

Investigating the relationship between problems of Agency theory and Auditor's fees in the listed companies in Tehran Stock exchange.

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ABSTRACT: The purpose of this study is to investigate the relationship between agency problems associated with free cash flow and audit fees in firms listed in Tehran Stock exchange. The data were analyzed using statistical population consisted of 80 companies listed in Tehran stock exchange for the time period 2006-2011 through pooled data system and ordinary least square (OLS) regression model in present study involves three hypotheses which examine the relationship between free cash flows, financing policy, and dividend policy as independent variables and the amount of fees paid to the auditor as a dependent variable. With the confirmation of hypotheses, we conclude that free cash flow among the sample companies has a positive significant association with the fees paid to auditors. Also, debt ratio in firms with higher cash flows has a negative significant association with audit fees. In addition, dividend in firms with higher cash flows has a negative significant association with audit fees. *Academ Arena* 2013;5(11):41-48] (ISSN 1553-992X). <http://www.sciencepub.net/academia>. 6

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INTRODUCTION

The main reason of demand for audit services as a regulatory tool can be the conflict of interests between firm owners and managers. The main goal of the independent audit is to determine that if financial statements fairly reflex the results of operations and financial status of the examined firm ? Validity and reliability of the data and quality of audit as proof of the Validity and reliability of financial statements seem Very important statements (Arabi, 2010).

Auditor's fees which is considered a constant cost for client companies, has been a controversial issue in recent years. Audit costs (audit fees) depend on various factors. Playing role as a protector of the interests of society demand that auditor be independent towards his client and carry out his job with as much quality as possible. Many empirical studies conducted have shown that typically, independent auditors are able to discover errors and irregularities in the financial system of the firm addressed (Griffin, Lont, and sun, 2010). Thus, it appears that with the increased planning and trying to address the firm agency problems, auditors will receive more fees. We will test various hypotheses so as to find out how companies with high cash flows and low growth opportunities lead to an increase in auditor's fees for compensating their efforts regarding agency problems. Given the importance of the subject of agency problems and also the free cash flows and determining audit fees, conducting the present study is necessary. If the results show that free cash flow is significantly associated with the amount of fees paid to auditors in the companies studied, it would send a

message to shareholders to consider the factors affecting the determination of auditor's fees and eliminating agency problems and conflict of interests with managers more than ever.

Theoretical bases of the research:

Agency problems are caused primarily by the conflict of interests between managers and shareholders. There is also conflict of interests between major shareholders and minority shareholders in another way. This conflict of interests would cause agency problems and as a result, agency costs, which are transferred to the company and its stakeholders. Managers always seek to prove that they are responsible for shareholder interests and they seek to increase shareholder wealth. On the other hand, owners (shareholders) bear agency costs in order to control the behavior of managers (Jensen, 1986). One of the main agency costs is audit costs. Investors and creditors as individuals outside the company cannot directly control. Opportunistic behaviors of managers. So, through careful and quality investigations, auditors can decrease accruals used by managers and restrict incorrect management decisions. Selecting independent auditors is necessary for monitoring and Validation of accounting data. Because independent auditor's reporting would validate the accounting data and create a foundation for decisions made by the interested parties (stakeholders) in firms. Both groups, managers and owners, are somehow willing to do the audit. So, independent auditor acts as a significant factor in limiting the power of managers in contractual relationships. Application of independent audit

