



# The Effect of Auditors Opinions on Shares Prices and Returns in Tehran Stock Exchange

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## Abstract

*The purpose of this study is investigate the effect of auditor's opinions on shares prices and returns in Tehran Stock Exchange. This study conducted about companies in Tehran Stock Exchange during the period 2002-2008. For to do the investigate opinion classified in two groups, and to be discussed two hypothesis. In this research two test named-Test and Man-Whiteny have been used. Present result of these research shows, in confidence interval 95% there is no significant relationship between auditor's opinion and share prices. Present result of these research shows, in confidence interval 95% there is no significant relationship between auditor's opinion and share returns. Generally the results of this study shows, the both of hypothesizes be rejected and there is no significant effect of the auditors opinion on share prices and returns in Tehran Stock Exchange. Originally, that is, no information content of the audit opinion in decision making.*

**Key word:** Tehran Stock Exchange, auditor's opinion, prices and returns.

## Introduction

These days there are many measurements in order to calculate the amount of development of countries. One of the development measurements among the developed and the developing countries is economic advancement. The economic advancement has different figures, one of these figures is the active manufacturing units and to create value added. One of the figures in economic advancement is the existence of active market of investment. Active stock and shares exchange, belonged to the market that the rate of shares deals of organizations accepted in which is high that is because of the positive attitude of people toward this market. The high amount of dealings in shares exchange is related to this that the organizations accepted in that to have a clear financial situation in past, present and also to have a good financial view for future<sup>1</sup>.

The main condition for calculating the financial situation of the organization is the financial statement of it. Additional to that the financial statement of the organization is criterions for measuring the usefulness and performance of the management. Actually the financial position of the organization in financial statement is better it shows that the management of the company has been efficient. So it can be concluded that financial statement are one of the main reasons in selecting a special organization for investment. But the important fact to pay attention to is that, based on the agency theory which points out the conflict of interest between managers and the shareholders so it makes the shareholders to have an ambiguity toward the numerals and data presented in financial statement. In order to eliminate this doubt or ambiguity and to make the financial

statement (both potential and actual) reliable must be certified by independent person or persons<sup>1</sup>.

In most of the countries the duty of statement and declaration about financial figures of organizations are on behalf of the independent auditor itself. Actually these declaration and calculation are independent that make the financial statement reliable for users. Declaration and calculation are issued based on the audit report this report contains a kind of declaration about the financial statement of the organization. In the profession of the audit there are four opinions unqualified, qualified, and adverse and disclaimer of opinion would opinion the four kinds of opinion after examining enough attention to the evidence of financials in the organization, based on the data obtained from that organization. Iran which is one of the developing countries, stock market has an important role in speeding this development and improvement. So the organizations attending Iran are not excluded from this rule. In Iran the responsibility of opinion and calculation is on the shoulders of the independent auditor and all of the organizations will need this certification in order to continue remaining in the market of investment.

So based on what mentioned before we would like to measure the amount of attention paid to this certification from the users and the active roles in the market of investment.

**Hypothesis:** Background investigation in an investigation Firth<sup>2</sup> discussed the information content and provided unqualified and qualified reports. The research performed under the topic of ("A note on the impact of audit qualifications on lending and credit decisions"). It was a research survey, in which the researcher used questionnaires to discover whether bank lending decisions

and credit analysts' reactions were affected by qualifications and the type of qualification. The questionnaires contained a set of financial statements from a hypothetical company which was accompanied by either a clean or one of different types of audit qualifications. The results indicate that certain types of qualifications, specifically the going concern and asset valuation qualification, affected bank lending and credit analysts' decisions. He also concluded that these results indicate that the audit report should contain more detail in respect of such qualifications in order to help readers of the report to assess the significance of the qualification for their decision making<sup>2</sup>.

Guilamon<sup>3</sup> made a research in the name of (The usefulness of the audit report in investment and financing decisions). Actually the researcher presented the investigation on the importance of the audit report in investment decisions made by dealers and brokering companies and lending decisions made by credit institutions. In other words the aim of the research was to investigate the influence of the auditor's opinion (clean, qualified, adverse and disclaimer) on investing and financing decisions. The researcher used the survey method, that is, the researcher used a questionnaire through which the respondents were asked about the source they consider relevant when making decisions. The findings of the study indicated that the auditor's opinion represents a useful source of information when making investment and financing decisions.

