8-2019

Informativeness of the expanded audit report: Evidence from China

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***** We thank Donghui Wu, and Yuan Zhang for their constructive feedback and suggestions. We also thank discusser Ryan Ballestero and other participants at 2020 Auditing Section Midyear Meeting and workshop participants at Tsinghua University and Central University of Finance and Economics for helpful comments. Goh thanks the Lee Kong Chian Fellowship at Singapore Management University for financial support. Li acknowledges financial support from National Natural Science Foundation of China (No. 71772105).

Informativeness of the Expanded Audit Report: Evidence from China

Abstract

This study investigates whether the expanded audit report is informative to investors in the setting of an emerging economy. Using the recent staggered adoption of the expanded audit report for A+H and A share firms in China, we find robust evidence that abnormal trading volume and earnings response coefficients are higher, and stock price synchronicity are lower, in the post-adoption periods than in the pre-adoption periods. In additional tests, we find that the expanded audit report is more informative for non-State Owned Enterprises and for firms with higher information asymmetry. To the best of our knowledge, our study is the first to document systematic evidence that the expanded audit report is incrementally informative to investors in an emerging economy.

Keywords: expanded audit report; information content; key audit matters

JEL Classifications: M41, M42, M48

Data Availability: data are available from the public sources cited in the text

I. INTRODUCTION

Prompted by the global financial crisis, the investment community has been calling for greater transparency from auditors to give users of financial statements more insights into the audit process and the auditor's roles. Standard setters internationally have responded by revamping the audit report to provide more than a pass/fail opinion. In 2013, the auditors of UK listed companies were required for the first time to include a discussion of the key risks identified in the audit and how they are being addressed in the audit report. Other jurisdictions have followed the lead of UK in introducing greater disclosures in the audit process. For example, in January 2015, similar requirements were introduced in the International Standards on Auditing (ISAs) with an effective date of financial years ending on or after 15 December 2016. In June 2017, the Public Company Accounting Oversight Board (PCAOB) enacted a new auditor reporting standard that requires the auditor to include a discussion of critical audit matters and to provide audit-specific information about particularly challenging, subjective, or complex aspects of the audit.[1]

Whether the expanded audit report provides information useful to investors continues to be a debatable question. On the one hand, regulators hope that the expanded audit report requirements will make the audit more relevant and informative to financial statement users, thereby reducing information asymmetry about the company's financial reporting (e.g., FRC 2013; PCAOB 2017). Supporting this notion, experimental studies

[1] Communication of critical audit matters for audits of large accelerated filers will be effective for fiscal years ending on or after June 30, 2019, and communication of critical audit matters for audits of all other companies will be effective for fiscal years ending on or after December 15, 2020.

provide evidence that market participants find the risk disclosures in the expanded audit report useful for decision-making (e.g., Christensen, Glover, and Wolfe 2014; Kachelmeier, Rimkus, Schmidt, and Valentine 2019; Gimbar, Hansen, and Ozlanski 2016). On the other hand, empirical studies find little or no evidence to support the information content of the expanded audit report. Specifically, Gutierrez, Minutti-Meza, Tatum, and Vulcheva (2018) fail to find that the new U.K. auditor reporting or the variation in the expanded reports' content significantly affect investors' reaction to the release of auditors' reports. Lennox, Schmidt, and Thompson (2018) do not find risk disclosures incrementally informative using short-window market reactions but find risk disclosures reliably capture the uncertainty in accounting measurements using long-window tests. Our study provides new insights on this debate by examining the informativeness of the expanded audit report in the setting of an emerging economy—China.

On 23 Dec 2006, the Chinese Institute of Chartered Public Accountants (CICPA) issued No.1504 Auditing Standard that requires auditors to disclose key audit matters (KAM) in audit report. China offers a unique setting to examine the informativeness of the expanded audit report for several reasons. First, A+H share firms, which are listed on both the stock exchanges in Mainland China and Hong Kong, are required to adopt the new audit reporting after January 1, 2017 and all other A share firms, which are listed only on the stock exchanges in Mainland China, are required to adopt it after January 1, 2018. This phased adoption affords a quasi-natural experimental research setting that allows us to compare changes in the treatment group with changes in the control group subsequent to the expanded audit report requirements. Second, concurrent studies focus on the new

audit reporting model in the U.K. which also require auditors to discuss in addition to the key audit matters, the applied materiality threshold and how it affects their audit scope. Because the disclosed materiality threshold could be informative of the firm's financial reporting quality (Goh, Lee, Li, Li, and Wang 2019), this can potentially confound any analyses that are solely interested in examining how the market reacts to the new risk disclosures. On the other hand, the new China auditing reporting standard only requires auditors to disclose key audit matters, hence allowing us to better isolate the effects of any market reactions to the risk disclosures content of the expanded audit report. Third, China have a different information environment from the U.K. that allows us to provide evidence on the informativeness of the expanded audit report in a contrasting setting. Further, as the world's largest emerging economy, China is economically significant and provides rich market depth for our empirical tests to explore cross-sectional variation in the effect of the expanded audit report.

Whether investors would find the expanded audit report incrementally informative in the China setting is not immediately obvious. On the one hand, there is a low demand for high quality external reports and information for control purposes because many publicly listed companies are still state-controlled. State-controlled firms also have less incentive to disclose bad news in a timely manner (Ball, Kothari, and Robin 2000; Piotroski, Wong, and Zhang 2015). Given the limited firm-level reporting and lack of alternative sources of information for investors (e.g. dissemination of information by financial intermediaries and media are ineffective), investors are more likely to find the risk disclosures in the expanded audit report incrementally informative vis-à-vis investors in

more developed economies. Furthermore, the prevalence of earnings management in China suggests that investors are more vulnerable to management's expropriation of firm resources and hence there would be a stronger demand for risk disclosures information in the audit report to better assess firms' earnings quality.

On the other hand, there are reasons to believe that investors would not find the risk disclosure informative. First, prior research fails to find evidence that financial disclosure and mandatory reporting regulation are effective in an emerging economy. For example, He, Wong, and Young (2012) find that mandatory adoption of the International Financial Reporting Standards does not increase earnings' usefulness in China. Second, because auditor independence is relatively weaker in China compared to most developed economics, it is questionable whether investors would find the risk disclosures supplied by auditors credible enough for decision-making.