services would subject to some for the company, which result from the addressed risk and workload assessment made by audit work. One factor affecting audit risk is the presence of free cash flow-related agency issues. Firms with high free cash flow and high growth prospects can invest internally which results in less willingness of capital market to analyze such companies. In addition, such companies make auditors feel the need for more activities and efforts. Directors of such companies prefer to invest in projects with negative present value so that they could divide more profits (earnings) (Griffin, Lont, and Sun, 2010). Jensen (1989) defines free cash flow as follows: cash from operating activities after deducting the investment divided by profitable projects. Free cash flow is important, because it allows firms to seek opportunities that would increase the value of shares held by shareholders. Jule and Tsui (2003) in their study found a positive relationship between agency problems of free cash flow and audit fees for firms with low growth. They showed that higher debts would increase this relationship. Companies often use debt for adjusting agency problems so they can decrease cash available for managers. Also, reduced dividend can be a good mechanism for managing extra cash. Therefore, the question we seek to find a proper answer for in the present study is that agency problems related to firms with high free cash flow and low growth opportunities lead to increased fees paid to an auditor? And if the amount of corporate debt and dividend policy is effective in decreasing agency problems and fees paid to the auditor?

Literature background:

Some domestic and foreign studies conducted in this area are described as follows: Jensen (1986) was the first researcher to claim that free cash flows cause agency problems in firms, since they increase the probability of value-decreasing investments. He showed that conflict of interests between shareholders and managers in firms with high free cash flow and low growth opportunities have been more. Change et al (2005) in their study showed that an increase in the audit risk resulted from earnings management practices and manipulation of financial statements would lead to increased audit fees. Change and Kallapur (2003) in their study empirically investigated the relationship between audit quality and auditor's fees. The results indicated that there is a positive significant relationship between audit quality resulting from the impact of discretionary accruals and audit fees. In other words, as audit quality increases, they receive higher fees from clients. Choi, Kim, and Zang (2006) in their study, investigated the factors affecting independent auditors fees and concluded that the amount of claims, firm's return on assets (ROA), and

the size of the audit firm are significantly associated with net fees paid to auditors. Ferguson and Taylor in their study investigated the association between agency costs resulting from free cash flows and independent audit fees in Australian companies. Their results showed that high free cash flow leads to increased audit fees. A research by Griffin, Lont, and Sun (2010) has concluded that agency problems in firms with high free cash flows and low growth opportunities cause auditor of U.S companies to receive more fees to compensate for their double efforts. Also, they showed that high debt cash, like a regulatory mechanism, reduces the amount of audit fees. Other mechanisms for reducing agency costs resulted from free cash flows such as dividend policy and buying back shares can not reduce audit fees. Choi and Gul (2011) in their study entitled "the impact of item of resubmitting financial statements on audit fees among 340 firms from Mexico in the time period from 1992 to 2006" concluded that in firms with higher resubmission, audit fees increase as well. Zarei (2005) investigated the impact of characteristics of audit firm and client on audit fees. The results indicated that auditor's expertise in the client's industry would affect auditor's fees. Thus, audit quality of such firms is higher than other firms. Rajabi and Mohamadi (2008) in an study investigated the relationship between agency costs in terms of corporate governance and audit service pricing in (2005) in Tehran stock exchange (TSE). In their study, they concluded that the institutional shareholder has a negative significant relationship with the amount of audit service fees. Khodadadi and Hajipour (2011) by investigating 95 stock companies during 2006-2009 concluded that in companies with higher free cash flows, there is a positive significant relationship between debt level and audit fees, and a negative significant relationship between future growth opportunities and audit fees.

Study hypotheses:

Given the theoretical bases and earlier studies, and in order to answer the study question, the hypotheses are developed as follows: first hypothesis: Audit fees in firms with high free cash flow are more compared to firms with low free cash flow.

Second hypothesis:

Debt ratio in firms with high cash flow has a negative significant relationship with the amount of auditor's fees.

Third hypothesis: Dividend in firms with high free cash flow has a negative significant relationship with the auditor's fees.

