

# THE IMPACT OF OWNERSHIP STRUCTURE ON THE AUDIT QUALITY OF VIETNAM LISTED COMPANIES

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**Abstract:** *The paper aims to investigate the impact of ownership structure on the audit quality in Vietnam listed companies within a five-year period 2015-2019. The empirical results from Probit models and Feasible Generalised Least Squares method show that ownership by institutional and foreign investors have positive impact on listed firms' audit quality while family and government ownership do not affect audit quality. To a certain extent, firm size also influences company's audit quality.*

• Keywords: *audit quality, family ownership, foreign ownership, government ownership, institutional ownership, ownership structure.*

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Tóm tắt: Bài viết nghiên cứu ảnh hưởng của cấu trúc sở hữu đến chất lượng kiểm toán trong các công ty niêm yết tại Việt Nam trong giai đoạn 5 năm 2015-2019. Kết quả từ mô hình Probit và Bình phương tối thiểu tổng quát khả thi (FGLS) cho thấy sở hữu tổ chức và sở hữu nước ngoài có tác động tích cực đến chất lượng kiểm toán của các công ty niêm yết, trong khi sở hữu gia đình và sở hữu nhà nước không có ảnh hưởng đến chất lượng kiểm toán. Ở một mức độ nhất định, quy mô doanh nghiệp cũng ảnh hưởng đến chất lượng kiểm toán của công ty.

• Từ khóa: *chất lượng kiểm toán, sở hữu gia đình, sở hữu nước ngoài, sở hữu nhà nước, sở hữu tổ chức, cấu trúc sở hữu.*

## 1. Introduction

Ownership structure, which is defined by the distribution of equity and the identity of the equity owners, holds a key role in corporate governance because it points out who has the ultimate decision-making power and affects the incentives of managers, thereby the efficiency of the firm (Denis & McConnell, 2003). As these characteristics vary greatly among types of owners, it is also expected that each type of owner has a distinctive view towards audit and its importance and thus makes different decisions when it comes to matters surrounding audit, which might severely affects the audit quality in different ways. Meanwhile, listed

companies' financial reporting is an important source of information on which stakeholders can rely to make economic decisions. Owing to the great information asymmetry between internal and external stakeholders, however, pre-verified company-prepared financial reports are always under questions for its relevance and faithful representation. Therefore, audit report is also of great value for company management, since auditors, through their working process to assure the company's compliance with standard accounting practices, also make several advice and proposals attributed to the improvement of the company's internal control, corporate governance, financial management and so forth.

In the case of Vietnam - an emerging market whose legal protection for investors is rather weaker as compared to the developed ones', audit quality is more vulnerable to external determinants. A few studies cover the influence of ownership identity on audit quality are: Mitra et al. (2007), Adeyemi & Fagbemi (2010), Zureigat (2011), Ashrafi et al. (2017), Alhababsah (2019),... Despite having extremely high public demand for market transparency and audit quality due to the recent bloom of the stock market and high-profile financial scandals among listed companies, it is necessary to enrich the literature by offering an analysis of the impact of ownership structure on the audit quality in the specific case of Vietnam.

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## 2. Literature review and Hypothesis development

### 2.1. Family ownership

From one perspective, Alhababsah (2019) suggests that family members who hold company's shares demand higher audit quality to ensure the "going concern" status of their company. From another perspective, families are often believed to be capable of expropriating firm's wealth and other shareholders through excessive compensation, related-party transactions,... (Anderson & Reeb, 2003). If family members own low proportion of company's shares, they may wish to hire a large reputable audit firm to serve as their external monitoring mechanism to improve and strengthen their position. Therefore, the family ownership is negatively related with audit quality, indicating that at a higher level of shares held by family owners, the level of audit quality will be lower. The above discussion motivates the study to state the following hypothesis:

*Hypothesis 1: There is a negative relationship between family ownership and audit quality.*

