

Study on the Impact of Related Party Transactions on Audit Opinions

-- Based on the A-share Manufacturing Industry

Ao Guo

School of Management, Northwest University of Political Science and Law, Shaanxi 710000,
China

Abstract

With the continuous expansion and development of the capital market, fraudulent means using related transactions appear frequently. As a special transaction with "two sides" at present, related party transactions are often accompanied by higher audit risks during auditing. However, do related party transactions have an impact on the type of audit opinion issued by the auditor? This paper selects the secured mortgage with the highest proportion of related party transactions as the research object, and explores its influence on the type of audit opinion. The results show that listed companies with collateral related party transactions are more likely to be issued non-standard audit opinions than listed companies without such transactions.

Keywords

Related Party Transactions; Mortgage Guarantee; Audit Opinion; Listed Company.

1. Introduction

According to the provisions made by the Accounting Department in the "Accounting Standards for Business Enterprises No. 36" document, it can be traced back to the definition of related parties: "One party controls, jointly controls or exerts significant influence on the other party, and two or more parties have the same If it is controlled, jointly controlled or significantly influenced by one party, it constitutes a related party". Since this article is based on the perspective of listed companies, the related parties are defined as holding or being held more than 5% of the shares of the other company in combination with the listing rules (that is, constituting direct or indirect control). According to the current accounting standards, related party transactions refer to the mutual transfer of labor services, obligations, and resources between a listed company and its related parties. As far as the current listed company data is concerned, there are as many as 21 types of transactions between related parties and transaction entities, and the more common types are mainly the four mentioned in the abstract. With the continuous expansion of my country's capital market and the scale of enterprises, this kind of "transfer" between related parties has become more and more common and hidden, and due to the nature of related relationships and transactions, related party transactions may be more common than non-related parties. Transactions carry a higher risk of material misstatement of financial statements. As an independent third party, the accounting firm in charge of auditing should pay more attention and prudence to related-party transactions when verifying the economic activities of the audited entity, so as to avoid investing investment due to improper presentation of audit opinions. and other stakeholders suffer losses. Based on this, this paper uses empirical research to explore whether related party transactions of collateralized mortgages have an impact on the type of audit opinion issued. It provides practical significance and practical value in improving the research on the relationship between related party transactions and audit opinions.

2. Literature Review

Lv Weilin Zhaocheng (2007) examined the relationship between related party transactions, audit opinions and external supervision mechanisms. The results of the study found that the amount of purchases and sales by related parties of the company and the controlling shareholder will have an impact on the non-standard audit opinions issued by certified public accountants. There is a positive correlation between the two, and the non-standard audit opinion issued by the Board of Directors will have an inhibitory effect on the purchase and sale activities between the related parties of the controlling shareholder in the next year. Rayong and Jiang Suzhi (2014) found that the amount of related party asset transactions of listed companies and the negotiated pricing method used in the transaction will increase audit fees. According to the findings of this study, it indirectly means that more audit resources are consumed when auditing asset transactions between related parties. Huang Fang and Zhang Guiqiao (2015) found in their research that there is a significant positive correlation between the amount of related party transactions and non-standard opinions, and the correlation between the first two has been significantly improved after the promulgation of the new auditing standards. Li Yulan and Ren Xuebin (2017) divided related party transactions into decision-useful and opportunistic types according to their motivations, and finally found that the two types have completely different effects on audit opinions. Wu Xiaolu (2020) found through theoretical research that the financial status of the company, the quality of internal control, and the size of the firm all affect the type of audit opinion to varying degrees. On the one hand, we need to consider other factors that will affect the type of audit opinion when conducting empirical research through the retrospective and sorting out of the related literature related to auditing. On the other hand, the relationship between related parties includes not only the purchase and sale relationship, but also other types of related party transactions. However, as far as the current articles on the relationship between related party transactions and audit opinions are concerned, most of the articles focus on related party transactions. There are few studies on the relationship between the amount of money and the audit opinion, and there are few studies on transactions of different types of associations.

