



## Investigating the relationship between domestic debt management and the cost of auditing adopter companies in the Stock Exchange Tehran

Ali Kamarkhani \*, Rahmatollah Mohammadipour

Department of Accounting, Islamic Azad University, Ilam Branch, Ilam, Iran

### ARTICLE INFO

#### Article history:

Received 4 December 2015

Received in revised form

22 January 2016

Accepted 22 January 2016

#### Keywords:

Cost accounting

Internal debt

Equity

Cash receipts CEO

### ABSTRACT

The aim of this study is to determine the effectiveness of debt management by the company and its relationship with audit fees in listed companies in Tehran Stock Exchange is done. The population of this study includes the companies listed in Tehran Stock Exchange during a period of 5 years, 2009 - 2013 and sampling method of elimination (112 companies). Using Eviews7, test was done using the appropriate methods Lamer and research model of Housman. The results show that there is a significant relationship between the domestic debt assumptions to the CEO and audit costs. Also, there are significant relationships among the ratio of debt to equity CEO, managing director of debt to equity ratio of debt to cash received by the managing director and audit fees.

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### 1. Introduction

Undoubtedly, the audit process and reassurance about the reliability of financial statement information. There are conflicts of interest between shareholders and managers, in order to resolve this conflict is of great importance to the audit. Audit as an effective mechanism to ensure that managers in the management of the company's shareholders in line with the interests of shareholders have surgery or not? So the audit reassurance to shareholders and other interested parties that are under contract with the company. Company auditor fees of any company's essential costs i.e. Davidson, Wallace N, III; Jiraporn, Pornsit, DaDalt and Peter. One of the audit fees could affect the domestic debt management. Results of previous studies show that companies change their auditor for various reasons, among these reasons are as follows:

- access to auditor industry specialization,
- client financial difficulties,
- the reputation of auditors,
- the audited financial scandals,
- greater access to non-audit services and
- access to audit reports for client management (favorable opinion).

Several factors contribute to the increase in the cost of the audit, including:

The complexity of the audit of the company's operations more complex and requires more time,

more sophisticated use of force is that it is faced with an increase in audit fees.

Debt leverage, which indicates the company's ability to repay debt of company; generally, lenders and creditors prefer debt ratio is relatively low. Relatively high probability of bankruptcy increases. As a result, auditors are concerned about the issues of financial statements that may have lower than normal reliability and to perform further tests are audited.

Domestic debt management of company, including pensions and wages is Fang Sun, Feng Yun Wu and Sherry F. Li, size and so on. Pension and other arrears, the payments that were committed by company executives and most of these payments in the future will face bankruptcy or lack of liquidity in the company, it is more like debt.

The result should be to establish a debt management agency or compensation payment. Edmans and Liu (2010) argued that compensation would be based on debt that the solution to the cost of the debt. They argue that domestic debt management resources on their behavior are variable and indicate that domestic debt needs for this type of compensation.

Sundaram and Yermack (2007) showed that most executives' length of service, pension payments can be 60% of final average pay is received in addition to their reward. Managers are also more domestic debt to your company with a more conservative management. Gerakos (2007) showed that the average benefits and pensions executives in a sample of his research in 2004 to 3.3 million dollars and 4.3 million dollars in 2005 reach. 9-2007 More financial

\* Corresponding Author.

Email Address: [kamarkhani\\_ali@yahoo.com](mailto:kamarkhani_ali@yahoo.com) (A. Kamarkhani)

crisis caused a lot of IOU (domestic debt, according to Jensen and Maclin, 1976), respectively.

In this study, a review of existing literature on this issue and the role of debt in the company and the economic aspects and the role of the audit fees paid on domestic debt management.

Previous research indicates that domestic debt management leads to conflicts of interest of directors and shareholders and debtors, and the demand for more conservative accounting (Jensen and Maclin, 1976; Edmans and Liu, 2010). It is also well known that conservative important regulatory mechanism to limit opportunistic behavior of managers of financial reporting. For example, Watts (2003) concluded that conservative management ability and incentives to reduce fraud. Chen et al. (2007) confirmed this view and suggest that the conservative bias of opportunism and managers reduces.

In all the above arguments have shown that when companies are more conservative, less managers engage in opportunistic behavior, which in turn try and further tests are created for auditors. If so, we expect the cost of auditing in companies that have a higher level of domestic debt, higher.

The purpose of this study was to determine the relationship between domestic debt management and relationship to the stock management and cost accounting is total equity.

