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GOVERNANCE STRUCTURES, ETHNICITY, AND AUDIT FEES OF MALAYSIAN LISTED FIRMS

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Abstract

Purpose – This study examines the association between external audit fees, and board and audit committee characteristics of 736 Malaysian listed firms. It is hypothesised that good corporate governance practices reduce auditors’ risk assessments, resulting in lower audit fees. Drawing on the existence of a clearly identifiable ethnic domination of board membership and ownership of Malaysian listed firms, the study also posits that Bumiputera-controlled firms pay higher audit fees because of their weaker governance practices.

Design/methodology/approach - This study employs a cross-sectional analysis of 736 firms listed on the Bursa Malaysia for the financial year ending in 2003. Multiple regression analysis is used to estimate the relationships proposed in the hypotheses.

Findings - Overall, the results of this study reveal that external audit fees are positively and significantly related to board independence, audit committee expertise, and the frequency of audit committee meetings. The study also finds a strong negative association between external audit fees and Bumiputera-owned firms. An additional analysis into the internal governance structures of firms in the sample show that Bumiputera firms practice more favourable corporate governance practices compared to their Non-Bumiputera counterparts.

Originality/value – This study is a unique contribution in that it provides data on corporate governance practices in Malaysia for a large sample in the period after the corporate governance reforms taken by Malaysian capital market regulators and participants. Previous studies have shown that Bumiputera-controlled firms pay higher audit fees than Non-Bumiputera controlled firms. These studies have not tested theoretical explanations for this fee differential. A theoretical explanation provided in the current study is that Bumiputera-controlled firms pay higher audit fees than Non-Bumiputera controlled firms partially because of differences in corporate governance practices. The study finds conflicting results with previous research suggesting that corporate governance practices have changed in Malaysia since the amendments of Bursa Malaysia Listing Requirements 2001.

Keywords Corporate governance, Boards of Directors, audit committees, audit fees, and Bumiputeras.

Paper type – Research paper

Introduction

Prior studies predominantly using data from the United States, the United Kingdom, and Australia have investigated the association between governance mechanisms and the financial
reporting process. For instance, using US-based data, Beasley (1996), Dechow et al. (1996), and Jiambalvo (1996) document a negative relationship between effective governance mechanisms and financial reporting decisions that are in violation of Generally Accepted Accounting Principles (GAAP). Recently, Carcello et al. (2002) and Abbott et al. (2003) show that firms with stronger internal governance structures demand higher audit quality and thus pay higher audit fees. Using UK data, Peasnell et al. (2000) confirm the findings previously reported by Dechow et al. (1996) that earnings management is negatively related to the independence of the Board of Directors. Similar to findings reported by Peasnell et al. (2000), Davidson et al. (2005) also find that greater board independence lowers the likelihood of earnings management in Australian firms.

Our study extends this line of research and examines the relation between external audit fees and internal corporate governance structures in emerging markets such as Malaysia. The examination of the association between internal governance structures and audit fees in Malaysia is motivated by two factors. First, Malaysia is an appealing case to study because it is likely that corporate governance practices practiced by Malaysian listed firms are different from those practiced in developed markets. While the empirical results provide evidence from a strong and sophisticated capital market environment (Carcello et al., 2002 (US); Goodwin-Stewart et al. forthcoming (Australia)), very little research has been conducted in countries where capital markets are less developed and where corporate governance mechanisms are still evolving.

Further, institutional differences exist between developing capital markets such as Malaysia and other developed markets. These institutional differences include a weak market for corporate control (Zhuang, 1999; Lins, 2003; Gibson, 2003), more concentrated stock ownership (Shleifer et al., 1997; Claessens et al., 2000), and significant government ownership in listed firms (Shleifer et al., Vishny, 1997; Claessens et al., 2000; Lemmon et al., 2001; Mak
et al., 2001). At the corporate level, these institutional differences may influence how the managers and the Board of Directors govern their firms. Although the audit fee literature is quite developed, no prior studies have examined the link between internal governance structures and external audit fees in emerging markets such as Malaysia. Therefore, this study addresses the scarcity of research in this environment and its influence on external audit fees in Malaysia.

Second, the Malaysian corporate environment offers clearly identifiable capital segments divided along ethnic lines. This division can clearly be observed in the listed firms whose board membership and share ownership are predominantly controlled by two main ethnic groups, namely the Bumiputera Malays and the Chinese [1]. Although there are other ethnic groups such as Indians, the distinction between the two main ethnic groups (i.e., Chinese and Bumiputeras) dominates much of the socio-economic activities and political policy making decisions. Given this unique corporate environment, this study extends the audit pricing and governance literature by examining proxies such as political and ethnic favouritisms (Gomez and Jomo, 1997) in the audit fee models and how this dimension of inherent risk influences external audit fees in Malaysia.

Further, Eichenseher (1995) and CheAhmad et al. (2001) also document a significant relation between ethnicity and audit fees in the Malaysian market. Together, these two studies show that Bumiputera-controlled firms pay higher audit fees compared to Non-Bumiputera controlled firms. They, however, do not provide theoretical explanations for the variations in audit fees. This current study is conducted after the incorporation of the Malaysian Code on Corporate Governance into the Listing Requirements of Bursa Malaysia 2001. Since then, the listed companies including Bumiputera-controlled companies have improved their corporate governance environment (KLSE/PricewaterhouseCoopers, 2002). This study, therefore, offers alternative explanations for the fee variations from a corporate governance perspective given
that there is a documented empirical association between ethnicity and external audit fees in previous studies. The study tests whether Bumiputera-controlled firms have weaker corporate governance practices than Non-Bumiputera controlled firms.

The remainder of this paper is structured as follows. The next section briefly explores corporate governance in Malaysia. This is followed by a discussion on the background of the study and development of our hypotheses. The third section describes the research design. The results of our study are reported in the fourth section while in the final section conclusions are drawn and the implications of the study are discussed.

**Malaysian Corporate Governance Environment**

The revised Listing Requirements of Bursa Malaysia in 2001 provides greater obligation for public listed companies to enhance Malaysia’s corporate governance regime[2]. Specifically, the amended Listing Requirements of 2001 outline the requirements for financial reporting disclosure on corporate governance matters and continuing listing obligations. Other than the audit committee, which has been mandatory since 1993, the Malaysian Code on Corporate Governance also recommends that the Board of Directors appoint Remuneration and Nomination Committees. The establishment of other committees such as a Risk Management Committee and a Corporate Governance Committee are also recommended but are less frequently set up by listed firms.

