribute lower audit fee charged to the company.

4.8 Conclusion

Further analyses conducted on the data by using different measurement on hypothesis variable, senior government officers (SGO). Besides, further analyses and partition analyses with the same hypothesis variable also conducted on different sample between the GLCs and Non-GLCs to know its association with audit fee. In addition, t-test also was conducted in purpose to know the mean variance of SGOAC on Big 4 and Non-Big 4.

The results show that hypothesis variable, senior government officers of the audit committee (SGOAC) in all population of 690 samples, 34 samples each for separate Non-GLCs and GLCs in partition analyses and 68 sample for the combination of GLCs and Non-GLC provide a significant negative result with audit fee. However, under 68 sample of combination GLCs and Non-GLCs, the interaction of senior government

officers of the audit committee and GLCs (SGOAC* GLCs), is positive with five (5) percent significant.

The results also show that under t-test for mean variance of SGOAC on Big 4 and Non-Big 4, the mean SGOAC for Big 4 is higher than Non-Big 4 auditor. This indicates that, in the presence of higher SGOAC, Big 4 is preferred to be appointed as auditor.

Besides, the regression for the partition analysis between the Big 4 auditor and Non-Big 4 auditor also provides a negative significant relationship between audit SGOAC and audit fee under Big 4 auditor sample. The result shows that even Big 4 charged lower audit fee in the presence of higher SGOAC. This indicates that the lower of audit fee in presence of SGOAC was not due to lower audit quality.

Therefore, it can be concluded that network governance plays by SGOAC resulted in lower audit fee charged to the company due to the good relationship with government through knowledge and information distribution, business opportunity and act as representative of the government. This is consistent with Jones et al. (1997) that transaction cost reduces through the social mechanism of network governance. In support, Jaffee (1995) mentioned that audit fee is categorised as monitoring cost under transaction cost.

CHAPTER 5

CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

The purpose of the study is to examine the relationship between senior government officers of the audit committee (SGOAC) and audit fee within Malaysia business environment.

The main result shows that hypothesis variable of SGOAC is negatively associated with audit fee. A further test using SGO as hypothesis variable also provide the same results. Besides, another further test using SGOAC as hypothesis variable with the sample of GLCs and Non-GLCs for 34 companies also provides a significant negative relationship for Non-GLCs with audit fee. In addition, the result significantly shows that when the same hypothesis variable (SGOAC) was utilized under a further test of the combination of both GLCS and Non-GLCs for a sample of 68, the association between SGOAC and audit fees also resulted in significant negative relationships.

Consistently, a similar result achieved with SGOAC as hypothesis variable under Big 4 auditor sample of 303 companies. Control variable of LOGASSETS, LOGSUB, ROA, BIG_N and CHINESE is significantly associated with audit fee throughout all the analysis.

Control variable of LOSS also has significant relationships with all analyses except under further analyses of combination sample GLCs and Non-GLCs for 68 companies. Meanwhile, the interaction variable, SGOAC*GLCs under the further analyses of combination sample GLCs and Non-GLCs for 68 companies provides positive and

five (5) percent significant relationship with audit fee. Overall, the results indicate that SGOAC has a negative influence on audit fee.

5.2 Recapitulation of the Study

Chapter 1 discussed the implication of network governance in Malaysia and its connection with senior government officers. In the study, specific analyses are done on senior government officers that hold the position as the member of an audit committee in Malaysian public listed companies. The appointment of senior government officers as the board in Malaysia public listed companies has already been introduced since the establishment of government linked companies (GLCs) and formation of New Economic Policy (NEP). However, the application of senior government officers appointment as board might not know in other countries due to Malaysia distinct features in terms of economic development and multi-culture except Malaysian neighbour countries, Singapore. Hence, the study aims to examine the effect of senior government officers of the audit committee (SGOAC) as board directors on audit pricing in Malaysian public listed companies. This contributes to the objective of the study, which is to study the relationship between network governance (represented by SGOAC) and audit pricing in Malaysia.

Chapter 2 reviewed the relevant literature on network governance, senior government officers, audit committee and factors that affect the audit pricing. It is noted that numerous studies have been conducted on audit service fee and several studies on network governance. However, there is limited published article particularly conducted on network governance represented by the senior government officers of the audit committee and its relationship with audit pricing in Malaysia based on prior studies.

Theory related and tested for the hypothesis developed is discussed in Chapter 3. The hypothesis is developed from the independent variable of senior government officers of the audit committee and is expected to have a negative relationship with audit service fee. This chapter also discussed and explained on the method and models used in the study. Audit fee model is regressed through OLS regression. The total sample of the study which comprised of 690 Malaysian public listed companies for the year 2014 is also stated in this chapter.

Chapter 4 described the results of the analyses conducted in the main test and the further test. For the main test, the data used comprise a total sample of 690 listed companies in Bursa Malaysia for the year 2014. The main result provides evidence that senior government officers of the audit committee (SGOAC) is negatively associated with audit pricing at ten percent significant. Besides, further tests that includes senior government officers (SGO) as hypothesis variable with a sample of 690 companies and SGOAC as hypothesis variable in a sample of 34 Non-GLCs, both provide a negative relationship with audit fee at five (5) percent significant level.