Study models and Variables:

To test the first hypothesis, the regression equation is estimated as follows (Griffin, Iont, and sun, 2010):

$$LAF = \beta_0 + \beta_1 SIZE + \beta_2 SEG + \beta_3 DA + \beta_4 QUICK + \beta_5 LOSS + \beta_6 BANKRUPT + \beta_7 AuditSize + \beta_8 MANU + \beta_9 DIVID + \beta_{10} DUM + \beta_{11} GROWTH + \beta_{12} FCF + \beta_{13} FCF * SIZE + \beta_{14} FCF * LOSS + error$$

Where, Laf=natural logarithm of audit fees, size= indicates firm size, which is calculated through natural logarithm of total assets of the company, SEG=indicates complexity of the company's activities, which is measured by the number departments in a business unit (if a company has more than one subsidiary companies, then the number is considered (1), there wise it will be considered zero), DA=indicates total debts to total assets ratio, quick: indicates quick ratio, which is calculated through current assets minus inventories divided by current debts, Loss= it is a dummy variable, which is (1) in case of loss, otherwise it would be considered zero, BANKRUPT= indicator of financial distress, which is calculated according to Article 141 of the commercial code. it is (1) for distressed companies, and zero for non-distressed companies, Audit size=it is a dummy variable (audit firm size), which is (1) if the organization is an audit firm, otherwise it would be zero, MANU=indicates industry type, which is used as a dummy variable. If the industry is a manufacturing one, it will be (1), otherwise it would be zero, DIVID= it equals dividend ratio, which is measured by DPS (dividend per share) to EPS (earning per share) ratio, DUM= it equals total amount of dummy variables (Four variables), GROWTH=indicates growth opportunities, which is obtained through market value of equities plus debts to total assets ratio, FCF= free cash flow. to confirm first hypothesis, it is expected that β_{13} and β_{14} in the above model be positive and statistically significant. to test second and third hypotheses, the two variables of debt and dividend are added to the above mentioned regression model, then it is estimated as follows (Griffin, Iont, and sun, 2010):

$$LAF = \beta_0 + \beta_1 SIZE + \beta_2 SEG + \beta_3 DA + \beta_4 QUICK + \beta_5 LOSS + \beta_6 BANKRUPT + \beta_7 AuditSize + \beta_8 MANU + \beta_9 DIVID + \beta_{10} DUM + \beta_{11} GROWTH + \beta_{12} FCF + \beta_{13} FCF * SIZE + \beta_{14} FCF * LOSS + \beta_{15} FCF * DA + \beta_{16} FCF * DIVID + error \quad (2)$$

To confirm second and third hypotheses, it is expected that β_{15} and β_{16} , respectively, be positive and statistically significant in the above model. In this part, we describe how to measure independent and dependent variables of the study separately: *free cash flow: free cash flow which is served as the independent variable, will be measured by using the

model introduced by Ient and Paulson (1989) as described by equation (3):

$$FCF_{it} = (EARN_{it} - CSDIV_{it} - CE_{it}) / A_{i,t-1} \quad (3)$$

where, FCF_{it} = free cash flow in year (t) for company (i), $EARN_{i,T}$ =net earnings in year (T) for company (i), $csdiv$ =PROPOSED cash dividend of common stock in year (t) for company (i), $ce_{i,t}$ =capital expenditure in year (t) for company (i), $A_{i,t-1}$ = book value of total assets in year (t-1) for company (I).

Debt ratio:

Debt ratio was used as second control variable of the study. This variable which also indicates the company's business risk, is calculated by the following equation:

$$DE = \frac{TL}{TA}$$

(4).where, TL is total liabilities (debts), and TA is total assets.

Dividend:

Equals the amount of dividends paid to the shareholders, which is approved at the general meeting of shareholders. It is extracted from the statement of retained earnings flow. To homogenize the variables, dividends have been divided by total assets.

Audit fees:

The amount of fees paid to auditor, which is served as a dependent variable. It can be extracted from explanatory notes to the financial statement of sample companies. This variable, like studies by Griffin, Iont, and sun (2010), and ferguson & taylor (2007), are calculated and measured by natural logarithm of audit fees: $LAF_{it} = \ln AF_{it}$ (5)

Where, AF indicates fees paid to the auditor in the current year.