In a research in the name of (The effect of qualified auditors' opinions on share prices: in Jordan) Thuneibat, Khamis and Fayumi<sup>1</sup> discussed the effect of qualified opinion of the auditors on the stock price and return of the accepted organizations in Jordan's stock and shares exchange market. The results of this research show that there is not any significant relation between the auditor's opinion and the stock price and return<sup>1</sup>.

**Mohammad-Ali Khatami<sup>4</sup>**: he discussed the effect of independent auditors' which are presented as audit qualifications of annual financial statements of organizations on the stock price and also the way they occurred based on the analysis of data on behalf of the financial analysts or stock brokers in a research called (The effect of audit qualifications on share prices and analysis of annual financial statements audited by the stock exchange). The results of the research show that there is relation between the audit qualifications and stock price. Meanwhile the brokers do not influence these audit qualifications as their own analyses and in fact the effect of the audit qualifications on the stock price must have a relation with the behavior of large investors<sup>4</sup>.

In a research survey he Seyed-Shahab Mohammadi<sup>5</sup> discussed (The effect of auditors' opinions on stock returns in Tehran Stock Exchange) in 1995-1998. The results show that there is not any significant relationship between the stock return and kind of auditors' opinions<sup>5</sup>.

Behnam Shahhosseini did a research called (the effect of Auditor's report on the decisions of the creditors). The conclusion of this research showed that the creditors used the auditors' reports to give out credit and the experts have efficient

knowledge and they believe that the auditors' reports would decrease the risk of giving out credit<sup>6</sup>.

In a research they presented the discussion of YahyaHasan-Yeganeh and Mohsen Ghasemi information content fraction of reserves referred to in the auditors' report. In this research the experts based on the design and test four hypotheses, discussed the information content fraction of reserves referred to in auditors' report and the effect of its price disclosure on experts' and investors' decision making<sup>7</sup>.

The findings of this research show that the changes of the number of paragraph in auditors' report about the information content fraction of the organization do not have any significant effect on the stock price. But the changes of the fraction price of the reserves in the auditors' report have a significant effect on the stock price. Also, in the group of the experts and brokers in Tehran's stock and shares exchange market, a significant difference between the suggested average stock price by any kind of aware or unaware groups of the fraction price of reserve taxes mentioned in auditors' report was visible, but in investors side there was no significant difference between the average stock price suggested by any sort of aware or unaware groups was not seen.

**Research hypothesis:** Ha. The kind of auditors' opinions has a significant effect on share prices Ho. The kind of auditors' opinions has a significant effect on return stock.

**Statistical population:** The statistical population of research includes all organizations accepted in Tehran's discussion of stock and shares exchange. It is necessary to be mentioned that in order to choose a sample the following limits have brought into concern: i. Organizations giving out financial and credit services, ii. Organizations that their end of financial year was not 29<sup>th</sup> of Esfand, iii. Organizations that their symbols in stock market have been stopped after three months, iv. Organizations with investment increase during the test period.

All organizations mentioned have been deleted from the statistical population.

After occurrence the four restrictions mentioned before, the number of organizations under examination in several years is as follows: i. Year 2002: 71 organizations, ii. Year 2003: 70 organizations, iii. Year 2004: 71 organizations, iv. Year 2005: 71 organizations, v. Year 2006: 67 organizations, vi. Year 2007: 71 organizations, vii. Year 2008: 71 organizations.

It is important to mention that one the restrictions occurred in the research was deleting the organizations that had an increase in their investment these organizations have been deleted only in the year of investment increase, which is why the number of organizations in some years is lower.

**Territory of the research:** The research's place of territory includes the accepted organizations in Tehran's stock and shares exchange. The research's time of territory includes the period between the years 2002 to 2008.

## Research Methodology

**Statistical method:** In the descriptive statistics section average, minimum, maximum, change domain and the related standard deviation to the stock price before and after the general meeting, also the differences between the shares prices after the general meeting with the shares prices before it have been calculated and also the calculations mentioned in order to determine the shares return in short term periods and long term periods occurred before and after the general meeting. These periods include 100 days, 30 days and 15 days before the general meeting and also 7days, 15days and 30 days after the general meeting. In the inferential statistics section also to examine the existence of normal or abnormal data based on KoloGrvf Smirnov has been used and after recognition of being normal or abnormal data in order to examine the research theories T-student's test and if abnormal the Mantinea's test have been used<sup>8-10</sup>.