The Malaysian Code on Corporate Governance strongly recommends the separation of responsibilities between the Board Chair and the CEO even though the Bursa Malaysia Listing Requirements 2001 does not require the segregation of these positions. The Malaysian Code on Corporate Governance also states as principle that the Board of Directors should maintain a sound system of internal control. This led to the issuance by the exchange of “*A Guide on Statement of Internal Control*” in May 2000. This guideline explains the key areas that
directors must pay attention to before they make *A Statement of Internal Control* in their companies’ annual reports. A listed firm is required to address in their annual reports the Principle and Best Practices in the Malaysian Code on Corporate Governance relating to internal control such as identifying principal risks and ensuring implementation of appropriate systems to manage risks.

In addition, directors appointed to the Board of Directors of a public listed company are required under the Listing Requirements to attend a director’s training program known as the Mandatory Accreditation Program. The scope of this program covers topics such as Companies Act 1965, the Listing Requirements, risk management and internal control and relevant securities laws. Self-regulatory initiatives also continue to be developed by various industry and professional bodies aiming at promoting knowledge and awareness of corporate governance best practices in Malaysia.

Although the Malaysian Code on Corporate Governance and the Bursa Malaysia Listing Requirements 2001 provide the recommendations and rules to restore investor confidence and to improve standards of corporate accountability, the efficacy of the recommended and mandatory governance practices in influencing external audit fees has not been empirically tested. Therefore, our study explores whether the various best practices and recommendations have influenced external audit fees in Malaysia.

**Theoretical Background and Hypotheses**

The economic framework underlying this study is that audit fees reflect the economic costs of efficient auditors (Simunic *et al*., 1996). These costs vary considerably with variables such as the size, complexity, riskiness, and specific characteristics of the audited client including various aspects of its internal governance structures (Simunic *et al*., 1996; Carcello *et al*., 2002; Cohen *et al*., 2002; Goodwin-Stewart *et al*., (forthcoming). This study posits that good
Corporate governance practices are likely to reduce both inherent and control risks, leading to lower external audit fees. Specifically, from the auditor’s perspective, a stronger control and governance environment is likely to reduce the auditor’s assessment of control risk and the extent of audit procedures, thus reducing audit fees. Following this line of reasoning, the study tests hypotheses related to several governance variables.

The study characterises strong internal corporate governance structures when a firm adopts best governance practices as prescribed by the existing empirical literature and various recommendations and rules for governance reforms (Fama et al., 1983a,b; the Cadbury Committee 1992; the Malaysian Code of Corporate Governance 2001; the New York Stock Exchange and the NASDAQ 2003). The strong governance practices considered in this study include greater board independence (measured by both a higher representation of independent non-executive directors on boards and the separation of the Board Chair and the CEO positions), smaller boards, diligent boards, and boards with a risk management committee.

In addition, the study also addresses audit committee characteristics identified by the Blue Ribbon Committee on Improving the Effectiveness of Corporate Audit Committee (BRC) (1999). These characteristics include audit committee independence, audit committee expertise, audit committee size, and audit committee diligence. The Blue Ribbon Committee (1999) contends that a more independent, diligent, expert, and larger audit committee is better able to objectively evaluate management’s accounting and reporting practices. These attributes of an audit committee are likely to contribute to an improved governance environment within a firm. Focusing on a risk-based approach of audit services, these audit committee characteristics are likely to reduce a firm’s inherent and control risks associated with the firm’s financial statements and disclosures (Beasley 1996; Dechow et al., 1996; Anderson et al., 2004). Finally, the study also considers elements of ethnicity that have been found to influence audit fees in institutional settings such as Malaysia (Eichenseher 1995; and CheAhmad et al., 2001).
This current study offers explanations for fee variations from a corporate governance perspective in which it argues that governance practices in ethnic favoured firms are likely to result in differential external audit fees.

In the following section, the study develops two main testable hypotheses on the relation between external audit fees and both board and audit committee characteristics. The third hypothesis tests the association between external audit fees and governance practices associated with ethnic domination of board membership and share ownership.

**Board Characteristics, the Financial Reporting Process, and External Audit Fees**

The Board of Directors has a primary responsibility of overseeing the firm’s financial reporting process. They also must assess the quality of corporate governance within the organisation and ensure that the organisation has, for example, effective accounting practices, internal control and risk management, and audit functions. Therefore, Boards of Directors are potentially viewed, in particular their structures, as important elements in delivering credible and relevant financial statements.

**Board Independence**

Agency literature suggests that board independence from management provides, among other things, the most effective monitoring and controlling of firm activities in reducing opportunistic managerial behaviours and expropriation of firm resources (Fama *et al.*, 1983a,b; Brickley *et al.*, 1994). Board independence is also likely to provide superior oversight of the financial reporting process, hence greater reliability and validity in accounting reports is expected (Beasley, 1996; Dechow *et al.*, 1996). As a result, this reduces the auditor’s risk assessments and less audit efforts are required, leading to lower audit fees charged.

The literature and governance guidelines also show that a board’s ability to perform its governance role is likely to weaken when the CEO is also the Board Chair (Fama *et al.*, 1983a,b; Brickley *et al.*, 1994).
For instance, Dechow et al. (1996) show that firms identified as earnings manipulators are more likely to have a CEO who also serves as a Board Chair. This suggests that the combination of these roles is likely to compromise the board effectiveness in monitoring management and the financial accounting process. As a result, the auditor needs to devote more audit efforts, hence charging the firm higher fees.

**Board Size**

Board size may play an important role in directors’ ability to monitor and control managers (Jensen, 1993; Lipton and Lorsch, 1992; the Business Roundtables, 1997). Lipton et al. (1992) and Jensen (1993) argue that because of difficulties in organising and coordinating large groups of directors, board size is negatively related to the board’s ability to advise and engage in long-term strategic plans. Beasley (1996) also finds that the size of the Board of Directors significantly affects the likelihood of financial statement frauds. His results indicate that as board size increases, the likelihood of financial statement fraud also increases. As such, board size is likely to affect the financial reporting process, hence audit process. If larger boards are less effective monitors of the financial reporting process (Beasley, 1996), then the firm’s external auditor assesses the control environment as weak, hence more audit hours are required, resulting in higher external audit fees.