6-Research method: based on purpose, this is an applied research, and it is a correlative-descriptive research by nature and method this study has been carried out based on quasi-experimental research design and using after the events approach (through past data). For data analysis and model estimation, pooled data approach was used. to develop the theoretical bases of the present study, the library method was used and primary data relating to the companies for calculating variables were collected directly from TSE website, the companies financial statements, as well as (tadbeer pardaz) software and used to examine the study hypotheses. So, in the current study, data were collected using field study method. In this study, after mining the data required

from above mentioned sources and preparing variables by using (Excel 2007) and performing necessary calculations in order to achieve the variables needed for carrying out the study, (E view 7) was used to used calculate the regression models using collected data.

Statistical population and sample:

Statistical population in this study consists of all firms that are listed in TSE between 2006-2011 and retained their membership during this period. Among all listed companies, those without any of the following qualifications were eliminated and finally, all the remaining companies were selected for testing: 1-companies whose fiscal year is not ended in march 29th or 30th, have been eliminated from the list. 2- banks, financial institutions, and investment companies were eliminated. 3- companies not having all necessary data for calculating the variables during

the study period have been eliminated. 4-companies must be listed in TSE before (2006) and also they must not change their fiscal year during the period of investigation. After examining listed companies in TSE and applying the above conditions and limitations, a total of 80 companies (equals 480 year of company) were selected model estimation and hypothesis testing.

Findings:

(8-1) descriptive statistics: first, using raw data, the values of variables were calculated and then, descriptive statistics of the independent and dependent variables including mean, median, max, min, and standard deviation (SD) of the data were calculated and presented in table(1). these values provide an overview of the data distribution status. All data associated with the variables were mined from financial statements of the firms listed in TSE.

Table 1: descriptive statistics of the variable:

Variables	SYMBOL	MEAN	MEDIAN	MAX	MIN	SD
Auditor's fees	LAF	4.3865	4.1439	6.4236	-2/5428	./8529
Firm size	SIZE	5.4364	5.4364	7.9343	-4/7108	1.8562
Complexity of firm Activity	SEG	./3839	./4254	1.0000	./0000	./1767
Liability (debt) Ratio	DA	./6238	./6869	8.8049	-1/4176	./5962
Quick ratio	QUICK	./1299	./1123	./4137	-./887	./0627
loss	LOSS	./2638	./3283	1.0000	./0000	./0238
Financial distress (bankruptcy)	BANKRUPTCR	./4139	./3673	1.0000	./0000	./0683
Audit firm size	AUDITSIZE	./3486	./2982	1.0000	./0000	./0683
Client's industry	MANU	./4729	./4462	1.0000	./0000	./1689
dividend	DIVID	./6739	./6428	1.4809	-./1427	./0906
Total dummy variables	DUM	2.8094	3.0892	5.0000	./0000	./2178
Firm Growth	GROWTH	./3683	./3884	./8699	-./4126	./2436
Free cash flow	FCF	./2639	./3226	./6704	-./1344	./4339

- **SOURCE:** calculation by the researcher regarding the financial strength variable (LAF), one can see that its mean is (4/38) indicating that most data associated with the variable are around this value. its mean is (4/14) indicating that about half of its data were larger than this value and the other half were smaller than it. Also, the standard deviation (SD) is ./85, showing that data fluctuations around the mean have been ./85. Other variables can also be interpreted similarly.
- **test to determine the Appropriate model in pooled data:** in this study, the number of observations for each section was 80 observations(company) for a 6-year time period. for pooled data analysis, a total of 480 observations (year-company) were used. when applying pooled data different models are used for hypothesis testing. these models include methods such as fixed Effect model, random Effect model, and pooled data model. To examine the type of model testing in different sections and time periods of pooled data, liner (F) test (Chow) and houseman test were used, which are presented in table(2). Results of Chow test for the first model confirm null hypothesis of this test that intercept is the same in all periods and thus, rejecting first hypothesis. so, pooled data estimation method is a better choice for first model estimation. according to this method, all data are put together and estimated by ordinary least square regression (OLS). However, regarding second model, the results of Chow test did not confirm null hypothesis of this test that intercept is the same in all periods. Therefore, panel model(fixed or random effects) should be used for second model testing. in order to select the best model among fixed and random effect models, Housman test was used.

