

Switching to Semi-annual Financial Statement Reports - Market Reaction, Audit Fee and Corporate Governance Quality

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Abstract: The aim of the research is to examine the reaction of market participants (investors and firms) to a regulatory exogenous shock of easing financial reporting statement regulations. Since 2017, small cap firms, publicly traded on Tel-Aviv stock exchange, are required to publish only Semi-annual reports hence any firm may opt to switch from formerly mandatory quarterly reporting to the currently required semi-annual financial reporting statement. We show that 2/3 of the firms chose to adopt the relief in regulation. In the group of firms that chose to apply the regulation relief, we find a significant negative abnormal market reaction of -2% to the announcement of adopting the relief. In the group of firms that waive the regulation relief and chose to stay on quarterly reporting, we observe a significant positive abnormal market reaction of +2.5% to the announcement of voluntarily continuing with the quarterly financial reports. Moreover, for the firms that switch to semi-annual reports, we show a significant decrease of 19.8% in the number of external auditing hours and a significant decrease of 16% in the annual external total audit fee in 2017 as compared to 2016. No significant change in the annual external total audit fee has been observed for the firms that opted not to adopt the abovementioned regulation. We also collect additional information about institutional investor holdings and outside directors which serves on these boards (financial expertise, gender and "busyness") as signals to corporate governance quality. We find positive and significant associations between the voluntarily continue the quarterly financial reporting and high quality corporate governance. The findings of the event study provide a valuable contribution to the ongoing debate on the relevance of the quarterly financial reports to investors. The additional finding of lower corporate governance quality and decreased external audit effort which characterized the firms that adopt the relief represent an increased risk for information asymmetry for investors in such firms thus further reinforces the importance of frequent financial reporting.

Keywords: Financial Reports, Relevance, Market Reaction, Corporate Governance, Audit Fee, Semi-annual, Quarterly

1. Introduction

The requirements of disclosing information of firms to investors are essential to reduce asymmetric information and issue of moral hazards. This paper focuses on the relevance and the observed costs (total audit fees) of quarterly financial reports of publicly traded firms on the Tel Aviv Stock Exchange (TASE).

The burden of regulation is costly to firms; we witness the costs of total audit fees and the time spent by management and boards for preparing the information to investors at high frequency, while instead they could utilize those resources to

focus on the management of the firm's operations. The costs of producing quarterly financial reports demotivate firms from listing their shares (by delisting and decrease in IPOs).

On the other hand, the high tendency of reporting financial information allows investors to make better investment decision and therefore attract more investors overall.

Globally, security authorities monitoring stock markets realize the burden of increased regulation on listed firms. Thus, they try to find the optimal balance between regulations imposed on firms and the transparency of financial information available to investors.

In the last decade, there is a significant decrease in the

number of listed firms on TASE. Several actions taken by the ISA to simplify reporting requirements did not yield the desired outcome and did not reverse the trend of delisting. Consequently, in the beginning of 2017 the ISA canceled the mandatory requirement of small firms to publish quarterly financial reporting. Rather those firms' needs to provide semi-annual financial reporting to the investors. Alternatively, they can provide voluntary quarterly financial reporting if they prefer to.

The decision of the IAS creates a new threshold that defines which firms are considered small publicly traded firms in Israel¹. The IAS definition of Small Reporting Entity (SRE) is firms that the market value of their shares is less than 300 million shekels and/or firms with a balance of traded bonds that is less than 200 million shekels. The definition of SRE does not include firms that are included in certain indexes traded in TASE or are dual listed companies. No change in reporting requirements was implemented for large firms that continue to report the financial information quarterly.

The IAS asked the SREs to inform by May 31st 2017 whether they prefer to switch to semi-annual reporting or whether they will voluntarily continue with quarterly financial reporting. On May 9th 2017 the ISA reported that 73 out of 180 SREs have adopted the relief in reporting regulations.

This exceptional change in financial reporting frequency may eventually affect the market reaction. Additionally, the reduced reporting frequency may influence the total auditing fees and effort of external auditors for those firms.