**Board Diligence**

The intensity of board activities is likely to contribute to the effectiveness of its oversight functions particularly in matters concerning the financial reporting process. Lipton et al. (1992) and Byrne (1996) argue that boards that meet frequently are more likely to perform their duties diligently and are beneficial to shareholders. Similarly, Conger et al. (1998) and Vafeas (1999) argue that board meeting time can improve the effectiveness of a board.
Therefore, a board that demonstrates a greater diligence in discharging its oversight responsibilities is likely to enhance level of oversight of the financial reporting process. It is, therefore, expected that more diligent boards (measured by the number of board meetings held during the financial year) are likely to be negatively associated with external audit fees.

The Existence of a Risk Management Mechanism

Consistent with a risk-based approach, a firm that establishes a risk management committee as one of the board committees demonstrates a greater awareness of the importance of risk management and control (The Committee of Sponsoring Organisations of the Treadway Commission, 1992 and 2004; Hermason, 2003; Selim et al., 1999). As monitoring by the Boards of Directors is heightened through a stringent risk management procedure, one can argue that the financial reporting quality of the firm is greatly enhanced. Hence, in the context of good corporate governance attributes, this study examines the association between external audit fees and the existence of a risk management committee. The study posits that firms with better internal control, in terms of risk management, are likely to reduce external monitoring from auditors, thereby lower audit fees are expected.

In sum, the preceding discussion argues that more independent and diligent boards, smaller boards, and boards with a risk management committee are likely to enhance internal governance and the control environment and reduce auditors’ risk assessments associated with the financial reporting process. As a result, the extent of audit procedures is also likely to be reduced, leading to lower external audit fees. The following hypothesis is, therefore, tested:

_Hypothesis 1: Lower external audit fees are associated with Boards of Directors that are more independent, have a smaller number of members, establish a risk management committee, and meet more frequently._
Audit Committee Characteristics, the Financial Reporting Process, and External Audit Fees

The Blue Ribbon Committee’s (1999) recommendations that address audit committee independence, financial literacy and expertise, as well as audit committee size and authority are expected to result in a more effective audit committee oversight of the financial reporting process. Therefore, in addition to board characteristics, this study also examines whether firms having audit committee structures consistent with the Blue Ribbon Committee’s (1999) recommendations are likely to be associated with higher quality of financial reporting, resulting in lower auditors’ assessment of control risks, hence lower external audit fees are expected.

Audit Committee Independence

Consistent with the risk-based approach, an independent audit committee is likely to result in a more effective audit committee oversight of the financial reporting process, thus reducing the incidence of financial reporting problems (the Blue Ribbon Committee, 1999; Abbott et al., 2004; Dechow et al., 1996; McMullen, 1996)[3]. An independent audit committee (relative to insider-dominated audit committees) is better able to protect the reliability of the accounting process and promote objectivity on the part of the audit committee. This helps strengthen internal controls and should lead to a reduction in the levels of both inherent and control risk. As a result, the firm requires less substantive testing, and hence lower external audit fees are expected.

Audit Committee Expertise and Size

The effectiveness of an audit committee is further enhanced if members of audit committees possess accounting and financial expertise. In its third recommendation, the Blue Ribbon Committee (1999) recommends a minimum of three audit committee directors, each of whom is financially literate and at least one of whom has accounting or related accounting and
financial management expertise. Further, in addition to a requirement that a majority of audit committee members are independent directors, Bursa Malaysia also mandates that audit committees of its listed firms be composed of at least three members and at least one audit committee member must be a member of the Malaysian Institute of Accountants (MIA).

Empirical findings also support the assertion that an audit committee should at least consist of one member with accounting and financial expertise. Audit committee expertise allows for a better understanding of auditing issues and risks, and the audit procedures proposed to address and detect these issues and risks (DeZoort et al., 2001). Knapp (1987) and Cohen et al. (2002) also find that auditors are less likely to refer a complex auditing issue to an audit committee that is perceived as not being knowledgeable about the technical auditing and financial reporting matters involved. Collectively, empirical evidence and governance best practices suggest that audit committee expertise reduces auditors’ risk assessments associated with the financial reporting process, resulting in lower external audit fees.

The audit committee size recommendation is consistent with the desire to increase the organisational status of the audit committee (Braiotta, 2000). Similarly, Kalbers et al. (1993) suggest that larger audit committees are legitimised by a meaningful organisational support from the Board of Directors and are thus more likely to be acknowledged as an authoritative body by the external auditors as well as by internal audit functions of firms. Therefore, consistent with the recommendation by the Blue Ribbon Committee (1999) with respect to audit committee size, this study argues that larger audit committees are likely to enhance the quality of financial reporting, resulting in lower external audit fees.

**Audit Committee Diligence**

A number of studies and governance best practices also call for audit committees to be diligent in carrying out their duties (Abbott et al., 2004; the Blue Ribbon Committee, 1999; Kalbers et al., 1993). Generally, studies in this area use the most common proxy for audit
committee diligence, which is the number of audit committee meetings held annually. Prior research also suggests that an audit committee that meets frequently can reduce the incidence of financial reporting problems. By meeting and communicating frequently, for instance, with the external auditor, the audit committee can alert the auditor on a particular auditing issue requiring greater attention from the auditor (Raghunandan et al., 1998). Consistent with the risk-based approach, it is therefore expected that a more diligent audit committee is likely to reduce financial reporting problems, leading to lower external audit fees.

Overall, audit committee structures that are consistent with the Blue Ribbon Committee’s (1999) recommendations help strengthen audit committee effectiveness in their oversight functions. This is likely to result in less substantive testing, leading to lower external audit fees. The following hypothesis is, therefore, tested:

Hypothesis 2: Lower external audit fees are associated with audit committees that are more independent, have more members, have greater accounting and finance expertise, and meet more frequently.

Ethnicity and audit fees

The effects of cultural differences and various aspects of culture (i.e., ethnicity and demography) have been shown to influence business practices, organisations, and accounting disclosure practices and audit services (Hofstede, 1980, 1991; Haniffa et al., 2002; Eichenseher, 1995; CheAhmad et al., 2001). However, prior research fails to explore the effect of ethnicity on monitoring differences (i.e., monitoring by internal governance mechanisms) despite recognition of its importance.

Malaysian capital market exhibits a unique corporate environment where its economy offers clearly identifiable capital segments divided along ethnic lines (Jesudason, 1989). Early economic development exhibited a clear distinction between foreign (mostly British) and local
Chinese capital formation. After independence in 1957 from the British, the government initiated the New Economy Policy, which gradually adds another distinct component of ethnic groups, namely the Bumiputera or Malay shareholders, to the Malaysian capital market.