• Table(2): results of Chow test:

model	Indicator for measuring environmental uncertainty	statistic	p-value	Test result
First model	Chow test	2.3249	./3268	Pooled data model
	Housman test	-	-	-
Second model	Chow test	6.5802	./000	Panel data
	Housman test	./4246	./8627	Random effect model

*source: calculation by the researcher

Results of Housman test for second model shows that null hypothesis of the test is confirmed. So random effect model was selected for second model estimation. (8-3) hypothesis testing: A-results of first hypothesis testing: first hypothesis of the present study investigates the relationship between free cash flow and auditor's fees. Results of first model significance testing and evaluation of the coefficients through pooled data model during (2006-2011) can be seen in table (3). As shown in table(3), (F) statistic is significant at./99 confidence level. thus, it can be concluded that the study model is general significant and independent and control models have the power to account for the model's dependent variable. In addition, the adjusted determination coefficient resulting from model testing was (.4293).this figure shows that about 43 percent of changes in the dependent variable, namely audit fees, is due to changes in independent and control variables existing in the model, and the remaining 57 percent of its changes is caused by other factors. To evaluate self-correlation of the regression model residuals, Durbin-Watson. test has been used. results of this test are obtained simultaneously with regression model estimation in the environment of E views. its optimal value for the absence of self-correlation is (2). if the value of this statistic is between 1/5-2/5, then self-correlation in error values of the model is rejected. Durbin-Watson statistic of the first regression model, which can be seen in table(4-4), is (1/8904). Given the value of Durbin-Watson statistic obtained, self-correlation in error values of the model is rejected.

Table (3): Results of first model testing:

Description	PARAMETER	COEFFICIENT	T-STATISTIC	P-VALUE
Constant	β_0	./0818	4/2316	0/0017
Size	β_1	1/1138	4/8794	0/0153
SEG	β_2	1/3809	6/0267	0/0000
DA	β_3	0/0026	3/3249	0/0000
QUICK	β_4	-0/1729	-2/0928	0/1744
LOSS	β_5	1.0216	1/3269	0/1192
BANKRUPT	β_6	0/2674	0/8342	0/2946
AUDITSIZE	β_7	0/4396	2/8243	0/0326
MANU	β_8	0/1894	0/3241	0/2139
DIVID	β_9	0/2905	0/4266	0/0893
DUM	β_{10}	-0/1657	-2/9846	0/0166
GROWTH	β_{11}	0/2128	2/6518	0/1218
FCF	β_{12}	0/0084	4/8463	0/0186
FCF*SIZE	β_{13}	0/4136	3/8674	0/0236
FCF*LOSS	β_{14}	0/0164	6/4236	0/0000
ADJUSTED R ²	0/4293			
F-STATISTIC	6/4358			
P-VALUE	0/0000			
D-W	1/8904			

Source:

Calculations by the researcher According to the results in table (3) t-statistic is related to the independent variable (FCF_t), and its significance level (p-value) is 4/8463 and 0/0186, respectively. given that error level intended for the present study was 0/05, thus with respect to this variable we may conclude that free cash flow with 0/05 error level is significantly associated with fees paid to the auditor. Coefficient of the variable FCF_t(β_{12}) is positive. As a result, the type of relationship between free cash flow and fees paid to the auditor is direct. In other words, as free cash flow increases among sample member firms, the rate of fees paid to the auditors of those firms goes up as well. Analyzing t-statistic for other explanatory variables is performed similarly. As discussed in chapter