This article is based on a statistical analysis of the affiliated transactions of listed companies in my country's A-share manufacturing industry in 2020, see Fig. 1:

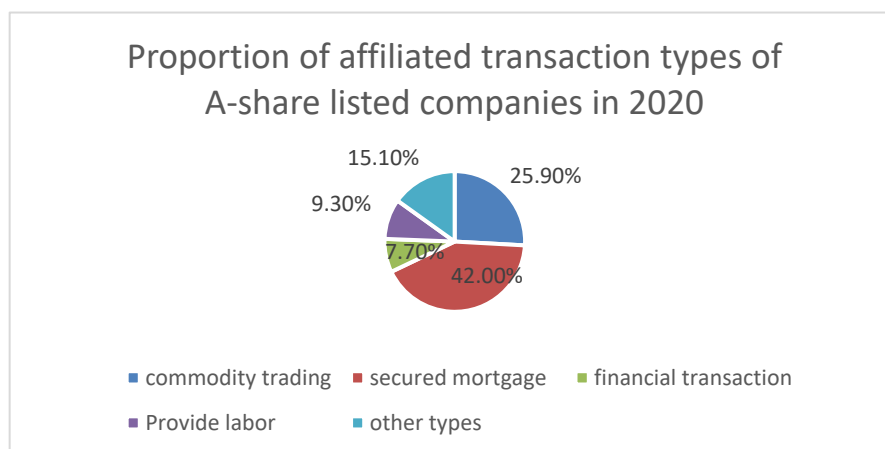


Figure 1. Pie chart of the proportion of affiliated transaction types of A-share listed companies in 2020

The pie chart obtained by filtering the data through Excel: Among the related party transactions conducted by my country's A-share listed companies in 2020, commodity transaction related accounts accounted for 25.9%, secured mortgage related accounts accounted for 42.0%, and

capital transactions accounted for 42.0%. Related-party transactions accounted for 7.7%, and related-party transactions for providing or receiving labor services accounted for 9.3%. It is not difficult to see from the statistics that the secured mortgage connection accounts for almost 1/2 of all transactions. Based on this, this paper selects the largest proportion of related party transactions in the secured mortgage type from the four more common types of commodity transactions, secured mortgages, capital transactions, and the relationship between providing or being provided labor services. Its impact on the type of audit opinion.

3. Research Design

3.1. Problem Formulation and Research Hypothesis

Compared with general enterprises, the internal related party transactions of listed companies occur more frequently, and their activities are more complex and hidden. As for the main forms of secured mortgage related transactions, there are guarantees for major shareholders, guarantees for subsidiaries or direct holding guarantee companies, etc., which makes the transaction likely to lose its fairness. These factors also ultimately make the CPA's audit of the related party transactions of listed companies riskier, which invisibly increases the difficulty of CPA's audit. Based on the competitiveness of the audit market and the cost-effectiveness principle of certified public accountants in conducting audits, most firms will increase audit fees accordingly. In addition, related party transactions bring higher risks of material misstatement and inspection. Therefore, when the audit work is completed, the certified public accountant is more likely to issue a non-standard audit opinion on such related party transactions.

In summary, the research hypothesis of this paper is put forward: whether there is a guarantee mortgage between related parties is related to the type of audit opinion.

3.2. Model Design and Variable Definition

3.2.1. Model Design

The explained variable in this paper is opinion; the explanatory variable is mortgage; the control variable is size, Top1, Lever, Profit, Recevier, Big4. Build a regression model to analyze the hypotheses as follows:

$$\text{Opinion} = \alpha + \beta_1 \text{mortgage} + \beta_2 \text{size} + \beta_3 \text{Top1} + \beta_4 \text{lever} + \beta_5 \text{Profit} + \beta_6 \text{Recevier} + \beta_7 \text{Big4} + \varepsilon$$

3.2.2. Variable Definition

Explained variable: The audit opinion is the explained variable (ie dependent variable) of this paper, which is expressed by opinion. Opinion takes a value of 0 if and only if the certified public accountant issues a standard unqualified audit opinion, and takes a value of 1 when issuing four types of opinion other than standard unqualified opinion.

Explanatory variable: The explanatory variable (ie independent variable) of this paper is whether there is a mortgage guarantee between related parties in the listed company, which is represented by mortgage. If the listed company has related-party transactions of collateral and mortgage type, it will be assigned 1; if it does not, it will be 0.

Control variables: Since the audit opinion issued by the certified public accountant is also affected by other factors, the following control variables need to be included in the study of the impact of related party transactions on the audit opinion:

The size of the enterprise, expressed in Size. Due to the large amount of total assets of the company, in order to achieve the simplicity of operation without changing the nature of the original variables, it is calculated by taking the natural logarithm of the total assets of the listed company at the end of the period.