**Research variables: Share price differences:** In order to find the differences in shares prices this kind of action has occurred that the last price of the final weekday before the general meeting which is actually the day of stopping the symbol of organization in stock market presented as the price before the general meeting and the first price after the opening of the symbol of organization on the first weekday after the general meeting counted as the price after the general meeting. This information has been derived from the information banks and after that the difference between the prices before and after the general meeting are calculated with the following formula. Of course it should be mentioned that in order to delete the effect of cash dividend mentioned in the general meeting, the amount of cash dividend was added to the shares prices after the general meeting:  $\{(share\ price\ after\ the\ general\ meeting + cash\ dividend) - share\ price\ before\ the\ general\ meeting\} / share\ price\ before\ the\ general\ meeting) \times 100$

It is necessary to explain that because of lack of price domain on the first day of opening of symbol just after the general meeting also because of not having limitations, the shares in different volumes with different prices would be traded. Regarding that it is not possible to examine all the prices and the volumes of the dealerships in a specified price as the price after the general meeting, in this research the final price of the first day of opening the symbol was counted exactly after the public general meeting.

**Return of the shares:** The return of shares in a period of time includes all the benefits that belong to the owner of that share. These benefits include the changes of price, cash dividend, and other benefits such as increase in investment and stock dividends. Of course in this research by share return, it meant the price return which is calculated from the following formula:

## Results and Discussion

**For periods before the general meeting:**  $\{(price\ of\ the\ day\ (n)\ before\ the\ general\ meeting - the\ final\ price\ before\ the\ general\ meeting) / price\ of\ the\ day\ (n)\ before\ the\ general\ meeting\} \times 100$

**For the periods after the general meeting:**  $\{(The\ price\ of\ the\ day\ after\ the\ general\ meeting - price\ of\ the\ day\ (n)\ after\ the\ general\ meeting) / the\ first\ price\ of\ the\ day\ after\ the\ general\ meeting\} \times 100$

As explained before the periods before and after the general meeting have been divided into short term and long term periods. In periods before the general meeting a period of 30, 100 and 15 days was noticed that in order to calculate the return in the mentioned periods the price of shares in that day was calculated with the final price of shares before the general meeting and was put in the formula and measured.

In the periods after the general meeting also periods of 15, 30 and 7 days were noticed and in order to calculate the return in these periods the price of the shares in the same day was calculated with the first price of the shares after the general meeting and was put in the formula to be measured.

The purpose of doing calculations in short term and term periods before and after the general meeting is to increase attention is the examination of the effect of the auditors' opinions which means that if it shows the affection of the kind of opinions on the stock price and return in each of these periods make it possible to show this affection. It is quite necessary to mention that after calculating the return in the periods in order to examine the effect of opinions the difference of return in these periods has been into concern. These differences in 9 different types are being mentioned as it follows: i. The return 7 days after the general meeting and 100 days before that, ii. The return 7 days after the general meeting and 30 days before that, iii. The return 7 days after the general meeting and 15 days before that, iv. The return 15 days after the general meeting and 100 days before that, v. The return 15 days after the general meeting and 30 days before that, vi. The return 15 days after the general meeting and 15 days before that, vii. The return 30 days after the general meeting and 100 days before that, viii. The return 30 days after the general meeting and 30 days before that, xi. The return 30 days after the general meeting and 15 days before that

**Auditors' opinions:** The auditors' opinions (unqualified, qualified, adverse and disclaimer of opinion) has been derived as one the research variables of the auditors' opinions which is an attachment to the organizations' financial statements. After clarifying the kind of auditors' opinions about generations', based on the kind of that it is divided into two different groups of unqualified and unacceptable opinions. Actually the organizations having one of these opinions of unqualified, qualified, adverse and disclaimer of opinion were classified in one group. Also in order to ease the calculations these two group were being coded and code numbers 1 and 2 were used that code 1 was for unqualified and code 2 for unacceptable.

**The result of the examination of hypothesizes: First hypothesis:** The first hypothesis suggests that the opinion of the auditor has effects on shares prices. The results show that the average of differences in the shares prices in total years in

unqualified opinion 256.52 and in unacceptable opinion is 240.82 and the level of significance of (t) test equals 0.239. Meaning that the average difference of shares prices in total years of unqualified and unacceptable opinions do not have a significant difference. The results show that the users of financial statements and information do not pay enough attention to the auditors' opinions in relation to the organizations under examination in this research.

