

# Audit research finds a way to identify listed companies with questionable practices

---



**Pierangelo Rosati**  
CMCRC PhD candidate  
U. of Chieti-Pescara



**Prof Alex Frino**  
CMCRC Research Director  
MGSM, Macquarie U.

**Evidence from research based on Italian listed companies suggests that audit pricing is affected by the information asymmetry that surrounds a company.**

Audit fees are the amount of money that auditors receive for their auditing services from their clients. An abnormally high or abnormally low audit fee is a signal that there may be questionable practices in play at the company. Previous academic studies have determined that audit fees are based on five factors which include audit effort, audit complexity, audit risk, the auditor's prestige and the relationship between the auditor and client. A study by Pierangelo Rosati and Professors Alex Frino & Riccardo Palumbo demonstrates that a relationship also exists between audit fees and information asymmetry. Information asymmetry is where there are different knowledge levels amongst investors in a stock and is measured by the difference in the bid and ask prices (bid-ask spread).

Pierangelo's research was conducted on Italian listed companies because the ownership structure is quite concentrated which makes the incidence of information Asymmetry more significant. Rosati analysed 108 Italian listed companies in the Blue Chip and Star segment (these sections have higher disclosure and governance standards than the rest) of the Borsa Italiana between 2008 and 2011. The research crunched data from both company financial statements and financial market data from a SIRCA dataset.

The main goal of the research was to test the hypothesis that the larger the bid-ask spread, the higher the information asymmetry, the greater the auditing risk and therefore the higher the audit fees. Most importantly, the research results confirm the hypothesis about the bid-ask spread and audit fees. In addition, Rosati's research also confirms the findings of the previous academic research in this field when it comes to the determinants of audit fees except the auditor/client relationship.

Pierangelo's research makes it possible to develop a model that identifies a usual level of audit fee for a company given different company features and also makes it possible to highlight companies that pay too much (over audited) and companies that pay too little (under audited). This is particularly significant because if you can accurately identify abnormal fees it is possible to identify companies that may have questionable practices or a lack of control.

**The Capital Markets Cooperative Research Centre is a world-leading research organisation that provides thought leadership and break-through technology solutions for capital and insurance markets ([www.cmcrc.com](http://www.cmcrc.com)).**