We empirically examine the informativeness of the auditor risk disclosures using firms listed on the Mainland China stock exchanges. We exploit the staggered adoption of the expanded audit report by A+H and A share firms, and use both pre-post and difference-in-differences research designs for our analyses. Our main proxies for the informativeness of the expanded audit report are: (1) cumulative absolute abnormal returns and abnormal trading volume around the issuance of the annual report, which includes the auditor's report, (2) earnings response coefficients, and (3) stock price synchronicity. Based on the sample period from fiscal years 2014 to 2018, we obtain the following results.

First, we find little or no evidence that the three days abnormal returns surrounding the date of the issuance of the expanded audit report is significantly greater in the post-

adoption period compared to the pre-adoption period. However, we find that abnormal trading volume significantly increases following the adoption of the expanded audit report. This result provides evidence that the expanded audit report provides new information to investors. Second, we find that the earnings response coefficient is significantly greater after the adoption of the expanded audit report. This finding is consistent with the notion that the expanded audit report enhances investor perceptions of the firm's financial reporting quality. Finally, we find that stock price synchronicity significantly decreases following the adoption of the expanded audit report. This result suggests that the expanded audit report facilitates the flow of firm-level specific information to capital market, thus enabling investors to focus more on firm-level unique information for decision-making.

We conduct several analyses to validate our inferences. For example, we re-estimate our main tests using alternative measures for the informativeness of the expanded audit report and obtain similar results. Next, given that A+H share firms may have fundamentally different characteristics from the other A share firms, we test the robustness of our results using entropy balancing method and propensity score matched sample. We continue to find similar results. In addition, to dispel the notion that the market reaction that we documented are driven by a differential time trend for treatment and control firms, we test the parallel trend assumption and find supportive evidence.

We also gain additional insights by conducting several cross-sectional tests and further analyses. First, we examine whether the expanded audit report is more informative in circumstances where there is a greater demand of information for decision-making. Consistent with our expectations, we find that the increases in abnormal trading volume

and ERCs, and the decrease in price synchronicity in the post-adoption periods are more pronounced for non-State Owned Enterprises, smaller firms, and firms that have lower analyst following. Second, to afford stronger inference that the investors' reaction that we documented earlier are more likely attributable to the expanded audit report rather than the annual report, we also examine the number of downloads of the audit report relative to the number of downloads of the annual report surrounding the adoption of the expanded audit report. Consistent with our expectations, we find that audit report downloads relative to annual report downloads is significantly greater in the post- than in the pre-periods. In addition, we find that the negative market reaction to modified audit opinions is more pronounced in the post-periods, indicating that the expanded audit report is also more informative in terms of understanding the implications of modified audit opinions. Finally, we examine whether the informativeness of the expanded audit report could be in part due to an increase in the quality of the auditor's work. We find that for A share firms, discretionary accruals decrease and audit fees increase in the post-adoption periods, suggesting that auditors curb more discretionary accruals and exert more audit efforts in the post-adoption periods.

Our study contributes to the ongoing debate over the usefulness of the auditor's report reforms. To the best of our knowledge, our study is the first to examine the informativeness of the auditor risk disclosures in an emerging economy. It extends and complements existing studies such as Gutierrez et al. (2018) and Lennox et al. (2018) who find that the expanded audit report is not incrementally informativeness in a large and developed economy such as the U.K. By exploiting the staggered adoption of the new

audit report requirements in China, we are able to afford stronger causal inference on the informativeness of auditor risk disclosures in the second largest economy in the world. Our findings suggest that the risk disclosures in the expanded audit report are incrementally informative to investors in a setting where this information is less likely to be available in alternative public sources and where demand for such information would presumably be high. This finding is in line with the view of regulators that "expanded auditor reporting may be relatively more informative for companies where alternative sources of information are less available" (PCAOB 2017). Our finding also supports Chen, Jiang and Zhang (2019) who show that audit quality disclosure increases auditors' effort incentives, if and only if the underlying financial reporting quality is relatively weak. Given that less developed countries such as China have weaker financial reporting quality, our results suggest that additional risk disclosures (which is informative of audit quality) can induce greater audit effort and hence higher audit quality; this can enhance the decision-usefulness of financial reports for the investor.

A concurrent study by Liao, Minutti-Meza, Zhang, and Zou (2019) (hereafter "LMZZ") examine the effect of KAMs for companies listed in Hong Kong and they do not find evidence that KAMs provide incremental information to investors or that the new rules affect audit fees or quality. There are major differences between our study and LMZZ. First, in our difference-in-differences research design, our treatment group comprises either A+H share firms (i.e., firms listed in both Mainland China and Hong Kong stock exchanges) that first adopt the expanded audit report after 1 Jan 2017, or the A share firms (i.e., firms listed only in mainland China stock exchanges) that first adopt

Commented [无名1]: As discussed before, we need to stress more that there are some differences between A-share and H-share (even firms operated in same area Mainland China). For example, A-share is a devolving capital market whose over 90% investors are retail investors while H-share is a developed market whose main investors are institutional investors. In other words, H-share is more alike UK, US capital market.

the expanded audit report after 1 Jan 2018. In the above design, the control group comprises the A and A+H share firms, respectively. On the other hand, in LMZZ, the treatment group comprises firms listed in the Hong Kong stock exchange that are subject to the new audit report requirements and the control group comprises firms listed in Mainland China stock exchanges. Second, our measures of informativeness of the expanded audit report are absolute abnormal returns, abnormal trading volume, earnings response coefficients (ERC), and stock price synchronicity. On the other hand, LMZZ focuses on absolute abnormal returns, abnormal trading volume, and bid-ask spreads. Finally and more importantly, LMZZ fails to find any evidence that KAMs provided incremental information to investors in the Hong Kong setting. In strong contrast, we find robust and consistent evidence of the informativeness of the expanded audit report in the setting of China, an emerging market. Together, our study and concurrent studies can help inform standard-setters and regulators around the world, especially those in developing economies, who would otherwise be skeptical about the usefulness of the risk disclosures in the expanded audit report. Our study further suggests that standard-setters and regulators should calibrate disclosures in the audit report to suit the unique institutional environment of each country.