The shareholding ratio of the largest shareholder, represented by Top1. Yang Xiaodan (2015) and others used R language and multiple correspondence analysis to find that a dominant company is more likely to obtain a standard unqualified audit opinion.

The asset-liability ratio, expressed as Lever, is calculated by the ratio of total liabilities to total assets at the end of the period.

Operating net profit margin, expressed as Profit. It is usually a representative of the profitability of a company, calculated by the ratio of net profit to operating income.

The proportion of accounts receivable, expressed in Recevier. Calculated by the ratio of net accounts receivable to total assets at the end of the period.

The size of the firm, represented by Big4. If the audit firm is in the top four in the international rankings, take 1; otherwise, take 0.

4. Empirical Testing and Analysis

4.1. Descriptive Statistics

Table 1. Descriptive statistics of all variables (n=2628)

Descriptive Statistics					
Variable	Obs	Mean	Std. Dev.	Min	Max
opinion	2628	.027	.163	0	1
size	2628	22.069	1.186	18.335	27.547
big4	2628	.051	.22	0	1
top1	2628	32.411	14.095	2.866	89.991
recevier	2628	.132	.093	0	.737
lever	2628	.38	.195	.014	3.051
profit	2628	-.15	10.81	-553.614	1.34
mortgage	2628	.667	.471	0	1

From the descriptive statistics of all variables in Table 1, it can be seen that among the sample of 2,628 listed companies, there are 72 listed companies whose financial reports have been issued non-standard audit opinions, accounting for 2.7% of the total number of samples; The difference between the maximum value and the minimum value of the selected listed companies in each sample is not large, indicating that the selected manufacturing companies are of appropriate and comparable scale, which is in line with the reason for our initial selection; the audit unit is the international big four accounting firms There are 134 listed companies, accounting for 5.1% of the total number of samples; the difference between the maximum value and the minimum value of equity concentration is large, and the average value is 32.41, indicating that the situation of each listed company is different and the average equity concentration is not high; although the inventory turnover rate is There is a large gap between the maximum and minimum values, but the average value is 13.2%, indicating that most companies have good capital turnover; in terms of asset-liability ratio, the average value is 38%, which is less than 40%, indicating that most companies have certain problems. Debt pressure; among the sample listed companies, there are 1752 listed companies with mortgage-guarantee related relationship, accounting for 66.6%, indicating that more than half of the listed companies in the research sample have related-party transactions of mortgage-guarantee.

4.2. Correlation Test

Perform a correlation test for all variables in the model, where: * means correlation at the 1% significance level.

Table 2. Correlation test of all variables

Correlation test								
	opinion	size	big4	top1	recevier	lever	profit	mortgage
opinion	1							
size	-0.0378	1						
	0.0525							
big4	-0.0389	0.2901*	1					
	0.0461	0						
top1	-0.0936*	0.0597*	0.1135*	1				
	0	0.0022	0					
recevier	0.0520*	-0.1746*	-0.0844*	-0.0669*	1			
	0.0077	0	0	0.00060				
lever	0.1810*	0.4150*	0.0410	-0.0709*	0.1656*	1		
	0	0	0.0356	0.00030	0			
profit	-0.0046	0.0036	-0.0867*	0.00330	0.0274	0.025	1	
	0.814	0.853	0	0.867	0.161	0.200		
mortgage	0.0890*	0.1390*	-0.0820*	-0.0708*	0.1024*	0.3475*	0.0246	1
	0	0	0	0.0003	0	0	0.2080	

According to the results of the correlation test in Table 2, we can see that the explanatory variables guarantee, mortgage related party transactions (mortgage) and the explanatory variable audit opinion type (opinion) are significantly positively correlated at the 1% level, which is related to Our hypothetical expectations match. However, this does not mean that the existence of guaranteed related party transactions in listed companies will lead to non-standard audit opinions issued by the firm. Because the correlation test can only determine that there is a correlation between the two, that is, there is a correlation, but it cannot determine whether the explanatory variable has an effect on the explained variable or the opposite. Therefore, further regression analysis is required to determine the specific relationship between the two. Among the control variables, the size of the enterprise (size) is significantly negatively correlated with the ownership concentration (Top1) and audit opinion (opinion) at the level of 1%, indicating that the size and ownership concentration of the enterprise are both related to the type of audit opinion, and show a reverse change relationship. The asset-liability ratio (Lever), the proportion of accounts receivable (recevier) and the type of audit opinion (OP) are also correlated, and they are significantly positively correlated at the 1% significance level. To sum up, for the sake of prudence, certified public accountants should pay more attention to guarantee related party transactions (explaining variables) during the audit process, so as to reduce the inspection risk of certified public accountants during auditing, so as to ensure Audit work is maintained at a high-quality level.

