International Journal of Asian Business and Information Management
Volume 9 • Issue 2 • April-June 2018

Ownership Concentration, Family Control, and Auditor Choice:
Evidence From Iranian Companies

Mohammad Amoonejad, Department of Accounting, Bandargaz Branch, Islamic Azad University, Bandargaz, Iran
Mehdi Safari Geraily, Department of Accounting, Bandargaz Branch, Islamic Azad University, Bandargaz, Iran

ABSTRACT

The present study investigates the relationship between ownership concentration and family control, with the choice of high-quality auditors. For this purpose, a sample of 94 firms listed in the Tehran Stock Exchange during the years 2011 to 2015 were selected and the research hypotheses were tested using logistic regression model. The findings indicate that there is a significant positive relationship between ownership concentration and the choice of high-quality audit firms. However, there was not any evidence of a significant relationship between family ownership and a choice of high quality audit firms. The findings, in addition to filling the Empirical gap in this area can be useful for investors, the Tehran Stock Exchange and other stakeholders.

KEYWORDS

Ownership Concentration, Family Control, Auditor Choice

1. INTRODUCTION

With the start of joint-stock companies, owners delegated governance of corporations to managers. Separation of ownership and management (control) led to the advent of an organizational problem, known as the agency problem. Auditing is usually proposed in the presence of agency relations to reduce the conflict of interests. Independent auditors can reduce the agency costs by ensuring the stockholders about the quality of financial statements, and provide the stockholders with the opportunity to make exact, clear and efficient contracts with the managers based on the audited financial statements (Chen et al., 2007). audit conducted by independent auditors plays an important role in improving the quality and reliability of its financial information disclosure (Ferguson et al., 2004). A key element of good corporate governance system is to carry out auditing. Today, one of the controversial issues about validating companies' financial statements is choosing independent auditors for them. Quality of audit firms is directly related to the degree of their independence. Therefore, larger audit firms by virtue of having more customers, have higher auditing quality. In companies with concentrated ownership structure, agency problems often occur between major and minor shareholders, because in these companies, major shareholders are trying to take self-benefits from minor shareholders' expenses. These issues lead to information asymmetry in the capital market. In such circumstances, the demand for higher-quality independent auditors as a monitoring tool is increased (Darmadi, 2016).

DOI: 10.4018/IJABIM.2018040104

Despite extensive studies done on the factors affecting the auditor choice in developed countries (Beasley & the Patroni, 2001), few studies on the subject were conducted in developing countries, including Iran's capital market. Therefore, in this study, the main research question is whether there is a significant relationship between ownership concentration and family control with the choice of high-quality auditors. The important effect of high-quality auditing on improving reliability of financial reporting and consequently gaining the trust of investors in the capital market as well as the lack of adequate research on this issue, provided the impetus for the present study.

The current study has some major contributions to the previous literature, the most important of which include developing the theoretical foundations of the prior studies in accounting and finance, providing evidence on how size and ownership structure can influence audit firm choice to aid investors, capital market regulators and other accounting information users make informed decisions and finally, introducing a novel research area to accounting and finance researchers, particularly those studying capital market and accounting profession.

2. THEORETICAL FOUNDATIONS AND HYPOTHESIS DEVELOPMENT

There have been various points of view regarding ownership concentration in the accounting literature. On the one hand, based on active monitoring hypothesis, it can be argued that the major shareholders are long-term-oriented investors who have great motivation and ability to monitor managers actively (Lin & Liu, 2009). On the other hand, proponents of self-interest hypothesis believe that it is more likely that major investors take advantage of special interests, such as access to private information that could be used for trading purposes. When ownership is concentrated, it seems plausible that major shareholders use their controlling rights in order to gain self-interest and exploit minor shareholders. Based on this reasoning, Darmady (2016) found that in companies with concentrated ownership structure, agency problems often occur between major and minor shareholders, because in these companies, major shareholders seek their self-benefit at the expense of minor shareholders. These issues lead to information asymmetry in the capital market. In such conditions, the demand for high-quality independent auditors as a monitoring tool is enhanced. Thus, regarding the above, the first hypothesis is presented as follows:

H_1: There is a significant positive relationship between ownership concentration and the choice of high-quality audit firms.

Family firms can be defined from various aspects. Presence of family members in the board of directors, the percentage of share ownership by family members, and control or considerable influence of family in the company are among the factors that are attributed to family firms (Namazi & Mohammadi, 2010). In family firms, family members are often not only the owners of the company, but also the managers. In such companies, because family members are both the shareholders and managers in the company, there will be an alignment of managers' and shareholders' interests which leads to a reduction in information asymmetry and interest conflicts between managers and owners, and thus, there will be less need for the use of high-quality audit firms (Darmady, 2016). Studies show that family ownership leads to an increase in the earnings quality, a reduction in abnormal accrual items and an increase in the firm's value (Ben Ali & Lesij, 2012). Similarly, Darmady (2016) offered some evidence of a negative relationship between family ownership and the choice of high-quality auditors. Therefore, based on the above reasoning, the second hypothesis is formulated as follows:

H_2: There is a significant negative relationship between family ownership and the choice of high-quality audit firms.