The remainder of our paper proceeds as follows. The next section discusses the related literature and develops hypotheses. Section 3 describes the data and research methodology. Section 4 presents the primary analyses and Section 5 presents the additional analyses. Section 6 concludes.

II. BACKGROUND, RELATED LITERATURE, AND HYPOTHESIS DEVELOPMENT

Background and Related Literature

Auditors play a critical role in the capital markets by monitoring management and protecting shareholders' interests through an independent examination of the financial statements. However, the traditional audit report has been challenged by investors because it lacks firm-specific information to address the information asymmetry between investors and auditors (PCAOB 2017). In response to demand for a more informative auditor's report, standard-setters, regulators, and auditors worldwide have taken steps to promote audit reporting reforms. The Financial Reporting Council (FRC) in the U.K. took the lead by introducing new requirements for auditor's reports on companies with effect for periods commencing on or after 1 October 2013. Specifically, ISA (UK and Ireland) 700 (Revised) ("ISA 700") requires auditors to include within their audit reports (a) a description of those assessed risks of material misstatement that were identified by the auditor and which had the greatest effect on the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team; (b) an explanation of how the auditor applied the concept of materiality; and (c) a summary of the audit scope, including an explanation of how the scope was responsive to the assessed risks of material misstatement described in (a) and the applied materiality as described in (b). Following Lennox et al. (2018) and for brevity, we refer to the disclosures in requirement (a) as "auditor risk disclosures"

Other regulators followed the lead of FRC in mandating more auditor risk disclosures. In January 2015, IAASB released the revised International Standards on Auditing Reporting Standards, *Forming an Opinion and Reporting on Financial Statements* and *Communicating Key Audit Matters in the Independent Auditor's Report*. The most significant change is for the auditors to include Key Audit Matters (KAMs) in the auditor's report (IAASB 2015) for fiscal years ending on or after December 15, 2016. KAMs, which are selected from matters communicated with those charged with governance, are those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. On Dec 28, 2016, the Chinese Institute of Certified Public Accountants (CICPA) followed the lead of IAASB and issued the Auditing Standard (No. 1504) "Communicating KAMs in the Independent Auditor's Report", which require auditors to address KAMs identified during the present audit engagement. More recently, the Public Company Accounting Oversight Board (PCAOB) finalized its reform on audit reporting in June 2017, mainly requiring the auditor to discuss critical audit matters (CAMs), auditor tenure, and audit firm independence in the audit report. CAMs are defined as issues communicated to the audit committee that relate to material financial statement accounts and that involve challenging, subjective, or complex auditor judgment (PCAOB 2017).[2] Hence, both KAMs and CAMs are similar in spirit (in terms of intent and content) to the audit risk disclosures requirements by the FRC.

[2] A CAM is defined as any matter arising from the audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial
statements, and (2) involved especially challenging, subjective, or complex auditor judgment.

Experimental studies find mixed results on how the expanded audit reporting affects investor decisions. For example, Christensen et al. (2014) find that experimental participants are more likely to change their investment decisions when a CAM is included in the audit report than when they are not. Similarly, Doxey (2015) find that a CAM causes experimental participants to perceive a lower risk of misstatement and thus increase their tendency to invest. Kachelmeier et al. (2019) find that their experimental participants have less confidence and perceive less auditor responsibility for a misstatement in a financial statement area disclosed in the auditor's report as a CAM. However, Gimbar et al. (2016) found that both related and unrelated CAMs increase auditor liability, but to a lesser degree under imprecise standards.

Empirical studies found little or no evidence that the expanded auditor's report providing little incremental information to investors. Reid et al. (2019) find that the new auditor reporting regime in the U.K. is associated with an improvement in financial reporting quality as proxied by significant decreases in absolute abnormal accruals and the propensity to just meet or beat analyst forecasts, and a significant increase in earnings response coefficients. However, Gutierrez et al. (2018) fail to find any evidence that the regulatory change in the U.K. or the variation in the expanded reports' content significantly affected investors' reaction to the release of auditors' reports. Using short-window market reactions tests, Lennox et al. (2018) find that the risk disclosures generally lack incremental information content. In additional analysis, they explore whether the risk disclosures lack incremental information content because investors already know about the risks from other sources, such as annual reports, conference calls, and earnings announcements. They

find that approximately 65 percent of the risks disclosed by auditors in the audit report had already been previously disclosed by management or the audit committee.

The finding in Lennox et al. (2018) is consistent with the argument that risk disclosures may not be incremental informative in the U.K. setting because this information could already exist in public domain. It is also consistent with PCAOB's (2017) view that "expanded auditor reporting may be relatively more informative for companies where alternative sources of information are less available". Prior literature has shown that country's institutional infrastructure could influence their financial reporting practices and disclosure decisions (e.g., e.g., Ball et al. 2000; Ball, Kothari, and Wu 2003; Leuz, Nanda, and Wysocki 2003; Bushman, Piotroski, and Smith 2004). Because the U.K. is a developed market with strong investor rights and legal enforcement, risk disclosures information may be more easily obtainable from alternative public sources, thus rendering them less useful when disclosed in the audit report. For that reason, our study exploits the unique institutional features of China to investigate the informativeness of the expanded audit report in an emerging economy.

Hypothesis Development

We argue that there are at least two reasons why investors would find the risk disclosures information in the expanded audit report informative in China.

First, although China have achieved significant economic growth since the 1980s, it still lacks the institutional arrangements that create incentives for high corporate transparency (Piotroski and Wong 2012). For example, although the government has corporatized its state enterprises by listing them on the stock exchanges, it still maintains

ownership control of these listed companies and retains the rights to appoint its CEO. As a result, stated-controlled firms still constitute a significant part of the stock exchanges. Because the government can use internal reporting mechanism and performance measures to monitor CEOs directly, this provides lower incentives for high quality external reports and information for control purposes. Furthermore, instead of wealth maximization, politically connected firms have incentives to suppress bad news in order to hide inefficiencies and rent-seeking activities, as well as to pursue political objectives (Piotroski, Wong, and Zhang 2015).