**Second hypothesis:** The second hypothesis suggests that the auditors' opinions on shares return are effective. As mentioned in the sections of research variables the second hypothesis in nine different types has been examined which is why the results of that will be presented in nine parts:

**First part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 247.89 and in unacceptable opinion are 245.71 and the level of significance of 0.870. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Second part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 246.90 and in unacceptable opinion are 246.27 and the level of significance of 0.962. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Third part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 37.08 and in unacceptable opinion are 35.41 and the level of significance of 0.745. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Fourth part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 243.53 and in unacceptable opinion are 248.75 and the level of significance of 0.641. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Fifth part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 241.20 and in unacceptable opinion are 249.50 and the level of significance of 0.534. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Sixth part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 237.78 and in unacceptable opinion are 251.45 and the level of significance of 0.305. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Seventh part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 239.88 and in unacceptable opinion are 250.25 and the level of significance of 0.437. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Eighth part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 238.50 and in unacceptable opinion are 251.04 and the level of significance of 0.347. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

**Ninth part:** The results show that the average of return difference in the total years in this part in unqualified opinion is 239.82 and in unacceptable opinion are 250.29 and the level of significance of 0.432. Showing that the average shares return difference of total years in this part in both groups of unqualified opinion and unacceptable one does not have a significant difference.

It shows that as the first hypothesis the users and also activists in stock and shares exchange market do not pay much attention to the kind of auditors' opinions in relation with the financial statement of the examined organizations. The total results of 9 different types have been gathered in table-1.

## Conclusion

This research was done with the purpose of showing the effect of auditors' opinions on shares and stock prices. That is why the opinion presented by the auditor is divided into two groups the unqualified opinion and the unacceptable opinion s and also based on the researched theories in the group of differences in prices and returns of examined shares to testify the effect of the kind of opinion on price and return differences. According to the research theories the results are as follows:

Based on the first hypothesis claim the auditors' opinions have effects on the shares prices. But the results of the research show the opposite of this hypothesis. The results show that the auditors' opinions do not have effects on the shares prices.

Based on the second theory's claim the auditors' opinions have effects on the shares return. But the results of the research show that the auditors' opinion does not have effects on the return differences in the several periods of before and after the general meeting.

According to what mentioned it could be concluded that the users of financial statements do not pay attention into the auditors' opinions and in fact the kind of auditors' opinions does not have an effect on the process of decision making for the users of financial statements.

**Suggestion for future researches:** i. It is being suggested to discuss the effect of audit qualifications opinion on the return and price of the shares in research, ii. It is being suggested to discuss the number and paragraph of units on qualifications in auditor on the price and return of shares, iii. It is being suggested to discuss the effect of the auditors' opinions on liquidity of shares and free shares in a research, iv. It is being suggested to discuss the auditors' opinions on the systematic and unsystematic risks in a research, v. It is being suggested to discuss the examination of Rial volume of items reported of auditors' opinions on the market variables.

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**Table-1**  
**The summary of second hypothesis (see below)**

Year	Opinion	Number rating	Average rating	Total rating	U Manwithney	Level of significance
First type	unqualified opinion	178	247.89	44125	27698	0.870
	Unacceptable opinion	314	245.71	77153		
Second type	unqualified opinion	178	246.90	43949	27874	0.962
	Unacceptable opinion	314	246.27	77329		
Third type	unqualified opinion	178	244.41	43505	27574	0.806
	Unacceptable opinion	314	247.68	77329		
Fourth type	unqualified opinion	178	242.53	43169	27238.50	0.641
	Unacceptable opinion	314	248.75	78108.50		
Fifth type	unqualified opinion	178	241.20	42934	27003	0.534
	Unacceptable opinion	314	249.50	78344		
Sixth type	unqualified opinion	178	237.78	42324	26393	0.305
	Unacceptable opinion	314	251.45	78954		
Seventh type	unqualified opinion	178	239.88	42699.50	26778.50	0.437
	Unacceptable opinion	314	250.25	78578.50		
Eighth type	unqualified opinion	178	238.50	42452.50	26521.50	0.347
	Unacceptable opinion	314	251.04	78825.50		
Ninth type	unqualified opinion	178	239.82	42678.50	26756.50	0.432
	Unacceptable opinion	314	250.29	78590.50		