Auditor Fee Disclosure Regulation

In 2006, the ISA initiated a mandatory disclosure of the external auditor total fees, depicted in the Management Discussion & Analysis (MD&A) – part of the financial annual report package of the publicly traded firms. While this regulation generates valuable information about auditor's fees and efforts, it is only partial—as it is a vague reflection of the auditor's efforts. Since 2008, the ISA also mandatory requires a detailed specification of the number of hours the external auditor works, a piece of data that is unique to Israel. As a result, we succeeded in calculating the external auditor's fee per hour, which shed more light on auditor's risk and efforts.

The goal of the research is to test the influence of the firm's decision on reduction of the financial reporting requirements on (i) investors' immediate market reaction (ii) on the external auditing fees as a part of the firms costs (due to the elimination of two quarterly statements). The research further tests correlation between the firm's decision on the quarterly reporting and the corporate governance quality.

Our research use a unique handily collected data and is innovative in three different aspects: first, we have a clean exogenous regulation shock that tests the importance of the quarterly financial reports to investors, using immediate excess market reaction on two different groups of firms –

those who apply the relief and the voluntarily continue publishing their financial reports quarterly. Second, we test the cost of regulation shock differences between the two groups of firms based on their disclosure frequency decision, using the yearly total audit fee change around the relief. In addition, the uniqueness of the ISA regulation concerning disclosing of the external audit hours (reported on the MD&A) allow us a rare glimpse to the pricing of audit service for small publicly traded firms as a function of effort change. Third, we shed a light on the correlation between voluntary disclosure and corporate governance quality of small publicly traded firms, using characteristic such as outside director financial expertise, gender and "busyness" (service on other boards) and the percentage of institutional investor holdings in those firms.

The rest of the paper proceeds as follows: in section II, we review relevant literature that focuses on audit fee. Section III describes the hypotheses and methodology; the empirical results are described in section IV; lastly, section V concludes our paper.

2. Literature Review

It is widely believed that the SREs have important contribution to the economy in general and stock markets in particular. As a result, investing in Small / Medium Entities (SME) had become increasingly attractive in recent years. As we describe below security authorities throughout the world are already aware of the high costs of the quarterly preparation of financial reports especially, for those SMEs.

In July 2015, IOSCO published a full report describing the work of "The Growth and Emerging Markets Committee of the International Organization of Securities Commissions". The finding of the committee from the survey indicated that authorities have had uneven success at helping SMEs to fully leverage capital markets. Successful measures that can be emulated include establishing separate equity and fixed income markets with regulatory requirements tailored to SMEs, establishing market advisory and market-making systems, as well as introducing alternative methods of financing such as private equity, venture capital and securitization.

2.1. The Usefulness of Financial Information Disclosure to Investors

The efficacy of financial information is of great importance to investors, researcher and standard setters, According to Lev [18], there is a widespread and growing dissatisfaction with the relevance and usefulness of financial report information, mainly among investors and corporate executives. The dissatisfaction is corroborated by extensive research, which consistently documents a growing gap between capital market indicators and financial information, more so for reported earnings. The reported earnings of most firms no longer reflect enterprise performance. Further to Lev [18], the tendency of financial reports is an issue with a great impact overall economy. For a sight, on August 17, 2018 President Donald

¹ The scale of reporting of companies don't change the trade on Tel Aviv stock exchange to avoid negative reputation to the SREs

Trump asked the SEC to study whether to stop requiring companies to report quarterly earnings.

2.2. The Effect of Reporting Frequency

In recent years, the debate on the importance of financial report and their frequency has intensified, Opponents of the quarterly reports believe that the financial information disclosure to investors is not useful for investors. Lev and Gu [17] in their book "The End of Accounting and the Path Forward for Investors and Managers" attempt to prove that "those voluminous and increasingly complex quarterly and annual reports... [have] lost most of [their] usefulness to investors...". In an earlier paper by Bhojraj and Libby [3], the researchers explain the shortsighted behavior of managers throughout a laboratory experiment. The results show that corporate managers behave shortsighted behavior of when faced with price pressure and high reporting frequency. These results were obtained in the absence of agency frictions and even when managers had the opportunity to make voluntary disclosures. Ernstberger et al. [10] empirically investigated the real effects of reporting frequency using the European Union data, in which less than half of the nations adopted mandatory quarterly reporting while others did not. The findings show that, in compare to semiannual reporters, quarterly reporters generally exhibit increased levels of "real activities management", in the form of myopic decisions that increase short-term cash flows at the expense of long-term value.