Due to limited firm-level reporting and disclosure practices, investors would have to rely on alternative sources, such as financial intermediaries or media, for firm-specific information. However, the market for financial analysts is not well developed in China as Chinese analysts face limited information and incentives when making firm-level forecasts (Ang and Ma 1999; Chen, Ke, and Yang 2013). In addition, the vast majority of media outlets in China are controlled by the government, and hence firm-specific information disseminated by these media outlets tends to be biased and constrained (Piotroski and Wong 2012). Given the opaque information environment and lack of alternative sources of information, the auditor's report issued in China, especially with the accompanying new audit risk disclosures, becomes a more formal and salient source of information, vis-à-vis similar reports issued in developed countries. Consistent with this notion, Chen, Su, and Zhao (2000) find that Chinese investors react significantly and negatively to modified audit opinions and argue that the lack of competing information sources in the Chinese market may explain why announcements of initial MAOs attract so much attention from investors.

Consequently, we expect investors in China to find the mandated risk disclosures information in the expanded audit report incrementally informative vis-à-vis those in more developed economies.

Second, we expect the risk disclosures information to be incrementally informative in China because of the prevalence of earnings management. In general, earnings management tends to be a greater concern in countries with weak institutional framework and investor protection (Leuz et al. 2003). In the China context, earnings management is exacerbated by regulatory pressure and financial needs. For example, firms must make two consecutive years of profits before they can be listed on an exchange (Aharony, Lee, and Wong 2000). In addition, according to guidelines introduced by the China Securities Regulatory Commission (CSRC) in 1998, a listed firm will be designated a special treatment (ST) firm if it reports a net loss for two consecutive years. A ST firm's semi-annual report must be audited. If it reports a net loss for three consecutive years, it will be suspended from normal trading. As a result, Chinese firms engage in both accruals-based earnings management and real transactions to achieve specific ROE targets and avoid losses (Piotroski and Wong 2012). Furthermore, the widespread use of related party transactions and group and pyramidal ownership structure afford more opportunities to manage earnings in China (Jian and Wong 2010; Piotroski et al. 2015). Given that outside investors in China are more vulnerable to management's expropriation through earnings management, we hence expect investors to have a stronger demand for risk disclosures information in the audit report to enable them to better assess the firm's earnings quality.[3]

[3] A recent paper by Chen, Jiang and Zhang (2019) also supports our contention that investors would find the audit risk disclosures more informative in less developed countries that have weaker financial reporting quality. Specifically, the

Notwithstanding the above arguments, there are also reasons to believe that investors may not find the risk disclosures incrementally informative in the China setting. First, prior research finds that the economic effects of disclosure regulations tend to be limited in China. For example, Barber, De George, Lehavy and Trueman (2013) find that while earnings announcement premia generally exist across the globe, such a phenomenon is absent in China. In addition, He et al. (2012) suggest that in emerging markets such as China, the intended benefits of improved transparency through mandatory adoption of high quality accounting standards, such as International Financial Reporting Standards (IFRS), may fail to materialize. One possible reason is that IFRS, an accounting system oriented towards providing relevant information to investors, may not fit with environments in which accounting plays a less powerful contracting role.

Second, auditor independence in China is weaker compared to most developed economics because audit firms and the Chinese accounting profession are not only regulated but also supervised by their local government (Chen, Su, and Zhao 2000; Piotroski and Wong 2012). This practice creates conflicts of interest between the managers who are politically connected and the auditors located in that same local region. Given the lack of independence of external auditors in China and that China's weak institutional environment generally results in lower-quality audits by the Big 4 auditors (Ke, Lennox, and Xin 2015), it is questionable whether investors would find the risk disclosures supplied by auditors credible enough or provide incremental information for decision-making.

authors develop a model to evaluate the costs and benefits of disclosing information about audit quality. They argue that when the underlying financial reporting quality is low, the investor uses the audit report primarily for its insurance value, which, in turn, enhances the auditor's incentives to exert effort, because higher effort increases audit quality in expectation. To the extent that the additional risk disclosures are informative about audit quality and induces audit quality, this can enhance the decision-usefulness of financial reports for the investor.

Based on the above opposing arguments, we formulate our hypothesis in the null form:

H1: Holding other factors constant, the risk disclosures in the expanded audit report is not incrementally informative.

III. RESEARCH DESIGN

Pre-post Adoption and Difference-in-Differences model (DD)

As highlighted earlier, A+H share firms (i.e. firms that are listed on both the Mainland China and Hong Kong stock exchanges) are required to issue the expanded audit report after 1 Jan 2017 (i.e., fiscal years 2016 and after), and all other A share firms (i.e., firms that are only listed on the Mainland China stock exchange) are only required to do so after 1 Jan 2018 (i.e., fiscal years 2017 and after).[4] We exploit this staggered adoption of the expanded audit report in China to examine the informativeness of the report, using alternative research designs (see Figure 1).

First, we employ a pre-post design and focus on the full sample (i.e., using firm-year observations from fiscal years 2014 to 2018) to examine the adoption effect of the expanded audit report. This design allows us to examine whether our variables of interests (e.g., market reaction, trading volume, etc.,) change from pre- to post-adoption of the expanded audit report for both A+H share and A share firms. Accordingly, we specify an indicator variable *POST* that equals to 1 for A+H share firms in fiscal years 2016, 2017 and 2018, and equals to 1 for A share firms in fiscal years 2017 and 2018, and 0 otherwise.

[4] In China, all listed firms have fiscal year ending 31 December and are required to issue their annual reports before 30 April of the following year.

Second, we employ two separate DD models to mitigate the effect of time-related trends contemporary with the expanded audit report, including economic, political, and other factors, by focusing on the first-year adoption effect. Our first sample "D1" focuses on firm-year observations from fiscal years 2014 to 2016, whereby we use the A+H share firms as the treatment group and the other A share firms as the control group. Accordingly, we code an indicator variable *TREAT* that equals to 1 for A+H share firms, and 0 for A share firms. We also redefine the indicator variable *POST* to equal to 1 for fiscal year 2016, and 0 for fiscal years 2014 and 2015. Our second sample "D2" uses firm-year observations from fiscal years 2016 and 2017 only, and the A share firms become the treatment group while the A+H share firms becomes the control group. Accordingly, we redefine the indicator variable *TREAT* to equal to 1 for A share firms, and 0 for A+H share firms; the indicator variable *POST* equals to 1 for fiscal year 2017, and 0 for fiscal year 2016.