(3), in order to confirm or reject first hypothesis, one should consider the significance of the coefficients β_{13} and β_{14} in the model. In other words, the variables intended by the researcher for confirming first hypothesis are $(FCF_t^* size_t)$ and $(FCF_t^* loss_t)$. According to the results of model estimation, t-statistic is associated with the independent variable $(FCF_t^* size_t)$, and its significance levels (p-value) are 3/8674 and 0/0236, respectively. These figures show that the coefficient of the variable is statistically significant at confidence level of (0/095). The same values for the independent variable $(FCF_t^* loss_t)$ are (6/4236) and (0/0000), respectively. These figures show that the coefficient of the variable is statistically significant at 0/99 confidence level.

(B)-result of second hypothesis testing:

Second hypothesis of the study examines the relationship between debt ratio and auditor's fees. In this hypothesis, the dependent variable is audit fees, and the independent variable is debt ratio, second and third hypothesis are tested using a regression model. Results of second model significance testing and evaluating the coefficients by random effect method during 2006-2011 are shown in table (4). As seen in table (4) f-statistic is significant at 0/99 confidence level. Thus, we conclude that this model is generally significant as well, and independent and control variables are able to account for the model's dependent variable. The adjusted determination coefficient resulting from model testing was (0/3148). This figure shows that about 31 percent of changes in the dependent variable, that is the auditor's fees, is due to change in the independent and control variables existing in the model. Durbin-Watson test statistic of second regression model shown in table (4), is (1/9894). According to the value of Durbin-Watson statistic obtained, the presence of self-correlation in the model's error value is rejected.

Table(4): result of second model testing:

Description	PARAMETER	COEFFICIENT	T-STATISTIC	P-VALUE
Constant	B ₀	0/0924	4/0089	0/0000
Size	B ₁	1/5428	2/4237	0/0043
SEG	B ₂	0/5476	4/5436	0/0060
DA	B ₃	0/0426	3/65589	0/0276
QUICK	B ₄	-0/1128	-2/6537	0/0328
LOSS	B ₅	1/9833	1/8905	0/0782
BANKRUPTCY	B ₆	-0/2537	-0/9078	0/1687
AUDIT SIZE	B ₇	0/0231	4/2133	0/0098
MANU	B ₈	0/1218	-3/2166	0/0000
DIVID	B ₉	0/1068	0/4268	0/2139
DUM	B ₁₀	-0/2136	-0/9808	0/1687
GROWTH	B ₁₁	0/4255	2/2265	0/0534
FCF	B ₁₂	0/0894	3/8790	0/0313
FCF*SIZE	B ₁₃	0/1216	2/8676	0/0227
FCF*LOSS	B ₁₄	0/3144	6/7556	0/0000
FCF*DA	B ₁₅	-0/0897	-4/2437	0/0098
FCF*DIVID	B ₁₆	-0/3146	-3/1165	0/0435
ADJUSTED R ²			0/3148	
F-STATISTIC			6/1328	
P-VALUE			0/0000	
D-W			1/9894	

SOURCE:

Calculation by the researcher in order to verify the confirmation or rejection of second hypothesis, we should consider the significance of the variable intended by the researcher (FCF*DA) in second model. According to the results of model estimation, t-statistic is related to the independent variable (FCF*DA) and its significance levels (p-value) are (-4/2437) and (0/0098), respectively. These figures show that the coefficient of the variable is statistically significant at 99% confidence level.

(C) – results of third hypothesis testing: third hypothesis examines the relationship between dividend and auditors fees. In this hypothesis audit fees is the dependent variable and dividend is the independent variable. To confirm or reject second hypothesis, we have to consider the coefficient of the variable intended by the researcher (variable FCF*DIVID) in second model. As seen in tables (4-5), t-statistic is associated with the independent variable FCF*DIVID, and its significance levels (p-value) are (-3/1165), and (0/0435), respectively. These figures

show that the coefficient of the variable is statistically significant at confidence level of (%95).