The opponents also discuss the high costs of the quarterly financial reports, Kajüter et al. [22], which exploit the effect of companies switching to mandatory quarterly financial reporting statement in Singapore. The research finds a 5 percent decrease in firm value consistent with the notion that mandatory quarterly reporting is perceived as a net burden for small firms. More importantly and contrary to popular opinion, they find no evidence of informational benefits or myopic investment for firms around the threshold. Additional support to reduce the frequency of financial reports and their high costs can be found in the UK; in 2007, publicly traded firms were forced to report the financial information quarterly rather than semiannually. Seven years later, in 2014 companies were allowed to stop quarterly reporting in favor of semiannual reporting. Gradually, most of the companies switched to semiannual reports.

The proponents show that current reporting requirements have been attributed to greater transparency of information (Beaver et al., [2]) and a lower cost of capital [12] for companies seeking to raise funds.

2.3. Voluntary Financial Information to Investors

Voluntary disclosure of the financial information published in the financial reports aims to provide investors with better information on their investments and thus, leads to improved capital allocation of stock markets.

The existing literature on voluntary disclosure describe several benefits that motivates firms to disclose additional

financial information to investors. Petersen and Plenbord [23] find that voluntary disclosure is negatively associated with information asymmetry. Healy and Palepu [14] also point out the important benefit of disclosing information to investors, explaining that a better capital allocation at national and international levels can be interpreted as a capital cost reduction. Botosan, [4] Botosan and Plumlee [5] find that voluntary information reduces the cost of equity capital and Sengupta [24] finds that a decrease in the cost of debt and Lundholm and Myers [20] show that voluntary information enables markets to incorporate more future earnings news into current stock returns.

However, despite the advantages described in the empirical voluntary disclosure literature, disclosing the information is costly to firms as described in the related theoretical models (Dye [8], Verrecchia [26] and Einhorn [9]).

Holland [15], examines the benefits versus costs of voluntary disclosure, explaining, "the management will publish until they will reach the point when they will observe that the capital agency costs reduction has equaled the increase of the information publication costs for the market and the other users".

Malone et al. [21] empirically examine the oil and gas industry. They point out that the firms, which are economically motivated to disclose more information, will do it only if the marginal cost will surpass the marginal profit of the additional disclosure.

It is complex to estimate the voluntary disclosure cost to the firms since some of them are indirect. The direct costs deals with collecting, processing, obtaining and auditing of data, while the indirect costs can be caused by the exposure of firms to actual or potential competitors. Singhvi and Desai [25] test the association between corporate size and disclosure. They show that the cost of the accumulation of certain information is bigger for the smaller companies than for the larger ones. This is especially true because the large firms dispose a more complex reporting system and a high level of earnings and the larger enterprises can more easily afford high advertising costs, which allows them to pick up the benefits of the easier shares' transaction and to obtain finance more easily. In additional, the small firms can risk their competitive situation due to disclosure of an excessive information.

Recently, research has highlighted the positive link between voluntary non-GAAP disclosure and the reduction of information asymmetries ([6]; [5]). According to audit analytics, research show that, the proportion of S&P 500 companies that reported non-GAAP metrics in 8-K or 10-K regulatory filings climbed from 59% in 1996, to 76% in 2006, to 96% in 2016. This research strengthen the perception of (2016) and show that the financial reports with the GAAP earnings information are less relevant and investors seek for more relevant information in the financial reports.

2.4. Voluntary Financial Information and Corporate Governance Quality

Voluntary disclosure models, as a component of signaling

theory, suggests that high quality firms motivate to disclose more information voluntarily than poor quality firms in order to signal to investors that they are high quality firms (Dye 1985; Verrecchia [25]).