Market Reaction Tests

Following Gutierrez et al. (2018), we employ two main proxies for investors' reaction to the expanded audit report: (1) the three-day cumulative absolute abnormal returns in the period surrounding the date on which the annual report, containing the audit report, is publicly distributed (i.e., the report filing date)[5] and (2) the sum of three-day abnormal trading volume around the report filing date. Absolute abnormal returns reflect the average change in investors' belief due to an announcement event and trading volume is the "most visible indicator of investors' response to public disclosures" (Miller 2010). Greater usefulness of the expanded audit report will be reflected in positive price reactions

[5] In China, the audit report is released together with the annual report, which includes the financial statement. In other words, investors obtain the audited financial information and audit report simultaneously.

and an increase in abnormal trading volume on the report filing date. We estimate the pre-post and DD models as follows:

$$ABCAR\ (AVOL) = \delta\ POST + (\beta ABCAR) + \beta_1 LnMV + \beta_2 LEV + \beta_3 MTB + \beta_4 INST + \beta_5 Analysts + \beta_6 \Delta EPS + \beta_7 ROA + \beta_8 MAO + \beta_9 SDRET + \beta_{10} BETA + Industry\ FE + Audit\ firm\ FE + \varepsilon \quad (1.1)$$

$$ABCAR\ (AVOL) = \beta TREAT + \delta_1 POST + \delta_2 TREAT*POST + (\beta ABCAR) + \beta_1 LnMV + \beta_2 LEV + \beta_3 MTB + \beta_4 INST + \beta_5 Analysts + \beta_6 \Delta EPS + \beta_7 ROA + \beta_8 MAO + \beta_9 SDRET + \beta_{10} BETA + Industry\ FE + Audit\ firm\ FE + \varepsilon \quad (1.2)$$

We calculate (1) *ABCAR* as the sum of the three-day absolute abnormal returns around the release date of the audit report, with abnormal return of each day calculated as the company returns = (Price $Close_t$ – Price $Close_{t-1}$)/Price $Close_{t-1}$ minus the same-day returns for the whole A share value-weighted portfolio, and (2) *AVOL* as the firm's average event-period volume minus same-day A share average trading volume (scaled by outstanding shares).

We control for firm characteristics such as market value of firm (*LnMV*), leverage (*LEV*), market-to-book (*MTB*), the level of institutional holdings (*INST*), the number of analysts following the firm (*Analysts*), firm performance (*ΔEPS* and *ROA*), the presence of modified auditor opinion (*MAO*), and firm risk using the standard deviation of stock return (*SDRET*) and firm beta (*BETA*). When the dependent variable is *AVOL*, we further include *ABCAR*, which is an important factor related to trading behaviour (Bamber, Barron, and Stevens, 2011). We include industry and audit firm fixed effects in all the above models to account for unobserved heterogeneity across industries and audit

firms.[6] We estimate all models using OLS and obtain t-statistics based on standard errors clustered by firm and the announcement date of report.[7]

Earnings Response Coefficient (ERC) Tests

According to Fischer and Verrecchia (2000), the information content of the earnings report should increase as investors' perceived information credibility increases. Hence, to the extent that the risk disclosures in the expanded audit report enhance investor perceptions of the financial reporting quality, we expect a larger stock price reaction to unexpected earnings after issuance of the expanded audit report. Hence, we test the following two regression models:

$$CAR=\chi UE + \delta UE*POST + \gamma_1 POST + \gamma_2 LnMV + \gamma_3 MTB + \gamma_4 LEV + \gamma_5 CFO + \gamma_6 SDSales + \gamma_7 Analysts + \gamma_8 Loss + \varphi_1 UE*LnMV + \varphi_2 UE*MTB + \varphi_3 UE*LEV + \varphi_4 UE*CFO + \varphi_5 UE*SDSales + \varphi_6 UE*Analysts + \varphi_7 UE*Loss + Industry\ FE + Audit\ firm\ FE + \varepsilon \quad (2.1)$$

$$CAR=\chi UE + \delta UE*POST*TREAT + \gamma_1 POST + \gamma_2 TREAT + \gamma_3 POST*TREAT + \gamma_4\ LnMV + \gamma_5 MTB + \gamma_6 LEV + \gamma_7 CFO + \gamma_8 SDSales + \gamma_9 Analysts + \gamma_{10} Loss + \varphi_1 UE*POST + \varphi_2 UE*TREAT + \varphi_3 UE*LnMV + \varphi_4 UE*MTB + \varphi_5 UE*LEV + \varphi_6 UE*CFO + \varphi_7 UE*SDSales + \varphi_8 UE*Analysts + \varphi_9 UE*Loss + Industry\ FE + Audit\ firm\ FE + \varepsilon \quad (2.2)$$

The dependent variable is *CAR*, which is the cumulative abnormal return as described before but without taking the absolute value. *UE*, which is the unexpected earnings (or earning surprise), is calculated as the change of earnings per share over the year, deflated by prior year's ending stock price. Following Reid et al. (2019), we control

[6] Our results are qualitatively similar when we include firm fixed effects. Following Gutierrez et al. (2018), we also calculate standard errors using the bootstrap method with 1,000 replications, given that the theoretical distribution of the test statistic is unknown and the sample sizes are small. Results are qualitatively similar.

[7] We cluster by announcement date because Chinese listed companies are likely to issue annual reports from the middle to end of April (the due date is April 30) and hence their market reactions could be correlated.

for firm-specific variables that have been shown to be associated with ERC, namely the market value of the firm (*LnMV*), market-to-book (*MTB*), leverage (*LEV*), net operating cashflow (*CFO*), sales volatility (*SDSales*), the number of analysts following the firm (*Analysts*), and a loss indicator (*Loss*).[8] We further control for the interaction of *UE* and the control variables. As before, industry and audit firm fixed effects are included in the above models.

Stock Price Synchronicity Tests

If there is a limited supply of firm-specific information to the market, the firm-level stock return is expected to be highly correlated with the market return and there would be high price synchronicity (Roll 1988). Jin and Myers (2006) find that Chinese firms displayed the highest level of stock return synchronicity out of the 40 countries included in their study, which suggests the limited supply of firm-specific information among Chinese firms. To the extent that the risk disclosures in the expanded audit report better direct investors' attention to key financial reporting areas and identify areas that deserve more attention (PCAOB 2017), we expect the risk disclosures to facilitate the flow of firm-specific information into the market, thus motivating investors to rely more (less) on firm-specific (common) information in their trading decisions.[9] Consequently, stock price

[8] We follow previous studies and calculate unexpected earnings using last years' earnings as benchmark in our main tests (e.g., Guan, Su, Wu and Yang, 2016). We obtain qualitatively similar results using analysts' forecasts as benchmark.