### 2.2. Institutional ownership

First, institutional investors have great incentives to increase the quality of corporate disclosure, as a firm's enhanced information transparency facilitates monitoring, and affects stock returns, investment, liquidity, resource allocation and cost of capital (Francis & Yu, 2009). One of the most effective ways to enhance information environment is to improve audit quality, by strengthening audit committee effectiveness and selecting high quality auditors. Second, Ashrafi et al. (2017) suggest that institutional investors require high quality data owing to their ability to analyse financial data and put pressure managers to use services of high-calibre audit firms due to their large influence in company. Abdullah et al. (2008) find that institutional ownership is an important factor that could assist companies to perform effectively and that companies tend to be audited by the Big4 if the level of institutional ownership increases. Overall, institutional investors are most likely to demand and exert power on the management to achieve high audit quality as an effective monitoring mechanism. Consequently, the study develops the following hypothesis:

*Hypothesis 2: There is a positive relationship between institutional ownership and audit quality.*

### 2.3. Government ownership

On the one hand, owing to the political pressure,

state ownership which is often linked with low firm performance usually leads to a higher probability of earnings management and auditor compromise, thus impairing audit quality (Song et al, 2014). In the same vein, by using unclean audit opinion as a proxy of audit quality, Wang & Zhao (2003) find that for Chinese SOEs, there is a positive relationship between state ownership and the likelihood of receiving a clean audit opinion, which suggests low audit quality. On the other hand, government representatives have an interest in increasing the credibility of financial reports in order to raise additional capital and give positive indications of their legal obedience (Ben-Nasr et al., 2015). Thus, it is expected that the state demands high audit quality to maintain firm performance, protect their reputation and promote trust and confidence in Vietnam on the global financial market. Given these discussion, the hypothesis could be stated as follows:

*Hypothesis 3: There is a positive relationship between government ownership and audit quality.*

### 2.4. Foreign ownership

Foreign investors always demand more reliable and transparent information environment to avoid expropriation by insiders (Ben-Nasr et al., 2015) and rely heavily on additional controls that enable them to effectively monitor and evaluate their investments. Fang et al. (2015) find that auditor selection is a mechanism through which foreign investors shape financial reporting comparability and increase the reliability of the firm's financial information. Likewise, Jiang & Kim (2004) suggest that large foreign shareholders usually exert pressure on management and ask for higher audit quality in order to decrease information asymmetry and obtain reliable financial reporting. Foreign ownership is significantly positively associated with audit fees, one common proxy for audit quality, which shows foreign owners' high demand for audit quality and investment for extensive auditing procedures, thus driving up audit fees (Probonis & Schaeuble, 2020). Therefore, the study posits the following hypothesis:

*Hypothesis 4: There is a positive relationship between foreign ownership and audit quality.*

## 3. Data and methodology

### 3.1. Data

To examine the impact of ownership structure on the audit quality in Vietnam listed companies, the initial sample consists of all non-financial companies listed on Hanoi Stock Exchange (HNX) and Ho Chi Minh Stock Exchange (HOSE) in Vietnam during

2015-2019<sup>1</sup>. However, in order to be consistent with the methods and models below, some exclusive criteria are applied, including companies which do not have enough data in the research models and companies lack full-set data for all periods. In addition, all data are winsorized at the 1% level to control for outliers. As a consequence, the total sample includes 1560 firm-year observations, and the number of companies in each year are 312 listed companies in Vietnam.

### 3.2. Empirical models

Based on the theoretical analysis, prior studies as Mitra et al. (2007), Adeyemi & Fagbemi (2010), Zureigat (2011) and information availability in Vietnam, the following model is designed:

$$(1) AFR_{i,t} = \beta_0 + \beta_1 * FAM_{i,t} + \beta_2 * INST_{i,t} + \beta_3 * GOV_{i,t} + \beta_4 * FOR_{i,t} + \beta_5 * SIZE_{i,t} + \beta_6 * LEV_{i,t} + \beta_7 * ROA_{i,t} + \beta_8 * SHARE_{i,t} + \varepsilon_{i,t}$$