The presence of clearly identifiable ethnic domination of board membership and ownership of Malaysian listed companies is likely to provide evidence of monitoring differences that may exist in these firms. These differences are also likely to influence auditors’ risk assessments, which in turn may affect variations in audit fees. Johnson et al. (2003) and Gomez et al. (1997) argue that Bumiputera-controlled firms (i.e., ethnically-favoured firms) and politically connected firms are perceived to have poor corporate governance practices and greater agency problems. In addition, Gul (2003) also documents evidence of a positive association between audit fees and agency costs of political affiliations using a sample of Malaysian listed firms. He argues that auditors perceive politically affiliated firms as having greater audit risks, thus charging them higher fees. Both Eichenseher (1995) and CheAhmad et al. (2001) suggest that Chinese business practices may influence differences in levels of agency conflicts and risks associated with Chinese-controlled companies (i.e., Non-Bumiputera companies), leading to lower external audit fees charged to these firms. Collectively, these studies indicate that an element of ethnicity or ethnic favouritism can be considered as another dimension of inherent risk.

Our study extends the work of Eichenseher (1995) and CheAhmad et al. (2001) by seeking an explanation for audit fee variations from a corporate governance perspective. Gomez et al. (1997) and Johnson et al. (2003) suggest that Bumiputera-controlled companies are likely to have a poor governance environment and are given preferential treatments by the ruling government. This study provides recent evidence on whether Bumiputera-controlled firms pay higher audit fees than Non-Bumiputera controlled firms. Further analyses are also sought for an association between Bumiputera-controlled firms and these internal governance structures.
If Bumiputera-controlled firms (by virtue of government ownership, and board membership and share ownership controlled by Bumiputeras) are associated with poor governance practices, then they should constitute higher levels of inherent and control risks[4]. The poor governance environment is likely to adversely affect the financial reporting process, hence reducing the quality and reliability of financial reporting. As monitoring from internal governance mechanisms is weak and ineffective, auditors are expected to do more substantive testing, hence higher audit fees are charged for these firms. The following hypothesis is, therefore, tested:

Hypothesis 3: Bumiputera-controlled firms pay higher external audit fees associated with poorer corporate governance practices.

Research Design

Data Collection and Sample Selection

The sample comprises the Bursa Malaysia non-financial public listed companies whose annual reports are available in 2003. Finance-related firms are excluded due to their unique characteristics and different compliance and regulatory environment. The firms in the sample are either listed on the Main Board or the Second Board of the Bursa Malaysia[5]. Both the financial and corporate data of these firms are obtained from their annual reports. These annual reports are available and downloadable from the website of the exchange (http://announcements.bursamalaysia.com). Listed firms are required to disclose both non-audit fees and audit fees (statutory audit fees) in their annual reports.

The number of firms listed on the Bursa Malaysia at the end of 2003 is 874 firms (excluding firms listed on Malaysia Exchange of Securities Dealing and Automated Quotations Berhad (MESDAQ)). Thirty-two firms do not have their annual reports available, while sixty-
one firms are involved in finance-related activities. The study also excludes forty-five firms that are newly listed[6]. The final sample consists of 736 firms. A total of 496 firms are listed on the Main Board of the Bursa Malaysia and the remaining firms are listed on the Second Board. Just over three quarters of the sample represent three major sectors classified by the Bursa Malaysia namely Industrial Products (237 firms), Consumer Products (119 firms), and Trade and Services (163 firms). The remaining firms in the sample are in sectors including Property (86 firms), Constructions (57 firms), Technology (19 firms), Plantations (40 firms), Infrastructure Companies (6 firms), Hotel (6 firms), and Mining (3 firms).

**Variable Measurements and Model Specification**

Consistent with existing literature on determinants of audit fees, this study employs the traditional audit fee model introduced by Simunic (1980) and modified by Craswell et al. (1995). In addition to using variables that are proxies for internal corporate governance structures (i.e., board and audit committee characteristics), the study also includes control variables identified by prior research that explain the cross-sectional variations in audit fees (Simunic et al., 1987; Francis et al., 1987; Craswell et al., 1995). These variables include client size, number of subsidiaries, audit quality, leverage, profitability, receivable and inventory intensity, and industries. The following regression equation is used as the primary model to test the hypotheses previously discussed. It is also important to note that this is not the only model used in the study. There are several other alternative models employed to test the validity of the primary model.

\[
LAF = b_0 + b_1 SIZE + b_2 SUBS + b_3 LEV + b_4 REC + b_5 INV + b_6 ROA + b_7 BIG4 + b_8 INDUSTRYDUMMIES + b_9 BoardIndependence + b_{10} Dual + b_{11} BoardSize + b_{12} RMC + b_{13} BoardMeet + b_{14} ACIndependence + b_{15} ACSize + b_{16} ACExpertise + b_{17} ACMeet + b_{18} BumiOwned + e
\]

Where:

- **LAF** = natural log of audit fees.
- **SIZE** = natural log of total assets.
LEV = total book value of debt to total assets.
SUBS = square root of the number of direct subsidiaries.
REC = the ratio of receivables to total assets.
INV = the ratio of inventories to total assets.
ROA = returns on Assets (the ratio of earnings before interests and taxes to total assets).
BIG4 = a dummy variable of 1 if financial statements audited by Big 4 audit firms, 0 otherwise.
INDUSTRY DUMMIES = a dummy variable of 1 if a firm is in Industrial Product sector, or in Consumer Product sector, or in Construction sector, or in Technology sector, or in Trade and Services sector, or in Property sector, or in Plantations sector, or in Hotel sector, or in Infrastructure Companies sector, or in Mining sector, 0 if otherwise.
BoardIndependence = the proportion of independent non-executive directors on boards.
Dual = a dummy variable of 1 if the role of the Board Chair and the CEO is separated, 0 if otherwise.
BoardSize = total number of directors on boards.
RMC = a dummy variable of 1 if a firm establishes a risk management committee, 0 if otherwise.
BoardMeet = the number of board meetings held during the financial year.
ACIndependence = the proportion of non-executive directors on audit committees.
ACSize = total number of directors on audit committees.
ACExpertise = the proportion of audit committee members with accounting and finance qualifications.
ACMeet = the number of audit committee meetings held during the financial year.
BumiOwned = a dummy variable of 1 if a firm’s shares outstanding are substantially held by Bumiputera shareholders[7].