[9] The PCAOB believes that the information provided in critical audit matters would be used by various types of investors in a number of different ways such as "informing" and "framing". Framing" refers to the notion that critical audit matters would provide investors with a new perspective on the financial statements and focus their attention on the related financial statement accounts and disclosures, which should facilitate their analysis of the financial statements, for example by highlighting potentially relevant information or by reducing the costs to process or search for the information. Consistent with this "framing" view, Sirois, Bédard, and Bera (2018) find that KAMs have attention directing impact, in that participants access KAMs-related disclosures more rapidly and pay relatively more attention to them when KAMs are communicated in the auditor's report.

synchronicity should decrease after adoption of the expanded audit report. Our regression specifications are as follows:

$$SYNC = \delta POST + \beta_1 TOPHOLD + \beta_2 TOPHOLD2 + \beta_3 QFII + \beta_4 BSHARE + \beta_5 SOE + \beta_6 SIZE + \beta_7 MTB + \beta_8 LEV + \beta_9 VOL + \beta_{10} ROA + Industry\ FE + Audit\ firm\ FE + \varepsilon \quad (3.1)$$

$$SYNC = \beta TREAT + \delta TREAT*POST + \beta_1 TOPHOLD + \beta_2 TOPHOLD2 + \beta_3 QFII + \beta_4 BSHARE + \beta_5 SOE + \beta_6 SIZE + \beta_7 MTB + \beta_8 LEV + \beta_9 VOL + \beta_{10} ROA + Industry\ FE + Audit\ firm\ FE + \varepsilon \quad (3.2)$$

We calculate stock price synchronicity (*SYNC*) by estimating the R^2 (i.e., the goodness of fit) of the stock return regression as in Gul, Kim, and Qiu (2010), whereby the estimation window is the 30 business days after the release of the audit report.[10] We then obtain $SYNC = Ln\ (R^2 / (1 - R^2))$.[11] Following Gul et al. (2010), we control for factors that are associated with stock price synchronicity. We include the percentage of top one shareholder (*TOPHOLD*) and its square (*TOPHOLD2*) to capture the inverted U relation between stock price synchronicity and the ownership concentration. Further, we control for foreign holding using the percentage of qualified foreign investor holding (*QFII*) and the issue of A+B share (*BSHARE*).[12] We also include state-owned enterprise (*SOE*) which is found to be positively related to stock price synchronicity. Other control variables

[10] We run the regression $R_{it} = \beta_0 + \beta_1 R_{mt} + \beta_2 R_{mt-1} + \beta_3 R_{indt} + \beta_4 R_{indt-1} + \varepsilon_{it}$, where R_{it} is the daily stock return for a given firm, R_{mt} is the daily stock return for the entire A share market, and R_{indt} is the daily average stock return for a given industry.

[11] Since R^2 value is bounded between 0 and 1 and the regression cannot be estimated using OLS (Wooldridge 2011), we use *SYNC* as the dependent variable.

[12] A+B share firms are firms that are not only listed on the China mainland stock exchange, but are also listed for trading to primarily international investors in U.S. Dollars as in the Shanghai exchange, or Hong Kong Dollars as in the Shenzhen exchange.

include the firm size measured by total assets (*SIZE*), market-to-book (*MTB*), leverage (*LEV*), average stock turnover (*VOL*), and *ROA*.

Sample Selection

We obtain accounting and market data from CSMAR and WIND database. Panel A of Table 1 presents our sample selection procedure. We began by considering all A share firms (15,679 observations) in China from fiscal years 2014 to 2018. We retain firms that are publicly traded before 2014 to make sure that firms have complete audited financial information. After deleting non-financial firms and firms with missing required variables, we have 7,325 firm-year observations, including 300 observations for A+H share firms (60 unique firms) and 7,025 observations for A share firms (1,405 unique firms).

As discussed earlier, D1 sample is used to examine the effect of the expanded audit report requirements for A+H share firms only, which are the early adopters. The sample period for this test is from fiscal years 2014 to 2016. Table 1 Panel A shows a total of 4,395 firm-year observations, including 180 observations for A+H share firms and 4,215 observations for A share firms. Next, D2 sample is used to examine the effect of the expanded audit report requirements for A share firms only, that is, the late adopters. The sample period for this test spans from fiscal years 2016 to 2017. Panel A shows a total of 2,930 firm-year observations, which consists of 120 observations for A+H share firms and 2,810 observations for A share firms. Tabl1 1 Panel B, which presents the sample distribution by industry, indicates that our sample firms are mostly concentrated in the manufacturing sector.

Descriptive Statistics

Table 2 presents the tests of overall differences in mean for all variables used in the market reaction, ERCs and stock price synchronicity tests for our full sample (i.e., A+H and A share firms combined). All continuous variables are winsorized at the 1st percent and 99th percent level. We first provide the differences in the means in abnormal returns (*ABCAR*) and abnormal trading volume (*AVOL*) between pre-adoption period and post-adoption period. The table shows that abnormal trading volume (*AVOL*) increases from pre-adoption to post-adoption period, but there is no significant change in abnormal returns (*ABCAR*) over the same period. This result provides some preliminary evidence that market reacts more to the audit report, in terms of abnormal trading volume, after the new audit reporting requirement. In untabulated analyses of the D1 and D2 sample, we find that *ABCAR* are not significantly different between the treatment group and control group. However, we find that the treatment group (A+H and A share firms for D1 and D2, respectively) experiences significantly greater increases in abnormal trading volume (*AVOL*) from the pre- to the post-adoption periods relative to the control group.

As discussed earlier, if the new risk disclosures in the expanded audit report facilitate the flow of firm-specific information into the market, and thus motivate outside investors to rely more on firm-specific information in their trading decisions, stock price synchronicity should decrease after the adoption of the expanded audit report. Table 2 shows that stock price synchronicity (*SYNC*) decreases from pre-adoption to post-adoption period. Moreover, in untabulated analyses of the D1 and D2 samples, we find that while all firms experience decreases in stock price synchronicity (*SYNC*) after the

adoption of the expanded audit report, the magnitude of decrease is significantly greater for the treatment firms than for the control firms. Taken together, these results provide some evidence that the expanded audit report provides more firm-specific information to investors.