$$(2) ARL_{i,t} = \beta_0 + \beta_1 * FAM_{i,t} + \beta_2 * INST_{i,t} + \beta_3 * GOV_{i,t} + \beta_4 * FOR_{i,t} + \beta_5 * SIZE_{i,t} + \beta_6 * LEV_{i,t} + \beta_7 * ROA_{i,t} + \beta_8 * SHARE_{i,t} + \varepsilon_{i,t}$$

$$(3) BIG4_{i,t} = \beta_0 + \beta_1 * FAM_{i,t} + \beta_2 * INST_{i,t} + \beta_3 * GOV_{i,t} + \beta_4 * FOR_{i,t} + \beta_5 * SIZE_{i,t} + \beta_6 * LEV_{i,t} + \beta_7 * ROA_{i,t} + \beta_8 * SHARE_{i,t} + \varepsilon_{i,t}$$

Where:

**Table 1: List of variables used in regression model**

Symbol	Variable name	Description
<b>Dependent variable</b>		
AFR	Audit firm rotation	Dummy variable equals 1 if the company replaces its audit firm for the year, 0 otherwise
ARL	Audit report lag	The period between a company's fiscal year-end to the audit report date
BIG4	Audit firm size	Dummy variable equals 1 if the company is audited by one of Big4 (PwC, EY, Deloitte, KPMG), 0 otherwise
<b>Independent variable</b>		
FAM	Family ownership	Percentage of family ownership in the firm
INST	Institutional ownership	Percentage of institutional ownership in the firm
GOV	Government ownership	Percentage of government ownership in the firm
FOR	Foreign ownership	Percentage of foreign ownership in the firm
<b>Control variable</b>		
SIZE	Firm size	Natural logarithm of total assets
LEV	Leverage	Debt divided by total assets
ROA	Return on asset	Net profit divided by total assets
SHARE	Market share	Company's net sales divided by total industry's net sales

Source: Author's analysis & synthesis

<sup>1</sup> We exclude data in 2020 to avoid potential Covid-19 pandemic effects.

In this study, audit quality is measured by three proxies, namely audit firm rotation, audit report lag and audit firm size. The expected signs are listed in Table 2 for easy tracking.

#### Audit firm rotation

High audit firm rotation rate is considered to be associated with low audit quality given (1) the loss of long-term built client-specific knowledge which assists auditors in fully understand company operation to detect misstatements in financial reports and make relevant recommendations to the client and (2) a risk of company's unwillingness to cooperate in audit process or malpractice, thus increasing auditor resignation rate.

#### Audit report lag

Audit report lag is assumed as a reflection of low audit quality due to (1) decreased usefulness of information caused by unachieved timeliness and (2) a risk of financial misreporting thus requiring auditors to pay extra time and effort to form an opinion.

#### Audit firm size

The appointment of larger-scale audit firm, in this case: the Big4 audit firm, is considered as an indicator of high audit quality given these firms' higher capability (high requirement for applicants and staffs, rigorous training sessions, financial resource,...) and incentives (risk of reputation loss) to form accurate audit opinions.

**Table 2: Expected signs of coefficients**

	Audit quality		
	Audit firm rotation	Audit report lag	Audit firm size
Family ownership	+	+	-
Institutional ownership	-	-	+
Government ownership	-	-	+
Foreign ownership	-	-	+

Note: "+" depicts positive correlation and "-" depicts negative correlation

Source: Author's analysis & synthesis

### 3.3. Data analysis method

To examine the influence of ownership structure on Vietnam listed companies' audit quality from 2015 to 2019, the study applies Pooled OLS, FEM and REM simultaneously for audit report lag and audit firm size. In addition, Hausman test and the Breusch-Pagan test are then performed to select the most efficient model.