## **2. Research purposes**

### **2.1. Main purposes**

Identify the relationship between the CEO and the company's internal debt audit fees in exchange companies in Iran

### **2.2. Secondary purposes**

1. Identify the relationship between the ratio of debt to stock VOX Company's managing director and audit fees.

2. Identify the relationship between the ratio of debt to equity and the cost of audit firms CEO of VOX.

3. Identify the relationship between the ratio of debt to cash received by the managing director and audit fees in exchange Iranian companies.

## **3. Research background and theoretical bases**

Sajadi and EbrahimMand (2007) to review the external auditor's independence have causes. The overall results show that non-audit services fees of pending audit client acceptance of gifts, long-term continuation of the auditor selection and reducing the impact of economic dependence on auditor independence and auditor to the client.

Bozorg Asl and Shayestehmand (2007) examined the relationship between auditor tenure and management for the benefit of Allameh Tabatabai University in Tehran. Overall, the findings suggest is

that by increasing the term of office of the auditor, the risk of earnings management, in order to reduce what in order to increase profits, gain more control and direction depending on the specific motivations of management.

Sajadi and EbrahimiMand (2007) the effect of non-audit services to the client and the auditor's economic dependence on auditor independence martyr Chamran University paid. In this study, the effect of non-audit services to the client and the auditor's economic dependence on the independence of auditors, auditors from the perspective of a member of the Official Auditors of Iran was investigated. The results show that the auditors for non-audit services and auditor independence are reducing economic dependence of the auditor to the client.

According to the law to supervision and regulation of audit firms responsible for handling public company, was founded. The law in 2002 in response to financial scandals such as Enron in the United States, and later adopted a similar law in Japan, Germany, France, etc., was approved. Sarbanes Oxley law includes 11 chapters and some of the responsibilities of the Board of Directors (5) and Section 404 standards published by the mentioned law relating to the assessment of internal controls is one of the most controversial parts of the law because its implementation is necessary to bear heavy costs for companies. According to research by US companies listed on the stock an average of about two per cent of their income in accordance with this Article and establish internal controls have costs. In 2007, these costs amounted to 3 billion dollars. The research results suggest that the benefits of compliance costs have increased.

Sundaram and Yermack (2007) showed that most executives' length of service, pension payments can be 60% of final average pay is received in addition to their reward.

Gerakos (2007) show that the average benefits and pensions data executives in a sample of his research in 2004 to 3.3 million dollars and 3.4 million dollars in 2005 alone. 9-2007 More financial crisis caused a lot of IOU (domestic debt, according to Jensen and Maclin, 1976), respectively.

Sundaram and Yermack (2007) were the first to examine the implications of their domestic debt management. Their findings suggest that more domestic debt to their managers who are more conservative may act to reduce the debt. This result is consistent with the theory of Jensen and Maclin (1976) in connection with the conflict of interest between the management of domestic debt by more debt. This conflict of interest as stated in Sundaram and Yermack (2007) confirmed that the document confirming the positive reaction to the disclosure of bond prices is considerable domestic debt management of company regarding compensation. If auditors to reduce the likelihood of default as a factor that reduces audit risk is acceptable and therefore less need to audit efforts, we may have a negative relationship between the cost of domestic

debt management audit and achieve the means Audit lower cost for our customers to better manage internal bad management by the company.

Dogan et al. (2007), the timeliness of financial reporting, in the case of international companies were listed. The results showed that the timeliness of financial reporting, affect the company's profitability. The results also showed that the size of the company, financial risk, the policy and the timing of the reporting during the past few years, the company timely financial reporting were effective. More than seventy factors affecting the quality of the documents reviewed by the audit states that the internal audit on the count back several factors affect the quality of the documents prepared by the client.

For example, Schultz (2008) reported that the debt figure is much higher among large companies, 8.11 billion in the now Goldman Sachs Group, 8.5 billion dollars in the company JP Morgan Chase and Co and 12-10 billion dollars at Morgan Stanley. Evidence shows that pensions and other arrears is very important (Schultz and McGinty, 2009).

In general studies and recent reports indicate that domestic debt recovery companies are widely adopted in the General Assembly. And the huge level of debt likes to have attracted the attention of researchers and academics. To the extent that companies are required to disclose detailed compensation details are debt managers.

Huang et al. (2009) conducted a study about factors affecting improve the quality of internal audit. They identified seven factors affecting efficiency of the internal audit findings, including the revision of the audit, improved audit procedures, increasing the accuracy of the audit program, the use of computers in the process of auditing the use of the offers, in coordination with independent auditors, and compliance with legal requirements respectively.