Firms with high quality corporate governance have incentives to inform investors about this as a signal. In support of this theory, Lokman, Cotter and Mula [19] find empirical evidence that shows that high quality firms signal their corporate governance quality by voluntarily disclosing corporate governance information in annual reports. Disclosures of high corporate governance quality are difficult to replicate by poor quality companies. These disclosures will potentially increase firm value since knowledgeable investors will infer that firms with high corporate governance quality are less risky than firms with lower corporate governance quality. Agency theory can also explain why managers voluntarily disclose information. Agency conflicts that occur between managers and shareholders are due to the separation of ownership and control. Managers have incentives to adopt better governance mechanisms such as voluntarily disclosure practices to reduce agency conflicts and the possibility of bonding and monitoring activities imposed by shareholders to control their behavior. Dey's (2008) study provides evidence that supports the argument that the extent of corporate governance mechanisms in a firm is a function of the level of agency conflicts it has. This suggests that firms with high levels of agency conflicts are likely to adopt effective corporate governance mechanisms. Hence, in this case, a firm with high corporate governance quality is expected to increase voluntary disclosure in order to reduce agency conflicts.

2.5. The Determine of Total Audit Fee and Effort

It is relatively difficult to understand the influence of certain drivers related to the firm's characteristics, such as size, reporting complexity, business risks on the total audit fees. Moreover, the size of the auditing firm itself and the competitive landscape of auditing services in a specific country or industry, may also impact auditing fees level irrespectively to the audited firm.

Francis [11] finds that asset level is a good predictor of the logged audit fees in Australian companies audited by Big-Eight auditing firms, becoming the conventional standard in the accounting and auditing literature.

Castro et al. [6] analyze audit fees paid by firms listed on the Brazilian stock exchange BM&FBOVESPA for the year 2012. They find a positive relationship between the logged audit fees and firm's characteristics: size, firm complexity, and Big N auditors. Additionally, the findings show that firm's risk as perceived by the auditor affect the total auditing fees differently according to the Firm's size. In smaller firms with higher leverage and perceived risk, the auditor charges lower fees in opposite to the hypothesis that the auditor shall charge higher auditing fees to balance the perceived auditing risk. As for larger firms with increased liquidity and leverage risks or firms with stronger governance practices, it finds that total spending on auditing fees is higher.

Summarizing, there are few studies on the predictors of audit fees and it seems that auditing firms match their fees to the firm's size and ability to pay higher fees more than anything else does.

3. Data

We handily collected firms that defined as SRE traded at TASE on the years 2016- 2017. After we identified our initial data, we then used Maya site <https://maya.tase.co.il/> to find firms announcements dates and decision whether they switch to semiannual financial reports. We also collected relevant information from the financial reports and stock market prices and registered capital for trading in order to calculate the market values of the firms from TASE site. Throughout the study, we divided the SRE firms to two different groups according to their frequency of publishing the financial reports on 2017: there are two groups: those who mandatory adopted the relief and switch to the semiannual reports and those who voluntarily decided to continue publishing quarterly reports.

We add to our sample, relevant information from the annual financial reports concerning corporate governance data, including outside director's serving on the boards of these firms: financial expertise, gender and "busyness" (We define multiple-board directors as those who serve on the boards of two or more public firms, defined at Bar-Hava et al. [1]. We also collected the relevant institutional investor holdings investing of the SREs from TASE.

In the last part of the research, we focus on the costs and pricing function of the external auditor's fee relating to the annual financial reports. For the two groups of firms we handily collected from the MD&A, the information on total external audit fee, number of audit hours and the name of the audit firm (BIG4 or other), for the years 2016-2017, see Appendix 1.

4. Hypothesis Development

The research examines the exogenous shock of relief in regulation from three different angels: investors, corporate governance and total costs of audit fee. The hypotheses development are described respectively.

Voluntary Disclosure

According to the literature mentioned above, we believe that investors will react positively to those firms that announce their decision to voluntary publish quarterly financial reports despite the high costs of preparing and auditing the reports. Thus our first hypothesis will be,

Hypothesis 1: the excess stock market reaction will be positive to firms that decide not to switch to semiannual reports, i.e. continue to voluntary publish quarterly financial reports.