In addition, further regression test for the partition conducted on the combination of both GLCs and Non-GLCs with 68 sample companies also provides significant one percent of a negative relationship of SGOAC with audit fee. Meanwhile, further test for the combination of both GLCs and Non-GLCs with 68 sample companies shows that the result for the interaction of senior government officers of the audit committee and government linked companies (SGOAC*GLCs) provides a positive relationship with five percent significant level. The result reveals that higher SGOAC in GLCs led to higher audit fees. Besides, further t-test conducted for means variance of SGOAC for Big 4 and Non-Big 4 auditor provide a result that Big 4 auditor is favoured by

SGOAC. In addition, further regression partition test conducted for SGOAC as hypothesis variable under a sample of Big 4 and Non-Big 4 auditor also provide negative significant relationships with audit fee. The result shows that even Big 4 auditor charge lower audit fee in the higher presence of SGOAC. Thus, it provides evidence that it is not because of lower audit quality that resulted in negative relationships between SGOAC and audit fee but because of the network governance effect on the audit pricing.

Generally, the results specify that there is a significant negative influence of SGOAC on audit fee as the SGOAC used their strong position in government for information, knowledge distribution and business opportunity which help the auditor's work that led to the reduction in audit pricing. This shows that social network and network governance used by SGOAC contributed to low audit fee charged by the auditor. Consistently, audit fee is regarded as monitoring cost under transaction cost (Jafee, 1995). Consequently, Jones et al. (1997) found that social mechanism in network governance resulted in the reduction in transaction cost. Indirectly, the study also found that due to the larger size (total assets), complexities (number of subsidiaries) and inherent risk (total inventories and account receivables), higher audit fees been charged (Hay et al., 2006) to GLCs in the presence of SGOAC.

5.3 Limitations

There would be changes in terms of a sample population of senior government officers of the audit committee (SGOAC) since the study used cross-sectional data for the financial year 2014 only. This is because the population of SGOAC would either has increased or reduced due to regulation imposed by the government. Thus, the findings might not reflect the general long-term sample population of SGOAC. Besides, the list

of SGOAC in the study only depends on the annual reports provided in Bursa Malaysia websites. Therefore, future studies may try to examine SGOAC using different methods such as through interviews and survey measurement.

5.4 Theoretical and Policy Implication of the Study

The study may contribute to the theoretical and practical (policy) implications based on the outcomes. Specifically, the study provides additional growing literature on network governance, senior government officers of the audit committee (SGOAC) and audit fee. Moreover, the implication of senior government officers as an audit committee member through explaining the variance of audit fee charged to the companies is also provided in the study. Besides, the study also provides a beneficial reference for regulatory bodies in developing and evaluating relevant policies based on its findings. This is because there is no specification on the characters and numbers of senior government officers should adhere in Malaysian board public listed companies by the regulations. The findings have shown that the more senior government officers or senior government officers of the audit committee on the board, the lower the audit fee.

In addition, the results also found that even Big 4 auditor charged lower audit fee in the presence of SGOAC. This information is beneficial as lower audit fee been charged normally caused by favoured to Non-Big 4 auditor that led to lower quality of audit information which apparently not significance in the study. Besides, the study contributes to the accounting profession in Malaysia through providing empirical evidence on the structure of audit service fee from the external perspective.

5.5 Future Research

Future studies can replicate the study through match pairing or partition approach with a sample of senior government officers of the audit committee and companies with none senior government officers of the audit committee or conducted the same study but with a different business environment (different country). Future studies may adapt the perceptual approach in investigating the effects of senior government officers of the audit committee on audit fee such as through interview conducted with stakeholders of the company for their opinion on SGOAC association with audit fee since the study has conducted theory-driven approach. In addition, further study may also use primary data that can be gained from the auditors and others respondent such as through questionnaire distribution as the study only utilised secondary data as its main source. Besides, more justification effect can be attained through regression model in identifying the relationships between the variations by carrying out similar studies in the longer period. Since the empirical evidence on the senior government officers is inadequate and scarce, future studies should proceed to investigate the effects of SGO in different aspects of committee members on audit quality. Lastly, further study should consider other factors as well to be included in the model.

5.6 Conclusion

The primary purpose of the study is to investigate the effect of senior government officers of the audit committee and audit pricing in Malaysian public listed companies. The sample of the study includes 690 listed companies in Malaysia for the period of 2014. The main results show that the senior government officers of audit committee tested in the study provides negative relationships for auditing pricing significantly.

Further analyses using senior government officers (SGO) as hypothesis variable in the sample of 690 companies, senior government officers of the audit committee (SGOAC) in Big 4 auditor sample (303 companies), SGOAC in Non-GLCs (34 companies) and the combination of GLCs and Non-GLCs (68 companies) also provide negative significant results. This is due to the fact that SGOAC used the knowledge and information distribution from their close connection with the government that helps reduce the audit work, thus contributed to lower audit fee.