Wang et al. (2010) examined the relationship between domestic debt and conservatism has been audited. Their findings showed that the company increased its domestic debt less conservative publishing the reports. This is good because it is an important regulatory mechanism for management accounting conservatism is opportunistic in financial reporting (Watts, 2003).

Edmans and Liu (2010) argued that compensation would be based on debt that the solution to the cost of the debt. They argue that domestic debt management resources on their behavior are variable and indicate that domestic debt needs for this type of compensation.

Although the basic theory research is empirical research in this area is rare. Existing literature is mainly based on stock-based compensation in limited stock, equity, while the literature has provided a lot of evidence suggests that excessive losses for equity and less on domestic debt Management is considering.

Conservatism in accounting includes stricter standards for the recognition and predictive diagnosis as profits or losses. Lack of control of the

Conservative Gray reports more potential exposure to accounting errors and irregularities will occur. As a result, auditors to conduct more tests essential to achieve the same level of audit risk is acceptable, need. Preference for conservative accounting auditors in detecting asymmetric shape are as well as profit losses due to concerns over exposure to more litigation over the users of financial statements to understand; because the auditors are more likely to be the case for truth. The relationship between accounting conservatism and the exposure to litigation auditors was found by Basu (1997). He concluded that the exposure to litigation to be reports that auditors are conservative. With regard to the pricing audits and litigation efforts include both performance audit risk, the higher costs may also give internal auditors of the company. He evaluated the effect of long auditor tenure on their independence. Their findings show that self-interest threats, an intimidation long period auditor tenure is effective advocacy threats intimate relations during a long tenure on auditor independence is not effective. Also, showed that factors timely audits of the companies listed in Tehran Stock Exchange are: audit fees, the audit, the auditing firm, the auditor's opinion and the loosing of the company.

#### **4. Research hypotheses**

##### **4.1. Main hypotheses**

The domestic debt audit costs related to the CEO and there.

##### **4.2. Sub-hypothesis**

1. The debt-to-equity ratio CEO and audit costs related there.
2. Managing the ratio of debt to equity and cost accounting there is a significant relationship.
3. The ratio of debt to cash received by the Managing Director and audit fees there is a significant relationship.

#### **5. Methodology**

In this study, the model was used to estimate using panel data. Also in this study, both descriptive and inferential methods to analyze the data will be discussed. On the surface, using statistical characteristics such as frequency, mean, standard deviation describes the public properties and inferential statistics to respond to hypotheses and to find specific relationships between variables tests, regression analysis, significant test T and F tests will be significant. In this study for testing of software Eviews statistical software is used.

#### **6. Statistical population**

The population of this study includes the companies listed in Tehran Stock Exchange and

sampling, methods of elimination. This means that models to estimate the survey, the companies with the following conditions, and the sample is in these circumstances and that those who do not have the sample, are eliminated. These conditions are as follows:

- Between 2009 and 2013 period is 5 years.
- In order to improve comparability, leading to the end of their fiscal year is March.

- Tehran Stock Exchange listed companies in all phases of the research will be.
- Member companies, financial intermediaries, holding on (holding companies) and banks are not.
- Companies are not losing.
- Do not interrupt quarter.

The following table summarizes the sampling survey shows (Table 1):

**Table 1:** The sampling survey

Description	Count	
Members of the population at the end of 2012	551	Total
Companies that ended their fiscal year are 12.29.	209	Filter
Companies that invest in the industry, banks and financial intermediaries are classified node are.	11	Filter
Companies that are part of the losing companies.	55	Filter
Companies listed on the Stock Exchange after 03/20/2008, or before 19.03.2013 is out of stock or into their information were not available.	164	Filter
Total companies removed from the population	439	All filters
Collect statistical sample of companies	112	Remaining

**7. Research variables and how to measure them**

The variables used to measure domestic debt resources manager include:

- Leverage CEO (CEOLev), debt to equity ratio. In other words, the purpose of the stock, the Board of Managing Director and to the debt, the sum of the present value of pension benefits and other deferred by the managing director.
- Leverage ratio of CEO (CEOFirmLev), including ratio of debt to equity
- The ratio of debt to cash (CEODEbtCash), including the company's debt divided by cash received CEO (salary and bonuses, etc.)

**8. Results from model estimation**

This section examines the relationship between domestic debt management and auditing costs listed companies on the Stock Exchange in Tehran. For this purpose, according to the characteristics of the studied statistical data, panel data models used. The estimated coefficients on panel data models, such as time-series models using ordinary least squares method is used. Therefore, in order to efficiently estimate the coefficients of the variables, assumptions must be associated with this estimate, will be met. In the assumptions reviewed and tested.