For the control variables used in our main regressions, we find that leverage, institutional ownership, analysts following, changes in EPS, systematic risk, and sales volatility are significantly greater in the post-adoption period relative to the pre-adoption period. On the other hand, market capitalization, market-to-book ratio, ROA, stock return volatility, operating cash flows, percentage of top 1 shareholder, and average stock turnover are significantly lower in the post-adoption relative to the pre-adoption period. These differences indicate the importance of performing a multivariate regression analysis.

IV. EMPIRICAL RESULTS

Results of Market Reaction Tests

Panel A of Table 3 presents the regression results of our market reaction tests. Column (1) shows the results of estimating Model 1.1 using the full sample, and Columns (2) and (3) show the results of estimating Model 1.2 using D1 and D2 samples, respectively. The coefficients on *POST* (in Column 1), and on *TREAT*POST* (in Columns 2 and 3) are positive but not statistically significant at the conventional levels. In terms of control variables, market reaction to the expanded audit report is smaller for larger firms and firms with higher beta, but is larger for firms with higher analyst following, more profitable firms, firms with higher stock returns volatility, and firms with modified audit opinions. Hence,

H1 is not supported using market reaction as proxy for the informativeness of the audit report.

Panel B of Table 3 presents the results of estimating Models 1.1 and 1.2 for the abnormal trading volume tests. The panel reveals that the coefficients on *POST* (in Column 1) and *TREAT*POST* (in Columns 2 and 3) are all positive and statistically significant ($p<0.05$), suggesting that abnormal trading volume of both the A+H and A share firms is greater after the adoption of the expanded audit reports. These results provide support for our contention in H1 that the expanded audit report contains new information that is useful to investors. With regards to control variables, we find that larger absolute CAR, smaller firm size, higher leverage, lower institutional holding, larger change in EPS, higher stock returns volatility, and lower beta are associated with higher abnormal trading volume.

Results of ERC Tests

Table 4 presents the regression results of estimating Models 2.1 and 2.2 for our ERC tests. We find that the coefficients on *UE*POST* (Column 1), and *UE*TREAT*POST* (Columns 2 and 3) are all positive and statistically significant ($p<0.10$), indicating that the market reacts more strongly to earnings surprise after the adoption of the expanded audit report for both the A+H and A share firms. Hence, these results are consistent with the expanded audit report enhancing investors' perceptions of financial reporting quality, providing more support for H1 on the informativeness of the expanded audit report. With regard to the control variables, we find that firms with higher market-to-book ratio firms have higher ERCs.

Results of Stock Price Synchronicity

Table 5 reports the results of estimating models 3.1 and 3.2. In Column (1), the coefficient on *POST* is significantly negative ($p<0.10$), suggesting that stock price synchronicity decreases after adoption of the expanded audit report. Columns (2) and (3) reveal that the coefficients on *TREAT*POST* are both significantly negative ($p<0.10$), suggesting that the decreases in stock price synchronicity for both A+H and A share firms after they first adopt the expanded audit report are greater than that of the control firms. Taken together, these results are consistent with the additional risk disclosures in the expanded audit report facilitaing the flow of firm-level specific information to capital market, thus enabling investors to focus on more firm-level information for decision-making. This finding provides further support for H1 on the informativeness of the expanded audit report.

Robustness checks

Alternative measures of CAR, AVOL, ERC and SYNC

We perform a number of robustness tests. For brevity, we only present the results of the variables of interests in Table 6. First, we measure cumulative abnormal returns using other alternative measures, such as signed cumulative abnormal returns (*CAR*), five-days absolute cumulative abnormal returns ($ABCAR_{[-2,\ 2]}$) and firm-specific adjusted cumulative abnormal returns ($ABCAR_{adj}$). Panel A shows that there are still no significant differences in the market reaction to the expanded audit report between the pre- and post-adoption period. Next, we measure abnormal trading volume by five-days abnormal trading volume ($AVOL_{[-2,\ 2]}$) and firm-specific abnormal trading volume adjusted by either

the mean ($AVOL_{adj}$) or median value ($AVOL_{adj\_median}$) of trading volume over the estimation window. Panel B shows that abnormal trading volume based on the revised measures continue to be significantly greater in the post-adoption relative to the pre-adoption period. Panel C presents the results for the ERC analysis. We first validate our results using analysts' forecast as earnings benchmark to measure unexpected earnings (Column 1), using robust regression instead of OLS (Column 2) and adding the non-linearity of unexpected earnings to the regression to address the concern about extreme value of unexpected earnings (Column 3) (Gipper, Leuz and Maffett 2019). Panel C shows that the coefficients on $UE_{alternative}$*$POST$ continue to be significantly positive across all specifications. Finally, Panel D presents the results of our stock price synchronicity tests. We measure $SYNC$ using its original R^2 as dependent variable instead of the transformed value as we have done previously (Column 1). We also consider a longer period of 90 days following the release of annual report in measuring $SYNC$ (Column 2) and R^2 (Column 3). We continue to find that stock price synchronicity is significantly smaller in post-adoption relative to the pre-adoption period. Interestingly, the larger coefficients on $POST$ compared to those in Table 5 suggest that the firm-specific information contained in the expanded audit report may continue to be useful to investors beyond 30 days after the release of the annual report. Finally, in untabulated analyses, we find that our earlier results in Tables 3 to 5 using the D1 and D2 samples are also robust to the above alternative measures of abnormal trading volume, ERC, and stock price synchronicity, thus further supporting our hypothesis that the expanded audit report is informative to investors in the China setting.

Entropy balancing and propensity score matching

Commented [无名2]: We applied entropy and PSM method to D1, D2 tests and results hold. As discussed before, we can add a note to mention this issue.