Besides, the result provided that even Big 4 auditor charged lower audit fee in the presence of higher SGOAC. Hence, the result indicated that lower audit fee with the association of SGOAC resulted not due to their preferred on Non-Big 4 as the auditor that provide lower audit quality but due to network governance represented by SGOAC. The finding argued that network governance through social network theory contributed to lower audit fee. This is consistent with the main result and further analyses conducted in the study that resulted in a negative relationship between SGOAC and audit fee. Therefore, the study supports the supply-side perspective of audit fee by concluding that network governance represented by SGOAC provides a negative relationship with audit fee.

Indirectly, further analyses result provide that higher audit fee been charged in the presence of SGOAC and GLCs. Consistently, the size, complexities and inherent risk of the company contributed to higher audit fee (Hay et al., 2006). Overall, the results have achieved the objectives of the study and consistent with social network theory that there is a negative relationship between SGOAC and audit fee in Malaysian public listed companies.

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APPENDIX 1: LIST OF GLCs AND NON-GLCs COMPANIES IN THE SAMPLE

NO	GLCs	INDUSTRY
1	AXIATA	telecommunication
2	Berjaya Land	travel& leisure
3	BOUSTEAD HOLDINGS/BSTEAD	retailer
4	DAIBOCHI	general industrial
5	DRB HICOM	ENGINEERING
6	FCW	consumer
7	FIMA CORPORATION	support service
8	HO HUP CONSTRUCTION	construction
9	HUME INDUSTRY BERHAD	consumer
10	JAYA TIASA HOLDINGS	forestrypaper
11	LAND & GENERAL	realestate
12	LANDMARKS BERHAD	forestrypaper
13	LION INDUSTRIES CORPORATION	mining
14	MAGNUM BERHAD	travel& leisure
15	MALAYSIAN RESOURCES CORPORATION BERHAD	construction
16	MISC BERHAD	transport
17	MULPHA INTERNATIONAL BERHAD	travel& leisure
18	PETRONAS CHEMICAL BERHAD	chemical
19	PETRONAS DAGANG	oil
20	PETRONAS GAS BERHAD	oil
21	PHARMANIAGA	pharmaceutical
22	POS MALAYSIA	transport
23	SHANGRI-LA HOTELS	travel& leisure
24	SIME DARBY	general industrial
25	STAR MEDIA GROUP	media
26	TASEK CORPORATION BERHAD	construction
27	TENAGA NASIONAL	electricity
28	TH PLANTATIONS	Foodproducers
29	TIME DOTCOM	telecommunication
30	UMW HOLDINGS	automobile
31	UNITED PLANTATIONS BERHAD	Foodproducers
32	UTUSAN MELAYU MALAYSIA BERHAD	media
33	YTL CORPORATION BERHAD	gas&water
34	YTL LAND & DEVELOPMENT BERHAD	Realestate

Sources: Johnson and Mitton (2003); Faccio (2006); Razak, Ahmad and Joher (2011), Abdul-Wahab et al. (2011); Khazanah Berhad website (www.Khazanah.com.my)

NO	NON-GLCs	INDUSTRY
1	MAXIS BERHAD	telecommunication
2	TA ENTERPRISE	travel& leisure
3	AEON	retailer
4	KIAN JOO	general industrial
5	COASTAL CONTRACTS	engineering
6	ENG KAH	consumer
7	WELLCALL HOLDINGS BERHAD	support service
8	WCT HOLDINGS BERHAD	construction
9	LATITUDE TREE	consumer
10	SUBUR TIASA HOLDINGS BERHAD	forestrypaper
11	PLENITUDE BERHAD	realestate
12	MUDA HOLDINGS BERHAD	forestrypaper
13	PERUSAHAAN SADUR TIMAH	mining
14	TA GLOBAL BERHAD	travel& leisure
15	UEM EDGENTA	construction
16	LINGKARAN TRANS KOTA HOLDINGS BERHAD	transport
17	BERJAYA ASSET	travel& leisure
18	HAP SENG CONSOLIDATED	chemical
19	GAS MALAYSIA	oil
20	DIALOG	oil
21	HOVID BERHAD	pharmaceutical
22	GD EXPRESS	transport
23	AIR ASIA X	travel& leisure
24	AMCORP	general industrial
25	PELANGI PUBLISHING	media
26	MITRAJAYA HOLDINGS BERHAD	construction
27	MEGA FIRST CORPORATION BERHAD	electricity
28	QL RESOURCES BERHAD	Foodproducers
29	OCK GROUP BERHAD	telecommunication
30	SAPURA RESOURCES BERHAD	automobile
31	MSM MALAYSIA HOLDINGS	Foodproducers
32	MEDIA PRIMA BERHAD	media
33	MMC CORPORATION BERHAD	gas&water
34	COUNTRYVIEW	realestate