**9. Results from variables estimation**

**9.1. Unit root test for reliability**

The econometric methods provided any estimate is to ensure the reliability of variables. For panel data models, the problem of spurious regression models for time series as well as true. The unit root test applications in hybrid models are essential. It is necessary for every single unit root test variables are taken to ensure convergence. When using panel data variables can be used to evaluate the reliability of the tests (Levin, Lin and Chu, Breitung, Im, Pesaran and

Shin, Fisher by Fisher-type tests using ADF and PP tests and Hadri can be used. In this study, the test Levin, Lin Vchav (LLC) is used (Table 2).

**Table 2:** Results unit root test Levin, Lin Vchav

Testing LLC (unit root test Levin, Lin Vchav)		
Variable	Statistics	Prob.
X <sub>1</sub>	-2.724	0.0075
X <sub>2</sub>	-3.782	0.0007
X <sub>3</sub>	-2.708	0.0001
Y	-5.375	0.000

Durability test results indicate that the variables according to the test and make sure each (Prob) of variables is less than 0.05, all variables are significant in the present study.

In addition – durability test dummy variables, since the probability of regression there. To avoid spurious regression situations, Co-integration test to be used as a pre-test. In this way, only in terms of the number of variables can trust the results and there is a group of tests to determine the variables Johansen Fisher used (Table 3).

**Table 3:** Test Johnson Fisher

Johnson Fisher test		
Hypothesis testing	Statistics	Prob.
H0: no co-integration	4.4567	0.000

As Table 3 shows, the model variables are assessed collectively (co-integration) and therefore the estimated regression, regression coefficients estimated reliance cannot be false.

**9.2. Normality test of error terms**

One of the assumptions discussed in the regression estimate by OLS, normal amounts of residues from the estimated distribution model. The non-normality of the distribution of residual values, estimated coefficients does not affect the performance and reliability of the model simply is not related to and impact assessment. In order to

test the normality of error terms *Jarque-Bera* statistic used to test the following hypothesis (Fig. 1):

$H_0$ =normal  
 $H_1$ =abnormalities

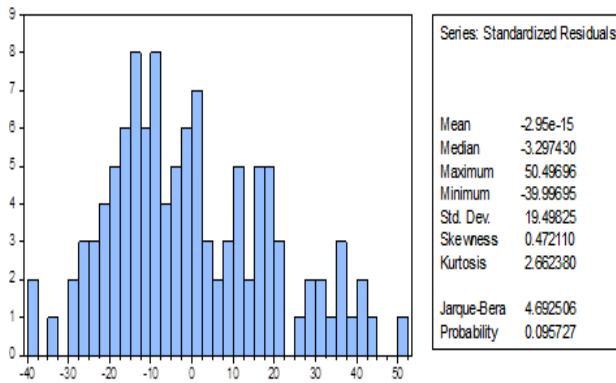


Fig. 1: Test results JB

Table 4: Results of correlation

Y	X <sub>3</sub>	X <sub>2</sub>	X <sub>1</sub>	Variable
0.0482	0.0105	0.0875	-	X <sub>1</sub>
0.081	0.1085	-	0.0875	X <sub>2</sub>
-0.807	-	0.1085	0.0105	X <sub>3</sub>
-	-0.807	0.081	0.0482	Y

According to the results presented in the table above, the correlation between the independent variables to the extent that it can be seen as a high correlation. So, it can be overlooked.

9.4. Anisotropy analysis of variance

In order to test the likelihood ratio test was used variance difference. The results of this test in the Table 5 are shown.

Table 5: Results of the analysis of variance difference

Statistics	Base	Significant level
Field of view	6.7863	0.17205

$H_0$  hypothesis is that there is no difference variance. Due to the significant (prob> 0.05) hypothesis  $H_0$ ,  $H_1$  hypothesis is accepted and rejected, resulting in a significant regression in the level of 5% variance is no difference.

9.5. Model estimation by panel data model and hypotheses test

In combination with the data in terms of the heterogeneity in grades, estimation bias and multicollinearity is reduced and efficiency increased degree of freedom and variability. The more complex models can be studied in a combined data and better effects can be detected and measured. To assess the heterogeneity of units or F Limar Chow test can help. If approved by the heterogeneity of the units, the model is estimated using panel data and otherwise normal or Pooling Data is estimated by OLS, but the process used to identify patterns in this research and the testing of hypotheses Research will be accepted.