Conclusion and suggestions

Results of first regression model estimation indicates that the coefficient of the independent variables in the model, namely (FCF*LOSS) and (FCF*SIZE), were significant at error levels of (%1) and %5, respectively and there is a direct positive relationship between free cash flow and audit fees. In other words, the findings confirm this hypothesis. thus we can claim that auditor fees are higher in firms with higher cash flow. the results of hypothesis testing can be explained as follows: agency problems are primarily caused by the conflict of interest between managers and share holders. This conflict of interest would cause agency problems and thus, agency costs, which will be finally transferred to the company and its stakeholders. Owners(shareholders) incur agency costs in order to control the behavior of managers. One of such costs is audit costs when a company has more free cash flow, the management can use it in various ways the most important of which are investment in projects or paying more dividends to shareholders. In such situations, in order for shareholders to receive more dividends, they may show more care about the company and expend more costs to receive more dividends and control opportunistic behavior of the management. so, with an increase in free cash flow as well as increased agency problems, more cash is paid to monitor the management behavior. Results of first hypothesis testing are similar to the results by jule and tsui (2003), ferguson and taylor (2007), and griffin, lont, and sun(2010). Results of second regression model estimation showed that the coefficient of the independent variable in the model, namely (FCF_T*DA_T) is significant at error level of (%1)and there is a negative relationship between debt ratio in firms with high free cash flow and audit fees. In other words, findings confirmed second hypothesis. Thus, as debt ratio increases in firms with higher free cash flows, higher fees will be paid to auditors. Results of the hypothesis testing could explained as follows: we previously discussed that agency problems are caused by a conflict of interest between managers and shareholders and this conflict of interests would lead to agency problems and thus, agency costs including audit costs. Increased debt ratio is usually due to an increase in liabilities(debts) and loans received, which leads to increased corporate risk. On the other hand, firms often use debts for adjusting agency problems of free cash flow through which available cash for managers is reduced. thus,with increased debts, agency problems would also be increased and shareholders pay more cash to control and monitor the

management behavior. Results of second hypothesis testing are similar to results by Griffin, lont, and sun(2010), however inconsistent with those by khodadadi and Hajipour (2011). results of third regression model estimation suggested that the independent variable coefficient in the model (the vats of third regression model estimation suggested that the independent variable coefficient in the model (the variable FCF*viabile FCF_T*DIVID_T) is significant at error level of (%5) and there is a negative relationship between dividend rate in firms with high free cash flow and audit fees. In other words, findings confirm third hypothesis. thus, as dividends. Increase in firms with higher free cash flow, higher used. This leads to increased agency problems. Results of the hypothesis testing are consistent with those by Griffin, lont, and sun (2010).there been some limitations in the course of our study, one of which is lack of control over some factors affecting the results, for instance, the impact of variables such as economic factors affecting the results, for instance, the impact of variables such as economic factors, political conditions, researcher and may be effective on evaluating the relationships. Another limitation is non- adjustment of financial statement items due to inflation that can be effective on the results. Given the results obtained in this study, we recommend that investors consider the amount of free cash flows in firms, since the decisions made by the management regarding such cash can largely determine management standards in optimally using resources upon suitable management opportunities. Debt and dividends are procedures for cash flow withdrawal and dividend is similar to debt in that upon approval, it must be paid by the firm in a short time-managers should notice that because debt (liabilities) are less flexible than dividends, they might be a better control mechanism for making managers pay future cash. Based on the results obtained in the present study, the following suggestions are presented for future research:1- investigating the impact of operating cash flow on the amount of fees paid to auditors and comparing in with free cash flow in stock companies. 2- Investigating the impact of agency problems on fees paid to auditors separately in different industries and comparing the results among industries.

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