Dependent Variable

The Companies Act 1965 of Malaysia requires companies to disclose their non-audit and audit fees in their notes to accounts. The figure was therefore collected from company annual reports. The fees are then transformed into natural logarithm and are used as the dependent variable. The natural log is used to control for the skewed nature of audit fees.

Hypothesised Variables
Recall that experimental variables tested in hypotheses are board and audit committee characteristics, and board ethnicity. Consistent with prior studies, this study tests the assertion that Boards of Directors that are more independent, have a smaller number of members, establish a risk management committee, and meet more frequently pay lower external audit fees (Hypothesis 1). Two measures of board independence are used in this study namely the proportion of independent non-executive directors on boards and whether different individuals hold the positions of the Board Chair and the CEO. An independent non-executive director is a director who is not employed to run the firm’s day-to-day business activities, and whose role is to provide an outsider’s contribution and oversight to the board of directors (Hanrahan et al., 2001).

The study also posits in Hypothesis 2 that firms with more independent, diligent, expert, and larger audit committees are likely to pay lower external audit fees. Audit committee independence and expertise are measured by the proportion of non-executive directors on the committee and the proportion of audit committee members with accounting and finance qualifications respectively (Goodwin-Stewart et al., forthcoming). The proxies used to measure audit committee diligence and size are the frequency of audit committee meetings held during the financial year and the number of directors on the audit committee respectively. Finally, the study also predicts that Bumiputera-controlled firms pay higher levels of external audit fees associated with their poor internal governance structures (Hypothesis 3). The ethnicity variable is measured using a dichotomous variable set as 1 if a firm’s outstanding shares are substantially held by Bumiputera shareholders, 0 if otherwise[8].

Control Variables

We expect audit fees to be positively related to the natural log of total assets, leverage, receivable and inventory intensity, and square root of the number of subsidiaries. The effects of these variables are controlled in our analysis. For instance, profitability is controlled by
including return on assets and it is expected to be negatively associated with audit fees. The study also includes a dummy variable for Big Four accounting firms to control for differences in audit quality. Further, there are likely to be variations in audit fees across companies in different industries (Low et al., 1990). Therefore, in order to control for industry variations, ten industry dummy variables according to sectors classified by the Bursa Malaysia are included in the equation. The sectors are industrial products, consumer products, technology, construction, trade and services, properties, plantations, hotel, mining, and infrastructure companies.

Results

Descriptive Statistics

Table I provides descriptive statistics for the variables employed in the model. Panel A reports those for continuous variables and Panel B presents those for dichotomous variables. In general, the distributions are similar to previous studies undertaken in the Malaysian market (Eichenseher, 1995; CheAhmad et al., 2001). For instance, the average audit fees of RM191,975 in this sample is slightly higher than those documented by Eichenseher (1995) and CheAhmad et al. (2001) where the average audit fees in their samples are RM113,000 and RM137,780 respectively. The mean asset size of RM1,167,849,518 is lower than that reported by CheAhmad and Houghton (2001) but higher than that found by Eichenseher (1995) which are RM1,290,316,000 and RM615,000,000 respectively. There are some 506 firms (68.8 percent) using Big Four external auditors.

Take in Table I

Of particular interest to the study are the corporate governance variables. The Listing Requirements of Bursa Malaysia 2001 require all public listed firms to have audit committees comprising at least three members, the majority of whom must be independent. The size of audit committees ranges from 2 to 7, with a mean of 3.49[9]. On average, the firms in the sample have their audit committees comprised of at least three non-executive members (about
79 percent of audit committee members are non-executive directors). Further, some 252 (one-third) firms in the sample have formally established a Risk Management Committee. The majority of firms in the sample also separate the positions of the Board Chair and the CEO (about 84 percent of the firms practice dual leadership).

The average number of non-executive directors on Malaysian boards is 4.74, ranging from a minimum of 1 to a maximum of 12 non-executive board members (63 percent of overall board members are non-executives). The number of directors on Malaysian boards is between 3 and 16 with an average board size of 7.51. There are 205 firms whose Boards of Directors are predominantly Bumiputeras. Finally, there are some 135 firms whose outstanding shares are substantially held by Bumiputra shareholders.

**Take in Table II**

Table II reports the correlations between the variables used in the regressions. The correlation matrix reveals that few variables are highly inter-correlated (above 0.5). Variables with high significant correlations include natural log of total assets and natural log of audit fees (0.741), the ratio of current assets to total assets and the ratio of receivables to total assets (0.574), and the proportion of non-executive directors on boards and the proportion of non-executive directors on audit committees (0.569). While a few governance variables are significantly correlated with each other, their correlations do not indicate that multicollinearity is a serious problem. As shown in Table II, the correlations range from 0.448 (between board size and audit committee size) to 0.503 (between the frequency of board meetings and audit committee meetings)[10].

**Multivariate analysis**

*Regression results of the association between external audit fees and control variables (Traditional Audit Fee Model)*
Table III presents the ordinary least square regression results for testing the hypotheses. In testing the validity of models used in the study, the traditional audit fee model introduced by Simunic (1980) is employed whereby the natural log of audit fees is regressed on the control variables only[11]. Results in Model 1 show the association between external audit fees and control variables derived from the extant literature (Francis et al., 1987; Simon et al., 1988; Francis et al., 1986) as independent variables[12]. The model is significant (p<0.01), with an adjusted R-square of 69.6 percent.

**Take in Table III**

Following prior research (Simunic, 1980; Francis et al., 1987; Simon et al., 1988; Craswell et al., 1995), it is expected that audit fees are positively associated with size, receivables and inventory intensity, leverage[13], the number of subsidiaries, and whether a firm uses Big Four auditing firms. The coefficients for these control variables are in the predicted direction and significant (p<0.01) except for the use of Big Four audit firms. The strong negative association between audit fees and return on assets (ROA) is also consistent with findings previously documented (Simunic, 1980; Craswell et al., 1995; Gul et al., 1998). The industry controls are also included (the regression estimates for industry variables are not reported in Table III) in all regressions presented in Table III. Overall results show that audit fees are not significantly related to all industry variables[14].

*Regression results of the association between external audit fees and internal governance structures.*

Model 2, which regresses external audit fees on control variables and the test variables of interest, is significant (p<0.01) with an adjusted R-square of 69.8 percent. The results reported in Model 2 show that external audit fees are positively and significantly associated with the proportion of independent non-executive directors on boards (p<0.05), audit committee
expertise (p<0.05), and audit committee meeting frequency (p<0.10). There is also a negative association between external audit fees and Bumiputera-controlled firms (p<0.10).