The methodology that we use for the first hypothesis and as a basic tool for the subsequent hypotheses is the market model. We examine abnormal returns (AR) in a window of 11 days (-5, +5) while the period of estimation is 200 days before the announcement. In this research, we choose the event window as 10 days around the announcement day due

to thin trading in some of the firms in our sample.

For calculating returns, we look at the daily closing prices of stocks. We use the Tel-Aviv 125 index (TA-125, the index of the largest stock companies traded on the TASE) as the stock market portfolio; we define R_m as the return on the TA-125 for calculating abnormal stock returns. We examine the statistical significance of our empirical findings by using a one-tailed t-test. Below is the equation we used to examine the excess return:

$$AR_{i,t} = R_{i,t} - (\alpha_i + \beta_i R_{m,t})$$

$AR_{i,t}$ = Abnormal return for firm i at time t

$R_{i,t}$ = Return for firm i at time t

Unlike the group of firms that decided to voluntarily, continue with the quarterly reports, the second group of firms announce switching to semiannual reports. Thus our second hypothesis will be,

Hypothesis 2: the excess stock market reaction will be negative to firms that decide to switch to semiannual reports.

Corporate Governance

According to prior research, corporate governance quality is positively correlated to voluntary disclosure. Hypothesis 3 a, b, c and d will test the difference in corporate governance quality using four complimentary measuring of corporate governance quality.

Hypothesis 3a: the group of firms that voluntarily continue with quarterly reports will have higher percentage of outside directors with financial expertise in comparison to the other group of firms.

The Israel Companies Law (the "Companies Law"), enacted in 1999, is applicable to public firms in Israel and states that if a board is composed of only one gender, any new non-executive director appointments must be of the other gender, thus requiring that boards of public companies include at least one woman.

Hypothesis 3b: the group of firms that voluntarily continue with quarterly reports will have higher gender diversification of outside directors in comparison to the other group of firms.

Hypothesis 3c: the group of firms voluntary continue with quarterly reports will have higher percentage of busyness of outside directors in comparison to the other group of firms.

Prior studies (Ajinkya et al. 2005; Boone and White 2015) find that the level of institutional ownership is positively associated with the likelihood and precision of voluntary forecasts and management disclosure.

We also test another complementary aspect of corporate governance quality using the difference of institutional investor holding between the two groups.

Hypothesis 3d: institutional investor holding are higher for firms that volunteer to continue with the quarterly financial reports compare to the other.

Extremal Audit Fee

Next part of the research deals with the total external audit fee and effort. The total fee is of a function of number of audit hours multiple by the fee per hour. Assuming that the size of the firms didn't change significantly, the component of audit risk increase for the firms that switch to semiannual

financial reports and thus, we believe that,

Hypothesis 4a: easing the regulation concerning financial report disclosure frequency will increase the total external audit fee for the group of firms that switch to semiannual reports and will not change for the other group of firms.

Hypothesis 4b: easing the regulation concerning financial report disclosure frequency will lead to increased audit hours for the group of firms that switch to semiannual reports and will not change the audit hours for others.

According to the relevant literature audit quality is correlated to BIG 4, thus we expect that,

Hypothesis 5: for the group of firms that apply the relief we assume that the change of the total audit fee payment to the external auditor is moderate for the BIG4.

5. Results

Table 1, shows the number of publicly traded firms on Tel Aviv stock exchange between the years 2008-2018. Over the years we can see a decrease of total firms traded, meaning the new listed firms are lower than the delisted firms are. It can be seen that in 2008 771 firms traded on TASE while on 2018 only 555 firm traded on TASE with net decrease of eight firms on 2018.

Table 1. Number of publicly traded companies in Israel in the years 2008-2018.

Year	New listed	Delisted	Number of publicly traded equity and bond companies
2008	22	34	771
2009	8	38	759
2010	33	46	746
2011	21	43	724
2012	14	70	668
2013	16	57	627
2014	6	41	592
2015	2	23	571
2016	2	16	557
2017	20	14	563
2018	14	22	555

The data was manually collected from the Maya TASE website, and show the total number of companies traded in the Tel Aviv Stock Exchange (TASE) that issued stock and/or debt for each year from 2008 to 2018. We also documented the number of IPOs and delisting for each of those years.