Normal test results suggest that the hypothesis  $H_0$  approved sentences waste and residues modeled estimate is normally distributed (p-value> 0.05).

9.3. Correlation (Pearson) coefficient among independent variables

OLS to estimate the parameters using the implicit assumption is that the explanatory variables are not linear correlation. Linear correlation between variables is called linear time. Linear problem arises when that line is extreme (near to number one), which in this case cannot be estimated coefficients of the regression equation. Pearson correlation coefficient was used to examine the relationship between variables and the results are presented in Table 4 has been proposed.

10. Examined model in this study

To investigate the effect of variables domestic debt management and auditing costs listed companies in Tehran Stock Exchange under the use of a linear relationship.

Chow test to determine the use of fixed effect model is the integration of data.

$H_0$ : Integrated data model

$H_1$ : Fixed effects model

Null hypotheses based on bound rates and its opposite hypothesis is based on the value. Chow test statistic is based on the sum of squared errors and bound model is as follows (Eq. 1):

$$Chow = \frac{(RRSS - URSS)/(N-1)}{(URSS)/(NT - N - NK)} \tag{1}$$

This statistic has an F distribution with N-1 and NT-N-NK degrees of freedom. If the value of F bound by the calculated value of F statistics table is less significant at the level specified hypothesis  $H_0$  Rejected and there will be no significant effect for sections and Fixed Model will be selected. Otherwise the data model used Pooled Model. Chow test results in Table 6 are shown. The results for the model presented in this study indicate that both F and chi-square statistic is significant at the 05% significance level. The null hypothesis that the use of combined model will not be accepted and must be based on panel data models is estimated.

After the appropriate model to estimate the panel was a diagnosed, fixed effects and random-effects method necessary to the proper method to test hypotheses to be determined. Hausman test is used

to determine the results of the research model as Tables 7 is.

**Table 6:** Chow test results (test F Bound) for the research model

Statistics	Base	Prob.
F bound	4.3562	0.000
Chi	11.5327	0.000

Hausman test results in Table 7 are shown. These results indicate that the chi-square statistic is significant at the 5% significance level. The null hypothesis that the importance of using random effects models will not be accepted and must be based on fixed effects estimates.

**Table 7:** Results of Hausman test model

Statistics	Base	Prob.
Hausman	7.457	0.000

**11. Final model estimation and hypotheses test**

Various tests were carried out according to the pre-end models to assess the impact

**Table 8:** Results of the regression analysis using fixed effects model 1

Variable	The coefficient of determination	Standard deviation	T calculated	Confidence level.
Debt to equity ratio of CEO	3.3256	.5426	2.5326	0.000
C	-3.4375	-4.0758	1.5749	.4265
Factor R	0.294	Level of significance (F-statistic)		0.000
Square root R	0.542	Watson camera test		2.235
F statistics	2.0214			

According to the results presented in Table 8 can be stated that the estimated coefficient for this variable is based on the ratio of debt to equity 3.32 positive relationship between the CEO and audit costs there and also the variable accuracy of the significant level See Probability calculated as equal to 0.000, which is so significant relationship was observed between these two variables. The first hypothesis of this study is that a significant correlation between the ratios of debt to stock the CEO and the cost of the verification audit.

**Table 9:** The results of the regression analysis using fixed effects model 2

Variable	The coefficient of determination	Standard deviation	T calculated	Confidence level.
Debt to equity ratio CEO	2.467	2.6434	1.4575	0.000
C	7.6871	0.7086	3.8711	0.781
Factor R	0.856	Level of significance (F-statistic)		0.000
Square root R	0.925	Watson camera test		1.9654
F statistics	1.967			

Suggests that since Probability calculated for varying the ratio of debt-to-equity CEO is equal to 0.000, so at 95 percent is a significant relationship between these two variables and also the accuracy of the estimated coefficient for which is equal to 2.46, indicating a positive relationship between these variables. The results of the study hypothesis of a significant correlation between the ratio of debt to equity and cost audit manager confirmed.

1. Debt to equity ratio CEO and audit costs related durability there.
2. Debt to equity ratio CEO and audit costs, there is a significant relationship.
3. The ratio of debt to cash received by the managing director and audit fees there is a significant relationship.

It is estimated. Results of regression testing are based on the fixed effects in Tables 8, 9 and 10 are summarized.