A number of board characteristics and audit committee characteristics are highly correlated (i.e., board size and audit committee size, the proportion of independent directors on boards and the proportion of independent directors on audit committees, and the frequency of board and audit committee meetings), and potentially lead to multicollinearity between variables. Therefore, two regressions are run to separately test the association between external audit fees and the board and audit committee characteristics. In addition, consistent with Beasley (1996) and Carcello et al. (2002), Model 3 in Table III focuses on the full Board of Directors characteristics, which also include the existence of a risk management committee[15]. Model 3, which regresses external audit fees on the control variables and on the five variables of interest, is significant (p<0.01) with an adjusted R-Square of 69.6 percent. The results in Model 3 indicate that there is a strong positive association between external audit fees and the percentage of independent non-executive directors on boards (p<0.05). The results in Model 3 also show that external audit fees are not significantly related to dual leadership, board size, the frequency of board meetings, and the existence of a risk management committee[16]. Recall that Hypothesis 1 predicts that lower external audit fees are associated with boards that are more independent, have a smaller number of members, establish a risk management committee, and meet more frequently. Using a risk-based perspective of audit services, it appears that the results do not support Hypothesis 1 as there is no negative significant association between external audit fees and these governance variables.

Hence, the findings do not support the view widely held in the financial reporting and governance literature (Jensen, 1993; Beasley et al., 2000; Dechow et al., 1996; Davidson et al., 2005) that greater board independence, smaller board size, and the existence of an internal control mechanism (as per the existence of a risk management committee) are likely to reduce
risks associated with the financial reporting process. With respect to the significant association between external audit fees and the proportion of independent non-executive directors on boards, the finding is similar to those of recent studies by Carcello et al. (2002), Abbott et al. (2003), and Goodwin-Stewart et al. (forthcoming). These studies report that board independence is positively associated with audit fees, suggesting independent boards are likely to demand a higher quality audit from external auditors, resulting in higher audit fees. Based on the propositions that directors wish to protect their reputational capital (Fama, 1980; Fama et al., 1983a, b; Gilson, 1990), to avoid legal liabilities (Gilson, 1990), and to protect shareholder wealth, firms with a stronger control environment may seek differentially higher quality audit services. The auditors are likely to incorporate the costs of providing these differentiated and higher quality audit services into the audit fees, resulting in higher audit fees.

Recall that a number of board and audit committee characteristics are highly correlated and this potentially leads to multicollinearity problems. Model 4 in Table III addresses this issue by regressing external audit fees on control variables and on the four audit committee variables of interest. The model is significant (p<0.01) with an adjusted R-square of 69.8 percent[17].

The results reported in Model 4 show that external audit fees are significantly associated with audit committee expertise (p<0.05) and the frequency of audit committee meetings (p<0.05). External audit fees, however, are not significantly related to audit committee independence and audit committee size. From a risk-based perspective of audit services, the results with respect to the association between external audit fees and audit committee characteristics do not support Hypothesis 2. The results are consistent with the demand approach of audit services in that more expert and diligent audit committees are likely to seek higher quality audits from external auditors, resulting in higher audit fees (Carcello et al. 2002; Abbott et al., 2003). One interpretation with respect to the positive significant association
between external audit fees and audit committee expertise is that audit committee members who possess professional certifications (i.e., Certified Public Accountants and Chartered Accountants) may seek to protect their reputations as experts in accounting and financial matters and are likely to demand increased monitoring (Fama and Jensen, 1983a, b; Gilson, 1990).

External Audit Fees and Bumiputera-controlled firms

Recall that the study also posits that firms whose directors are predominantly Bumiputeras are expected to pay relatively higher audit fees associated with poorer corporate governance practices (Hypothesis 3). The results in Model 2 in Table III show that there is a significant negative association between external audit fees and the ethnicity variable measured using a dichotomous variable of whether a firm’s outstanding shares are substantially held by Bumiputeras or otherwise ($p<0.10$)[18]. This indicates that Bumiputera-controlled firms pay lower audit fees than Non-Bumiputera controlled firms, which is the opposite to the prediction of Hypothesis 3. This result is not consistent with those documented by Eichenseher (1995) and CheAhmad et al. (2001) in which they report that Bumiputera-controlled firms pay higher external audit fees than their Non-Bumiputera controlled counterparts (i.e., ethnic Chinese-controlled firms). Two possible explanations for this difference in findings are the changes in the regulatory environment during late 1990s and in 2001 and the differences in increased focus on board and audit committee oversight responsibilities. These are likely to have strengthened the motivation of Boards of Directors and audit committees to act in a manner inconsistent with our hypotheses.

Additional testing of Hypothesis 3 is undertaken by an investigation into internal governance structures of both Bumiputera-controlled and Non-Bumiputera controlled firms. An examination of internal governance structures is likely to help explain the lower audit fees paid by the Bumiputera-controlled firms as reported in the previous section.
Additional tests of corporate governance structures of firms

The proportion of Bumiputera directors on boards is regressed against the set of control variables and governance variables used in the study. An independent sample t-test is also conducted to compare means of internal governance structures for Bumiputera-controlled and Non-Bumiputera controlled firms.

T-tests for internal governance variables for firms grouped as Bumiputera firms (assigned value of 1) and those Non-Bumiputera firms (assigned value of 0) are presented in Table IV. With the exception of audit committee expertise, there is a significant (p < 0.05) difference in internal governance structures for Bumiputera-controlled and Non-Bumiputera controlled firms. The t-test results are confirmed by non-parametric Mann-Whitney U tests. Chi-Square tests are conducted for dichotomous variables (i.e., dual leadership structure and the existence of a risk management committee) and indicate that there is a statistically significant (p<0.01) difference between Bumiputera-controlled and Non-Bumiputera controlled firms in their internal governance structures (dual leadership structure and the existence of a risk management committee).

Take in Table IV

Table V presents the results of a regression model using the proportion of Bumiputera directors on boards as the dependent variable, and the model is significant (p<0.01) with an adjusted R-square of 18.6 percent. The results in Table V indicate that boards of Bumiputera-dominated firms are more independent and these firms are more likely to separate the roles of the Board Chair and the CEO. This is evidenced by the strong positive association between the proportion of Bumiputera directors on boards and these two internal governance variables (p<0.01). Bumiputera-controlled firms also appear to have a better risk management environment as evidenced by the strong positive relation between the proportion of Bumiputera directors on boards and the existence of risk management committees (p<0.01).
Further, Bumiputera-controlled firms are more diligent as indicated by the strong positive association between the proportion of Bumiputera directors on boards and the frequency of board meetings (p<0.05).