Table 2 shows the final sample of 115 SRE firms in our sample. Table 3, shows the descriptive statistic of our sample of SREs firms. We divided the SRE firms in our research to two different groups according to their decision concerning the regulation shock of decreasing financial reports frequency. 75 firms switch to semiannual reports and 40 firms did not adopt the relief and continue with the quarterly reports.

In 2016, the financial data of total assets, total equity and market value for the firms that adopted the regulation are much smaller than those for the group that continue with quarterly reports: 131,005, 63,887 and 120,634 thousands shekel compare to: 284,481, 109,265 and 219,634 thousands shekel.

Table 2. *The Sample of Small Reporting Entity (SRE) data.*

Sample Selection and Number of Filings Removed	
Starting	183
Didn't publish financial annual reports on time	51
Valid stock pricing	17
Final sample	115
No. of Firms that announce adopting the relief in regulation and switch to semiannual reports	75
No. of Firms that continue publishing quarterly financial reports	40

The data manually collected from Maya TASE website for the years 2016 -2017. We collect from the balance sheet of the financial reports the Total Assets and Equity. We also extracted the stock prices and number of shares of the publicly traded firms in Israel. The firms in this table are defined as Small Reported Entity (SRE), that announce switching or not to semiannual financial reports.

Table 3. *Descriptive Statistic of the two groups of Small Reporting Entity (SRE) firms.*

	Switching to Semi-annual financial reports			Voluntary continue with quarterly financial reports		
	Total Assets	Equity	Market value	Total Assets	Equity	Market value
Year 2016						
AVG	131,005	63,887	120,634	284,481	109,265	219,643
STD	184,725	80,900	183,415	374,561	123,726	258,494
MED	66,732	41,267	73,271	146,413	86,923	157,986
MIN	675	-16,649	2,910	2,896	-118,989	26,845
MAX	797,348	473,416	1,112,719			
Obs.	75			40		
Year 2017						
AVG	136,220	66,907	93,445	273,291	116,197	224,062
STD	185,618	88,534	112,887	275,254	129,441	222,062
MED	69,650	47,105	59,067	178,813	87,459	174,234
MIN	1,706	-31,262	5,225	5,557	-195,429	19,801
MAX	859,359	496,870	813,670	1,134,085	545,025	1,277,141
Obs.	75			40		

We divided the sample to two different groups: those that chose to switch to semiannual financial reports and those that chose to voluntarily continue publishing the quarterly financial reports. (In thousand shekel).

In 2017, the total equity increased for both groups of firms in our sample. Thus, for the group that adopted the regulation relief the market value decrease compare to 2016 while it increase for the others SRE firms.

In Table 4 we show the cumulative abnormal return (-5 to +5

days around the announcement) to firms immediate reports decision of adopting the relief in regulation and publishing only semiannual financial reports. We show two groups of SREs in our sample: firms that switch to semiannual financial reports and those that continue voluntarily with the quarterly financial reports.

Table 4. *Market Reaction to SREs Announcement to the Regulation Relief.*

	N	CAR (-5,+5)	p-value
Voluntary continuing publishing quarterly financial reports	40	0.02*	0.07
Switching to Semi-annual financial reports	75	-0.02**	0.02

***, **, and * denote the significance at the level of 1%, 5%, and 10%, respectively (two-tailed tests).

The data manually collected from Maya TASE (Tel Aviv Stock Exchange) website for the years 2017. We extracted the stock prices and number of shares of the publicly traded firms in Israel. The firms in this table are defined as Small Reported Entity (SRE), divided to two groups according to their preferences to the regulation relief: adopt the relief and switch to semiannual report or voluntary continue publishing the quarterly financial reports.

The CAR (-5,+5) of firms that decrease the frequency of financial reports is -0.020 and significant while the CAR (-5,+5) of the others is +0.025 and significant. The difference in reactions between two groups of firms show that investors find the information in the quarterly financial reports relevance.