## 4. Empirical results

### 4.1. Descriptive Statistics

Table 3: Descriptive statistics

Variable	Observation	Mean	Standard deviation	Min	Max
AFR	1560	0.1447	0.3520	0	1
ARL	1560	73.3255	16.5845	8	140
BIG4	1560	0.2670	0.4426	0	1
FAM	1560	13.3927	17.1514	0.050	76.4700
INST	1560	30.6941	20.9408	0	96.4900
GOV	1560	24.7649	24.4090	0	82.9500
FOR	1560	11.7852	14.7708	0	77.5800
SIZE	1560	11.8127	0.6885	10.1801	14.6061
LEV	1560	1.4198	1.7340	0.0027	29.2345
ROA	1560	0.0602	0.0733	-0.2974	0.4845
SHARE	1560	1.6851	7.0785	0.0001	77.8293

Source: STATA 15 output results based on study data

It can be seen that the mean value of AFR is still greater than zero (0.1447), showing that Vietnamese enterprises do rotate audit firms on their own will, which probably roots in an attempt by company to avoid overfamiliarity with auditors or in worse case, company’s dispute with previous audit firm. As for audit report lag (ARL), there is a surprisingly large range between the minimum and maximum value. While there are companies that have their financial reports audited within eight days after the fiscal year-end, there are some whose audit process takes almost five months. Audit firm size (BIG4) has an average value of only 0.267 as the majority of companies in the sample tend to choose small and medium-sized audit firms such as Bakertilly A&C, CPA Vietnam, RSM,... rather than Big4. Firm size, leverage, ROA and market share all vary greatly among firms with high dispersion as the selected sample includes companies from several industries, which are characterised by different capital structure, net income ratio, firm size,... In the same vein, companies also have distinctive ownership structure.

4.2. Correlation matrix

Table 4 shows the pairwise correlation coefficient matrix of variables used in the model. The correlation matrix also indicates that the correlations between the independent variables are not too large (under 0.5).

Table 4: Correlation matrix

	AFR	ARL	BIG4	FAM	INST	GOV	FOR
AFR	1.000						
ARL	0.091*	1.000					
BIG4	-0.009	0.130*	1.000				
FAM	-0.011	0.088*	-0.134*	1.000			
INST	-0.062	-0.162*	0.101*	-0.395*	1.000		
GOV	0.021	-0.176*	-0.094*	-0.222*	0.461*	1.000	

	AFR	ARL	BIG4	FAM	INST	GOV	FOR
FOR	-0.043	0.047	0.290*	-0.138*	-0.157*	-0.201*	1.000
SIZE	-0.012	0.257*	0.469*	-0.048	0.011	-0.162*	0.277*
LEV	-0.039	0.095*	0.041	0.001	0.148*	0.123*	-0.161*
ROA	0.039	-0.318*	-0.030	-0.100*	0.073*	-0.047	0.053
SHARE	-0.039	-0.105*	0.228*	-0.008	-0.111*	-0.087*	0.190*

	SIZE	LEV	ROA	SHARE
SIZE	1.0000			
LEV	0.2068*	1.0000		
ROA	-0.0773*	-0.2867*	1.0000	
SHARE	0.3327*	0.0007	0.1409*	1.0000

Note: “\*”: Correlation is significant at the 0,05 level

Source: STATA 15 Output Results based on study data

The study continues to run a test on model’s variance inflation factor (VIF). As demonstrated in Table 5 below, model’s average VIF is 1.25 with all values smaller than 2. Given this result and the conclusion from the correlation matrix, it is safe to conclude that there is no multi-collinearity threat to the interpretation of the regression coefficients.

Table 5: Variance inflation factor test result

Variable	VIF	1/VIF
FAM	1.26	0.7930
INST	1.54	0.6497
GOV	1.36	0.7341
FOR	1.24	0.8095
SIZE	1.33	0.7492
LEV	1.22	0.8197
ROA	1.16	0.8646
SHARE	1.19	0.8379
Mean VIF	1.29	

Source: STATA 15 output results based on study data.

4.3. Regression results and discussion

4.3.1. Audit firm rotation – Model 1 & Audit firm size - Model 3

The regression result presented in Table6 shows a significant yet quite weak relationship between institutional ownership, government ownership and foreign ownership with audit firm rotation. Such unclear relationships might be attributed to a lack of mandatory requirement for audit firm rotation, hence companies replace their audit firm rather based on preference and financial availability.