**Take in Table V**

The results also show that audit committees of Bumiputera-controlled firms are more independent as indicated by a strong positive association between the proportion of Bumiputera directors on boards and audit committee independence (p<0.01). The proportion of Bumiputera directors on boards are not significantly related to audit committee expertise, audit committee meeting frequency, and audit committee size. Overall, these results do not support the view that Bumiputera-dominated firms have weaker governance environments relative to Non-Bumiputera controlled firms as previously suggested by Gomez and Jomo (1997) and Johnson and Mitton (2003).

With respect to the association between Non-Bumiputera controlled firms and their internal governance structures, these results appear to be consistent with the view that Chinese-controlled firms tend to have more inside directors on their Boards of Directors and are likely to have a unitary leadership structure (Weidenbaum, 1996; Redding, 1995). Chinese businesses do adopt some of the practices of western firms like recruitment of professional managers and some degree of public ownership. But essentially, the ownership stakes and control are still in the hands of family holding companies and family members. Therefore, it is likely that the selection of personnel for key positions such as Board Chair, CEO, and Managing Director, and Board of Directors is another way through which control of the company is maintained[19].

The study also explores the internal governance practices of Bumiputera-dominated boards using logistic regression analysis with the dependent variable set at 1 for firms whose board members are predominantly Bumiputeras and 0 if otherwise. Unreported results obtained using
The logistic regression method confirm those obtained using the ordinary least square method indicating that firms whose boards are predominantly Bumiputeras practice improved internal corporate governance practices relative to their Non-Bumiputera counterparts.

The results obtained in this additional analysis are likely to help explain the negative significant association between external audit fees and Bumiputera-controlled firms. It appears that Bumiputera-controlled firms practice favourable corporate governance practices relative to Non-Bumiputera firms and thus are likely to contribute to lower auditors’ risk assessments, resulting in lower external audit fees.

Conclusion

The unique institutional environment in Malaysia coupled with the presence of a clearly identifiable ethnic domination of corporate boards and ownerships of Malaysian listed firms potentially provides evidence of monitoring differences that exist in these firms. The study examines the link between external audit fees and internal governance structures and the element of ethnicity. Overall, we find that external audit fees are positively and significantly associated with board independence, audit committee expertise, and the frequency of audit committee meetings. In contrast to the findings documented by Eichenseher (1995) and CheAhmad et al. (2001), we document a significant negative relation between external audit fees and Bumiputera-owned firms.

An additional analysis also reveals that Bumiputera-controlled firms practice improved internal corporate governance practices compared to their Non-Bumiputera counterparts. This finding supports the result obtained earlier wherein Bumiputera-controlled firms pay lower external audit fees because their internal governance structures are stronger relative to their Non-Bumiputera counterparts. With respect to the association between external audit fees and governance variables, the results do not support the risk-based perspective of audit services (i.e., good corporate governance practices reduce external audit fees). The results, however, are
consistent with the demand approach of audit services, wherein firms with good corporate governance attributes demand higher audit quality, resulting in higher external audit fees.

While our study makes an important contribution to the governance debate, there are a number of limitations that are inherent in this current study. One of the limitations is that the results of this study cannot be generalised and should be interpreted in the context of the Malaysian corporate environment, particularly where ethnicity is concerned. Further, the financial and corporate data employed in this study and the findings thereafter may not completely explain the link between governance variables and external audit fees as other variables such as detailed ownership structures are likely to better explain the relationship. In addition to archival data, data gathered using survey methods for instance are also likely to provide better insights to findings of this study.
Notes

1. Bumiputera means in Malay “sons of the soil”. It refers to Malays and other indigenous people as distinct from Chinese, Indians, and other non-indigenous residents.

2. The Kuala Lumpur Stock Exchange (KLSE) became de-mutualised exchange and was renamed Bursa Malaysia in April 2004.

3. It is also important to note that recent studies have documented the link between audit committee member independence and audit fees from a demand approach of audit services. For instance, Abbott et al. (2003) find that audit committee independence and other audit committee characteristics (i.e., expertise and diligence) are positively related to audit fees. They suggest that an independent, expert, and diligent audit committee demands increased audit coverage or purchases a higher-quality audit, hence higher audit fees. Independent audit committee directors are likely to view their service on an audit committee as a means of enhancing their reputational capital (Fama and Jensen, 1983a, b). The preservation of reputational capital serves as one motivation for higher quality reporting.

4. It is also important to note that recent studies have documented the link between audit committee member independence and audit fees from a demand approach of audit services. For instance, Abbott et al. (2003) find that audit committee independence and other audit committee characteristics (i.e., expertise and diligence) are positively related to audit fees. They suggest that an independent, expert, and diligent audit committee demands increased audit coverage or purchases a higher-quality audit, hence higher audit fees. Independent audit committee directors are likely to view their service on an audit committee as a means of enhancing their reputational capital (Fama and Jensen, 1983a, b). The preservation of reputational capital serves as one motivation for higher quality reporting.

5. The Main Board companies have a minimum paid-up capital of Ringgit Malaysia (RM) 60 millions while the Second Board companies are those that have a minimum paid-up capital of RM40 millions.

6. Following Abbott et al. (2003), firms in their first year of public trading are excluded because it is expected that these firms require an initial period of time post initial public offerings to appoint an audit committee and effectively transfer functions to the committee and for the committee to meet. Some companies in the sample did not meet during the year as stipulated by the Listing Requirements of Bursa Malaysia because they were new listings. The Listing Requirements of Bursa Malaysia requires audit committees of its listed firms to meet at least four times a year.

7. In compliance with the Companies Act 1965, all listed firms disclose their substantial shareholders including their 30 largest shareholders in their annual reports. The Bumiputera shareholding percentage is based on the 30 largest shareholders. Therefore, a Bumiputera-controlled company (by virtue of their largest shareholdings in a company) is one in which 50% or more of the 30 largest shareholdings is held by government and semi-government agencies, Bumiputera individuals, Bumiputera-owned companies, and Bumiputera trust agencies. The same categorisation procedure is used to identify Non-Bumiputera shareholdings.