4.3. Logit Binary Regression

In order to further test the influence of the audit opinion type of collateral related transactions, the Logit binary regression analysis was carried out on the explained variable opinion, explanatory variable mortgage, size and other control variables in the established model, and the results were as follows:

opioion	Coef.	Std. Err.	z	P> z	[95% Conf. Interval]	
size	-.3935122	.1350889	-2.91	0.004	-.6582817	-.1287428
big4	0	(omitted)				
top1	-.0346491	.011966	-2.90	0.004	-.0581021	-.0111961
recevier	1.174139	1.238275	0.95	0.343	-1.252835	3.601113
lever	3.431908	.7370657	4.66	0.000	1.987286	4.87653
profit	-1.455015	.2814829	-5.17	0.000	-2.006712	-.903319
mortgage	1.053483	.4470368	2.36	0.018	.1773067	1.929659
_cons	3.456022	2.932851	1.18	0.239	-2.29226	9.204304

Figure 2. Logit binary regression results analysis

According to the regression results in Figure 1, we can obtain the expression of the null hypothesis as:

Opinion=3.456022+1.053483mortgage-0.3935122size-0.0346491Top1+3.431908lever-1.455015Profit+1.174139Recevier. There is a linear correlation between the explained variable audit opinion type (Opinion) and the explanatory variable (mortgage), and there is a significant positive correlation at the 5% level. This result also verifies the initial assumption that related party transactions of collateralized mortgages will have an impact on the type of audit opinion issued. The control variables of enterprise scale, equity concentration, and operating net profit rate are significantly negatively correlated at the level of 1%, which indicates that the larger the scale of the enterprise, the more perfect its operation and management, so the certified public accountant issued a non-standard audit opinion during the audit. The lower the possibility; the higher the equity concentration, the higher the decision-making efficiency, which is beneficial to the company's internal business incentives to a certain extent, and the probability of being issued a non-standard audit opinion during the audit is also lower; The interest rate represents the operating performance of an enterprise. According to the regression results, the better the operating performance, the lower the possibility of the firm issuing non-standard audit opinions; the asset-liability ratio and audit opinions are significantly positively correlated at the level of 1%, indicating that The asset-liability ratio is an important indicator in the operation of an enterprise. The higher the asset-liability ratio of an enterprise, the lower the credibility of the enterprise and the concern of auditors, and the easier it is for certified public accountants to issue non-standard audit opinions on such enterprises; The proportion of accounts receivable is significantly negatively correlated with audit opinions at the level of 10%, indicating that the excessive proportion of accounts receivable will also increase the possibility of auditors issuing non-standard audit opinions on such enterprises, which also reflects Excessive proportion of accounts receivable of outgoing enterprises will bring more risks, which are reflected in the risk of bad debt loss and the risk of increased capital cost. This also reflects the defects of internal control of the enterprise (irrational credit policy). Certified public accountants are also more inclined to issue non-standard audit opinions due to risk considerations.

5. Research Conclusion

Based on the data of manufacturing companies listed on A-shares in 2020, this paper puts forward hypotheses and uses the logit model to conduct empirical analysis. The results show that there is a correlation between related party transactions and audit opinions, and it is significant at the 5% significance level. Positive correlation, that is, the existence of secured mortgage transactions in listed companies will increase the possibility of being issued non-standard audit opinions. Because as far as the current status of related-party secured transactions is concerned, when a company that is related to a listed company has a debt crisis, the listed company usually provides a guarantee for the related company to alleviate the debt

crisis of the related company, so as to keep the related company in the No bankruptcy or delisting in the short term. However, for the party providing the guarantee, it will expose its own enterprise to huge financial risks and potential operational risks. Therefore, the reason is that, on the one hand, due to the complexity of related party transactions in the collateral and mortgage type, it objectively increases the financial and operational risks of the enterprise; on the other hand, the auditors need to ensure the audit work out of the principle of prudence. When assessing the risk of guarantee related party transactions, certified public accountants tend to be more conservative and cautious, so it is easier for enterprises with guarantee related party transactions to issue non-standard audit opinions after the completion of the forensics work. Investors are reminded.

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