Specifically, INST and FOR are negatively correlated with AFR (-), which suggests that the more shares held by institutional and foreign investors, the less likely the company rotates its audit firm. As the study assumes that audit firm with longer tenure has better insight into client company, lower audit firm rotation rate equals better audit quality. Taken together, the result supports hypothesis 2 and 4. On

the contrary, there is a positive correlation between GOV and AFR (+), suggesting that companies with high proportion of state ownership tend to have its audit firm rotated more frequently. This result is not in line with hypothesis 3.

**Table 6: Regression result for Audit firm rotation and Audit firm size**

AFR	Coefficient	z value	BIG4	Coefficient	z value
FAM	-0.0041	-1.25	FAM	-0.0053	-1.51
INST	-0.0097	-3.06***	INST	0.0118	4.33***
GOV	0.0046	1.83*	GOV	-0.0036	-1.54
FOR	-0.0077	-1.89*	FOR	0.0151	4.20***
SIZE	0.1114	1.26	SIZE	0.9866	10.09***
LEV	-0.0388	-0.96	LEV	-0.0338	-1.03
ROA	1.0474	1.40	ROA	-1.3556	-1.78
SHARE	-0.0170	-1.55	SHARE	0.0334	2.94***
_cons	-2.0519	-1.98	_cons	-12.7549	-10.92***
LR chi <sup>2</sup> (8): 17.41			LR chi <sup>2</sup> (8): 285.72		
Prob > chi <sup>2</sup> : 0.0261			Prob > chi <sup>2</sup> : 0.0000		
Pseudo R <sup>2</sup> : 0.224			Pseudo R <sup>2</sup> : 0.2619		

\*, \*\*, \*\*\*: statistically significant at 10%, 5% and 1%

Source: STATA 15 Output Results based on study data

Table 6 also demonstrates that BIG4 is positively correlated with INST and FOR (+), suggesting that companies with high level of institutional and foreign ownership are more likely to hire Big4 audit firm. Though the correlation is quite weak, this finding is consistent with the hypothesis 2 and 4 that institutional and foreign investors demand high audit quality as an effective monitoring mechanism due to the high level of risk they bear and thus prefer the use of a large-size reputational audit firm like Big4.

In addition, there is a strong correlation between the dependent variable (Big4) and firm size, which is well expected given a common belief that Big4 audit firms offer better audit quality considered the high-quality human resources, long term reputation to protect, standardised audit methodologies and so on, which make stakeholders place more trust and prefer Big4's assurance service. Large-scale companies which have more stakeholders and receive more public and press attention, therefore, have a tendency to appoint Big4 as their audit firm to better protect its image of financial integrity

#### 4.3.2. Audit report lag - Model 2

Based on the Hausman test, FE model is better than RE model as the Prob>chi<sup>2</sup> is smaller than 0.05 (0.0002). As the dataset suffers from heteroscedasticity and autocorrelation, the FE model will be estimated again using the Feasible Generalised Least Squares (FGLS) method to fix

both problems.

**Table 7: Regression results for Audit report lag - Model 2**

Variable	Pooled OLS	FEM	REM	FEM (FGLS approach)
FAM	-0.0006 (-0.02)	0.0509 (0.73)	0.0331 (0.76)	0.0267 (1.18)
ISNT	-0.0939*** (-3.29)	-0.0101 (-0.20)	-0.0651* (-1.77)	-0.0741*** (-3.56)
GOV	-0.0724*** (-3.14)	-0.0857 (-1.58)	-0.0800** (-2.45)	-0.0953*** (-5.14)
FOR	-0.0293 (-0.91)	0.160** (1.98)	-0.0129 (-0.25)	-0.0528* (-1.90)
SIZE	6.973*** (8.62)	21.66*** (6.41)	8.507*** (6.73)	6.8803*** (10.57)
LEV	-0.148 (-0.48)	-0.635 (-1.46)	-0.2600 (-0.73)	-0.4776* (-1.94)
ROA	-61.00*** (-8.62)	-38.79*** (-4.05)	-45.98*** (-5.76)	-44.5422*** (-7.65)
SHARE	-0.425*** (-5.71)	-0.503 (-1.54)	-0.488 (-4.11)	-0.3466*** (-5.84)
CONS	-0.577 (0.06)	-178.5*** (-4.45)	-19.82 (-1.33)	3.7449 (0.49)
R <sup>2</sup>	0.2139	0.1681	0.2859	Wald chi <sup>2</sup> (8): 320.42
P-value	0.0000	0.0000	0.0000	Prob > chi <sup>2</sup> : 0.0000
Hausman test	0.0002			