**12. Hypotheses test**

**12.1. The first hypothesis is that the debt-to-equity ratio there is Managing Director and audit fees**

H<sub>0</sub>= between debt to equity ratio of CEO and audit costs there was a significant relationship.

H<sub>1</sub>= between Debt to equity ratio of CEO and audit costs there is significant relationship.

**12.2. The second hypothesis is that those between the ratio of debt to equity and cost audit manager**

H<sub>0</sub>= between debt to equity ratio CEO and audit costs there was a significant relationship.

H<sub>1</sub>= between debt to equity ratio CEO and audit costs there is significant relationship.

Table 9 shows the results of test of the second hypothesis, which states that the ratio of debt to equity and cost audit manager.

**12.3. The third hypothesis is based on the ratio of debt to cash received by the CEO and there is the cost of the audit**

H<sub>0</sub>= the ratio of debt to cash received; there is no significant relationship between the CEO and audit costs.

H<sub>1</sub>= the ratio of debt to cash received by the Managing Director and audit fees there is.

**Table 10:** Results of the regression analysis using fixed effects model 3

Variable	The coefficient of determination	Standard deviation	T calculated	Confidence level.
The ratio of debt to cash incoming CEO	3.754	1.0732	2.7452	0.0001
C	-3.07888	0.453	1.4528	0.247
Factor R	0.735	Level of significance (F-statistic)		0.000
Square root R	0.857	Watson camera test		2.325
F statistics	2.325			

The results (Table 10) test the third hypothesis, which states that the ratio of debt to cash received by the Managing Director and audit fees there was a significant relationship.

Suggests that since Prob calculated for changing ratio of debt to cash incoming CEO, is equal to 0.0001 so 95 percent is a significant relationship between these two variables and also the accuracy of the estimated coefficient for which is equal to 3.75, indicating a positive relationship between these variables. The results of the third hypothesis of a significant correlation between the ratio of debt to cash received for the CEO and the audit fee is approved.

#### 12.4. The main assumption of the debt of the company's internal audit costs related to the CEO and durability

$H_0$ = between domestic debt to the CEO and audit costs there was a significant relationship.

$H_1$ = between domestic debt to the CEO and audit costs there is.

The main research hypothesis can be stated that according to the three hypotheses were confirmed and the ratio of debt to equity research subsidiary CEO, managing Director of the ratio of debt to equity and debt-to-cash accounting charges related to the incoming CEO There is a significant, so the research hypothesis was confirmed by the company's internal debt audit costs related to the CEO and durability.

#### 13. Conclusion

As was observed in this study to describe the company data exchange and analysis of this study was the estimation models. After describing the data to test data for the start of the test panel was Limr test results indicate that the panel of data from the selection method used to estimate models of the Hausman test and the results of the test methods the best way to estimate the constant research models introduced. The classic tests durability (reliability) data and analysis of variance difference was the lack of variance difference was that the results of the durable. After these tests was to test the hypothesis that all assumptions based on the results of the research output of software other than the first hypothesis, verified and found a significant relationship.

#### 14. Suggestions

##### 14.1. Suggestions based on research findings

The first hypothesis is based on the ratio of debt to equity CEO and audit costs There is a significant relationship, it is suggested at the time of the issuance of shares in listed companies in Tehran Stock Exchange refused to give shares to managers, because according to a first hypothesis of this study will be part of the increased cost of the audit.

According to the second theory, which states that the ratio of debt to equity and the cost of the audit CEO significant relationship exists, it is suggested in the payment of debt management companies and owners act more and more accurate cost audit not increase.

According to the third research hypothesis which states that the ratio of debt to cash received by the CEO and audit costs, there is a significant association, owners of companies to manage cash payment instead of paying stock exchange with a bonus of increased audit costs prevent to act.

Finally, it is recommended to reduce the cost of audit firms as its ability to reduce their bad.

##### 14.2. Suggestions for future researches

Check domestic debt management and prediction error earnings per share and the company's growth using quarterly data. Suggestions hypotheses:

The ratio of debt-to-cash income received by the CEO and the prediction error is a significant relationship.

Debt to equity ratio CEO and profit forecast error is a significant relationship:

- The relationship between the management and the company's profitability in the stock.
- The relationship between the percentage of ownership in the company's management and audit costs.
- The relationship between the percentage of ownership in the management company and the auditor's reliance on the report.

The ratio of debt to cash received by the CEO and the company's growth has a significant relationship.

The ratio of debt to equity is a significant relationship between the CEO and the company's growth.

The researchers suggest that the extreme volatility of financial and non-financial performance metrics stock index to get explored.

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