8. Other measures of ethnicity used in this study include (1) the proportion of Bumiputera directors on boards; (2) a dichotomous variable set as 1 if a Board of Directors is predominantly Bumiputeras, 0 if otherwise; and (3) the proportion of Bumiputera substantial shareholdings. The ethnicity of the board of directors is determined by examining the names of directors. If the names are of Chinese origin, for example, having surname of Tan, Chan, or Lee, the criterion is satisfied, that is, the director is assumed to be Chinese. A similar approach is also used for directors who are Non-Bumiputera (i.e., foreign directors or other ethnicities other than Bumiputeras or Malays). For Bumiputera names or Malay names, the same procedure is used. The Board of Directors is categorised as Non-Bumiputera directors in the case of uncertainties between Bumiputera directors and Non-Bumiputera directors (Eichenseher, 1995). This categorization rule is based on the notion that government pressure is exerted

9. All companies have at least three members on their audit committees except Johan Holdings Berhad, KPS Consortium Berhad, and UCP Resources Berhad which have two directors on their audit committees.

10. Two tests are performed to detect multicollinearity. First, variance inflation factor (VIF) scores reveal no problems with multicollinearity (all scores are less than 2). Second, per Besley et al. (1980), the condition indices are calculated. The condition index is less than 30 indicating weak relations among the independent variables (Besley et al., 1980). Therefore, it appears that multicollinearity is not a problem. The study performs a number of diagnostics on the regressions reported in Table III, and in those reported in subsequent analyses, including investigation of outliers for both control and governance variables. The variables with univariate outliers include size, leverage, receivables and inventory intensity, frequency of both board and audit committee meetings, and board size. To test whether outliers alter the results, the outlying observations whose standardised z-scores exceed ±3 are excluded and the regressions are re-run. The unreported regression results are qualitatively similar as those reported in Table III. Tests are also conducted to detect heteroscedasticity. The Breusch-Pagan-Godfrey (B-P-G) test indicates that a heteroscedasticity problem exists. White’s (1980) heteroscedasticity consistent covariance matrix is performed for all regressions run in this study to help correct the problem.
11. The study performs a number of diagnostics on the regressions reported in Table III, and in those reported in subsequent analyses, including investigation of outliers for both control and governance variables. The variables with univariate outliers include size, leverage, receivables and inventory intensity, frequency of both board and audit committee meetings, and board size. To test whether outliers alter the results, the outlier observations whose standardised z-scores exceed ±3 are excluded and the regressions are re-run. The unreported regression results are qualitatively similar as those reported in Table III. Tests are also conducted to detect heteroscedasticity. The Breusch-Pagan-Godfrey test indicates that a heteroscedasticity problem exists. White’s (1980) heteroscedasticity consistent covariance matrix is performed for all regressions run in this study to help correct the problem.

12. To address the potential effect of listed board, a dichotomous variable (i.e., whether a firm is listed on the Main Board or the Second Board of the Bursa Malaysia) is included in the regressions. The unreported results show that external audit fees are positively and significantly associated with the BOARD variable (the coefficient = 0.108; t-statistic = 2.204; p-value = 0.028). The unreported correlation indicates that this variable is highly correlated with the SIZE variable (0.511; significant at the 0.01 level; two-tailed). Because of high correlation between the BOARD and the SIZE variables, the study drops the BOARD variable from the regressions. Regression results remain qualitatively and statistically unchanged when the variable is included (or excluded) from the regressions.

1 As an alternative measure of leverage, the ratio of long-term debt to total assets (LTDebt/TA) is used in place of the ratio of total debt to total assets (a variable denoted as Leverage in the regressions throughout the study). The unreported results show that there exists a positive association between external audit fees and the ratio of long-term debt to total assets. The positive association, however, is not statistically significant (the coefficient = 0.252; t-statistic = 1.497; p-value = 0.135).

13. As an alternative measure of leverage, the ratio of long-term debt to total assets (LTDebt/TA) is used in place of the ratio of total debt to total assets (a variable denoted as Leverage in the regressions throughout the study). The unreported results show that there exists a positive association between external audit fees and the ratio of long-term debt to total assets. The positive association, however, is not statistically significant (the coefficient = 0.252; t-statistic = 1.497; p-value = 0.135).

14. External audit fees are not significantly associated with Industrial Products (p-value = 0.827), Consumer Products (p-value = 0.665), Constructions (p-value = 0.852), Technology (p-value = 0.563), Trade and Services (p-value = 0.495), and Hotel (p-value = 0.638). There also exists a non-significant negative association between external audit fees and Property (0.909), Plantations (p-value = 0.985), and Infrastructure Companies (p-value = 0.529) sectors. In order to have parsimonious models and also due to their non-significant associations with external audit fees, the industry variables are excluded and regressions are re-run. The results remain qualitatively and statistically unchanged after excluding the industry variables from the regressions. It is also important to note that the adjusted R-square for the regression with industry variables is 70.6 percent, which is about 0.01 percent higher than that without industry variables (see R-square in Model 1 in Table III). Other control variables also remain qualitatively and statistically unchanged.

15. The ethnicity variable is excluded because Model 3 seeks to investigate the association between external audit fees and board characteristics, which are largely found in the existing literature.

16. The study also further examines whether board size is likely to be influenced by size of companies measured by total assets. One would argue that larger companies are likely to have more directors on their boards to reflect complexity of their operations and diversifications of the company. Therefore, a greater number of directors with diverse expertise and greater facilitation of task assignments are required. The study, therefore, scales board size by total assets. When this transformed variable is included in the regressions and the regressions are re-run, the results obtained containing this variable is statistically similar to those of absolute value of board size, indicating that board size is not influenced by the size of the company.

17. An explanation for the adjusted R-Squares being almost the same for all models is that control variables consistently explain more variation in external audit fees than governance variables. Governance variables provide little incremental explanatory power. Notwithstanding that, the strong association between external audit fees and governance variables appear to support existing empirical evidence from the demand approach of audit services.

18. There are some mixed results with respect to other measures of ethnicity. For instance, when measured using the proportion of Bumiputera directors on boards, the proportion of Bumiputera substantial shareholdings, and a dichotomous variable of whether a firm’s Board of Directors is predominantly Bumiputeras, the association between external audit fees and these variables are not statistically significant.

19. The majority of businesses in Malaysia are owned and operated by Chinese (Horii, 1991). Chinese businesses generally have some common characteristics. These characteristics include centralised decision-making with heavy reliance on one dominant chief executive, family ownership and control, and most if not all top management positions are filled with family members.
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