In table 5, we examine some corporate governance characteristic of the two groups of SRE using handily collected data on the outside directors serving on the boards of those firms. Our findings show that the boards of the firms that continue with the quarterly financial reports are more diverse; 50% of the outside detractors are women compare to only 32% on the other group. In addition, 81% of the outside directors have financial expertise versus 77% on the other

group. The data on the "busyness" (serving on more than three boards) of the outside directors show that the outside directors serving on boards that voluntary publish quarterly financial reports are much more busy (0.66 versus 0.33).

Table 6 show the institutional investor holdings of the two groups of SRE in our sample. It can be seen that on average the institutional investor holdings is higher for the firms that decided not to switch to semiannual reports, meaning 0.15 versus 0.05.

Our finding of c

orporate governance quality emphasizes the difference between the two groups, meaning that the group that volunteers to continue publishing quarterly financial reports has a higher percentage of outside directors that are financial

experts, more women as outside director, double percentage of "busyness" outside directors and higher institutional holdings. All differences are significant, except the difference of the number of outside directors with financial expertise.

Table 5. Outside Directors Characteristic Year 2017.

	N	Gender 1=Male 0=Female	Financial Expertise	Busy
Voluntary continuing publishing quarterly financial reports	80	0.5	0.81	0.66
Switching to Semi-annual financial reports	140	0.68	0.77	0.33
p - value for differences between the groups		0.03**	0.36	<0.001***

***, **, and * denote the significance at the level of 1%, 5%, and 10%, respectively (two-tailed tests).

The outside directors relevant information were manually collected from Maya TASE (Tel Aviv Stock Exchange) website, from the Management, Discussion and Analysis MD&A, for the year 2017. The firms in this table are defined as Small Reported Entity (SRE), divided to two groups according to their preferences to the regulation relief: adopt the relief and switch to semiannual report or voluntary continue publishing the quarterly financial reports.

Table 6. Investor Institutional Holding of the SRE.

Institutional investor holding	Voluntary continuing publishing quarterly financial reports	Switching to semiannual financial reports
AVG	0.15	0.05
MAX	0.83	0.33
MIN	0	0
MED	0.09	0
STD	0.20	0.09
No. of Obs.	40	75
P -value for difference between the groups	0.002	

The Institutional investor holding were manually collected from Maya TASE (Tel Aviv Stock Exchange) website, for the year 2017. The firms in this table are defined as Small Reported Entity (SRE), divided to two groups according to their preferences to the regulation relief: adopt the relief and switch to semiannual report or voluntary continue publishing the quarterly financial reports.

Table 7 describes the audit fee of SREs that switch to semiannual reports for the years 2016- 2017. The total audit fee per year decrease in 19% from 187 thousands shekel to 157 thousands shekel. The total hours also decrease in 24.7%, from 1392 to 1116. There is almost no change (-3%) in the fee per hour 164 on 2016 to 169 on 2017.

Table 7. Descriptive statistic of audit fee of SRE that switch to Semiannual reports in 2017.

	Year 2016			Year 2017		
	Total Audit fee (In thousands Shekel)	Total Hours	Fee per Hour (in Shekel)	Total Audit fee (In thousands Shekel)	Total Hours	Fee per Hour (in Shekel)
AVG	187	1392	164	157	1,116	169
STD	130	1222	67	118	1023	70
MEDIAN	152	966	147	119	827	152
MIN	40	150	55	35	150	56
MAX	645	6000	433	585	6000	433
Obs.	75			75		

The data manually collected from Maya TASE website, and show the total number of companies traded on the Tel Aviv Stock Exchange (TASE) in 2017 that are defined as Small Reported Entity (SRE), that chose to change frequency of disclosure of the financial report from quarterly to semiannual reports. The data were manually collected from the financial reports.

Table 8. Descriptive Statistic of Audit fee of Firms that Voluntary Disclosure Quarterly Financial Reports.

	Year 2016			Year 2017		
	Total Audit fee (In thousands Shekel)	Total Hours	Fee per Hour (in Shekel)	Total Audit fee (In thousands Shekel)	Total Hours	Fee per Hour (in Shekel)
AVG	326	2240	145	330	2305	143
STD	254	1560	58	49	235	43
MEDIAN	253	1975	151	273	2018	154
MIN	55	225	29	49	235	43
MAX	1279	8260	340	1165	8330	354
Obs.	40			40		

The data manually collected from Maya TASE website, and show the total number of companies traded on the Tel Aviv Stock Exchange (TASE) in 2017 that are defined as Small Reported Entity (SRE), that chose to NOT to change frequency of disclosure of the financial report from quarterly to semiannual reports. The data were manually collected from the financial reports (MD&A).