\*, \*\*, \*\*\*: statistically significant at 10%, 5% and 1%

Source: STATA 15 Output Results based on study data

Table 7 shows that ARL is inversely correlated with INST, GOV and FOR (-). This result suggests that companies that have more shares owned by institutions, government and foreign investors tend to have their audited financial reports released earlier - an indicator of increased audit quality, and therefore supports hypothesis 2, 3, 4. Among these types of ownership, GOV has the greatest coefficient of -0.0953 at 1% significance level. This is in line with the finding of Ben-Nasr et al. (2015), suggesting that government representatives have an interest in increasing the credibility of financial reports in order to raise additional capital and give positive indications of their obligations to market-oriented policies, hence demanding higher audit quality from companies by having audit report released on time.

It is notable that ARL is correlated with all control variables used in the model, suggesting that it is closely associated with firm performance and characteristics. Significantly, the coefficient of SIZE is over 6.88, indicating a strong direct relationship between audit report lag and firm size (+). This is inconsistent with several empirical studies about

audit report lag which argue that audit report lag tends to be shorter in large companies because (1) larger companies may have stronger internal controls, which in turn should reduce the propensity for financial statements errors to occur and enable auditors to rely on controls and interim work more extensively, (2) larger companies have the resources to pay high audit fees so that audit process can be rapidly performed after the fiscal year end, (3) larger companies may be monitored more closely by investors, trade unions and regulatory agencies, and thus face greater external pressure to report earlier. However, in the case of Vietnam, the stock market is characterised by an excessively large number of small and medium-sized enterprises that have their financial reports audited within surprisingly short period (under 1 month) such as Dam Sen Water Park Corporation (DSN), Safoco Foodstuff Joint Stock Company (SAF),... As compared to these companies, those that release audited financial reports on time (ARL at around 90 days) are already considered to be “lagged”. Hence, such positive correlation is fairly understandable.

On the contrary, ARL is strongly and negatively correlated with ROA at a 1% significance level (–), suggesting that companies with worse financial performance (lower ability to utilise its assets in terms of profitability) often take much longer to release audited financial statements. On the bright side, such correlation might be due to the size bias just discussed as large-scale firms that have long audit report lag are also companies that have high asset value (which is used as denominator in the ROA formula). However, it can also be the case that in years of poor financial performance, management is under more pressure to keep their image among investors, thus making them more prone to earnings management and data manipulation. Auditors, therefore, need to pay extra time and effort to guarantee reasonable assurance over company’s reports.

#### 4.3.3. Hypothesis outcome

**Table 8: Hypothesis outcome**

	Expectation			Empirical results		
	AFR	ARL	BIG4	AFR	ARL	BIG4
FAM	+	+	–	/	/	/
INST	–	–	+	–	–	+
GOV	–	–	+	+	–	/
FOR	–	–	+	–	–	+

Note: “+”: positive correlation, “–”: negative correlation, “/”: insignificant correlation

Source: Author’s analysis & synthesis

From those above results in Table 8, it can be concluded that hypothesis 2 and hypothesis 4 are accepted. This result is consistent with the findings of Zureigat (2011) and Alhababsah (2019).

### 5. Conclusion

This study analyses the impact of ownership structure on the audit quality of Vietnam listed companies from 2015 to 2019 by using data collected from 312 non-financial enterprises listed on Hanoi Stock Exchange and Ho Chi Minh City Stock Exchange. The empirical results provide evidence of a positive relationship between institutional and foreign ownership with audit quality while find no significant impact of family and government ownership on audit quality. Hence, besides raising capital from individual investors, firms should also attract institutional and foreign investors by enhancing the corporate governance system, firm performance, firm valuation.

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