Table 8 shows the audit fee for those firms that voluntarily continue publishing quarterly financial reports. It is clear that the total audit fee is higher for this group of SRE firms in comparison to the other group mentioned above (Table 6). In

addition, there is a very slight change in the total audit fee for these firms, 326 thousands shekel on 2016 to 330 thousands shekel on 2017. The numbers of hours and the fee per hours are 2240 hours and 145 in 2016, 2305 and 143 in 2017. Interestingly, the fee per hour for the riskier firms is higher.

In table 9, we run a regression test on the parameter that influences total fee audit for the year 2017. Our findings show that the minimum audit fee is 126,627 shekels (significant) and it positively and significantly correlated to the total audit fee of 2016 and to the auditee firm quality (big 4 or others). Additionally, the decision to switch to semiannual reports has a negative and significant influence, meaning it decrease the total audit fee in 117,610 shekel.

$$\text{Total Audit Fee 2017} = \alpha + \beta_1 \text{Total Audit Fee 2016} + \beta_2 \text{Apply the relief} + \beta_3 \text{BIG4} + \varepsilon$$

The dependent Variable is the Total Audit Fee 2017 – is the total annual external audit fee extracted from the MD&A of the year 2017.

Explanatory variable are: Total Audit Fee of the year 2016, the decision to switch to semiannual reports and audit quality (Big 4 or others).

6. Conclusion

In this paper, we investigate exogenous shock of regulation easing to financial reports mandatory disclosure for small publicly traded firms traded in TASE. We find that investors react positively and significantly to firms that announce a voluntary decision to continue with the quarterly reports and that investors react negatively and significantly to those that switch to semiannual financial reports.

Next, we examine the correlation between firm's decisions to voluntarily publish the financial reports quarterly to it corporate governance quality. Our findings according to corporate governance quality examination, using outside directors characteristic show: higher percentage of outside directors with financial expertise, more "busyness" (serving on more than two boards) outside directors, and greater

Table 9. Regression Pricing Audit Fee for the Year 2017.

	Coefficient	t-stat
Intercept	126,637***	5.02
Total fee 2016	0.58***	12.19
BIG 4	60,963**	2.80
Firms that Apply the relief	-117,610***	5.37
No. of Obs.	115	
R square	0.74	

***, **, and * denote the significance at the level of 1%, 5%, and 10%, respectively (two-tailed tests).

The data was manually collected from the Maya TASE website. The linear regression equation that we use is as follows:

gender diversity among the outside directors. Moreover, a higher percentage of institutional holdings for the group of firms that opt not to switch to semiannual reports.

Last, we test the pricing of the total audit fee and effort between the two groups of firms. We find that firms that switch to semiannual reports pay on average 19% less to the audit firm although auditing risk increased. Additionally, the disclosed audit hours decreased on average in almost 25%. The results are moderate for the Big 4 audit firms. These findings show that for small firms, the audit firm price determines the price mainly according to the clients willing to pay for the auditing services.

Our findings show that despite the decrease in auditing fee costs and others costs around preparing the financial reports, the investors find the information in the quarterly financial reports relevant and significant.

Appendix

External Audit Fee Disclosure in the Management, Discussion and Analysis (MD&A) of "Shufersal" firm traded on Tel-Aviv stock exchange in the financial reports package of 2017.

Table 10. Example of disclosure of audit fee from a financial statement.

"Shufersal" Financial Annual Reports 2017				
	2017		2016	
	Total Fee (thousands shekel)	Number of Hours	Total Fee (thousands shekel)	Number of Hours
Auditing and Tax	919	6930	1,205	8,893
Auditing and Tax (daughter company)	209	1,542	195	1,509
Other services	260	851	409	1,397
Total	1,388	9,323	1,809	11,799

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