One limitation of our earlier analyses is that the number and/or characteristics of the treatment firms are different from that of the control firms. Entropy balancing is a quasi-matching approach that re-weights each control observation so that post-weighting distributional properties of matched variables between the treatment and control observations are virtually identical, thereby ensuring covariate balance (Hainmueller, 2012; McMullin and Schonberger, 2020). Hence, we examine the robustness of our results using entropy balancing technique.[13] In Panel E1 of Table 6, we first show covariate balance after pre-adoption observations are reweighted to achieve the covariant balance (the first moment adjustment) via entropy balancing. Panel E2 of Table 6 then reports the results of the effects of expanded audit report on trading volume (*AVOL*), earnings response coefficient (*ERC*) and price synchronicity test (*SYNC*), respectively, using the new sample. The panel shows that the coefficients on *POST* (Columns 1 and 3) and *POST*UE* (Column 2) remain statistically significant ($p<0.10$) with signs consistent with our earlier results in Tables 3 to 5.

To further strengthen the robustness of our results, we next use a propensity score matching technique (PSM) for our pre-post analysis to examine the adoption effect of the expanded audit report.[14] Panel F1 of Table 6 confirms that the matching variables are not significantly different between the treatment and control groups. Panel F2 reports the results of replicating Tables 3 to 5 using the PSM sample. We continue to find significant

[13] Unlike standard matching procedures, entropy balancing preserves the size of the control sample, which is important in studies with significant imbalance between the size of treatment and control samples (Chapman, Miller, and White 2019; Shroff, Verdi, and Yost 2017; Ferri, Zheng, and Zou 2018).

[14] Because the number of A+H share firms are much greater than that of A share firms, we use a logit regression to estimate the probability of being an A+H share firms. The variables we include in the logit regression are shown in Panel F1. We then create a matched sample using the 1:5 nearest neighbor matching technique without replacement and a caliper set at 0.03 following Shipman, Swanquist and Whited (2017).

coefficients on *POST* (Columns 1 and 3) and *POST*UE* (Column 2). In sum, our results are robust to using both entropy balancing and PSM techniques.

Parallel Trends Assumption

One identifying assumption for the consistency of the difference-in-differences estimator is the parallel trends assumption: in the absence of treatment (i.e., the adoption of the expanded audit report), the treatment and control firms should experience parallel trends in the outcome variable (i.e., *AVOL*, *ERC* and *SYNC*). While the assumption is not directly testable (since the trend in those outcomes absent the 2016 or 2017 rules is not observable), we examine the trends prior to the event of interest similar to other studies using a difference-in-differences design (e.g. Dyreng, Hoopes, and Wilde 2016). To do so, we re-run the regressions in Tables 3 to 5, except that we include two indicators to capture *FY2015* and *FY2016* instead of *POST* (we still interact these indicators with the relevant variables, similar to the indicator *POST*). This test aims to assess the extent of differences in the variables of interest between the treatment and control groups in the years prior to the adoption of the expanded audit report. If the parallel trends assumption is not violated, we expect the coefficients on *TREAT*FY2015* for the abnormal trading volume or stock price synchronicity test, and that on *UE*TREAT*FY2015* for the ERC test, to be insignificant. Panel G of Table 6 reports these results that confirm that the parallel trend assumptions are supported. In addition, we conduct some placebo tests to confirm that our results are indeed due to the new regime by (1) using randomly-selected listed companies as the treatment group, and (2) using A+B instead of A+H share firms as the

"earlier adopter" treatment group (i.e. D1 sample test).[15] All our earlier results in Tables 3 to 5 disappear (untabulated), confirming that our findings are not driven by spurious factors.

V. ADDITIONAL ANALYSES

Cross-sectional Analysis - Demand of the Audit Report

In our main analyses, we find that the expanded audit report is incrementally informative to investors in terms of higher abnormal trading volume, higher ERC, and lower price synchronicity. In this section, we attempt to gain further insights by examining whether the informativeness of the expanded audit report varies according to the demand of the audit report. As discussed earlier, state-owned enterprises (SOEs) have lower demand for high quality audit than non-SOEs for control purposes (Piotroski and Wong 2012; Wang, Wong, and Xia 2008). Hence, we expect investors in non-SOEs firms to be more likely to rely on the expanded audit report and its accompanying additional risks disclosure information for decision making relative to their counterparts in SOEs. To test our assertion, we use an indicator variable *NSOE* that equals to 1 if the controlling shareholder is not state-owned, and 0 otherwise. In addition, we expect investors' demand for the risk disclosures information in the expanded audit report to be greater when there is higher information asymmetry in the firm (i.e., when the information environment is more opaque). Because smaller firms and firms with lower analyst following have poorer information environments (e.g., Lang and Lundholm 1993, 1996), we proxy for

[15] A+B firms are defined earlier in footnote 8. We examine A+B firms as one of the placebo tests because according to Ke et al. (2015), A+H and A+B share firms are similar in that they are both subject to dual accounting and auditing standards.

information asymmetry using (i) *MV_median*, which is an indicator variable that equals to 1 if the firm's market value is below the sample median, and 0 otherwise, and (2) *Analysts_median*, which is an indicator variable that equals to 1 if the number of analysts following the firm is below the sample median, and 0 otherwise. To examine the cross-sectional variation, we include *NSOE*, *MV_median*, and *Analysts_median*, together with their interactions with *POST* into our full sample models. Table 7 presents the regression results.

In Panel A, the coefficients on *POST*NSOE*, *POST*MV_median*, and *POST*Analysts_median* are all positive and statistically significant ($p<0.05$), suggesting that the increases in trading volume after the adoption of expanded audit report is larger for non-SOEs, smaller firms and firms with lower analyst following. In Panel B, we find that the coefficients on *POST*NSOE*UE and POST*Analysts_median*UE* are positive and statistically significant ($p<0.10$), while the coefficient on *POST*MV_median*UE* is positive but not significant at the conventionally level. These results suggest that the market reaction to unexpected earnings after the adoption of the expanded audit report is more pronounced for non-SOE firms and firms with lower analyst following. Finally, in Panel C, we find that the coefficients on *POST*NSOE* and *POST*MV_median* are negative and statistically significant ($p<0.10$), while the coefficient on *POST*Analysts_median* is negative but not significant at the conventional level. These results indicate that the decrease in stock price synchronicity after the adoption of the expanded audit report is more pronounced for non-SOE firms and smaller firms. Taken together, our results in this section provide some support that investors find the expanded audit report more informative when there is a greater demand for the expanded audit report.

Investor's Attention to Expanded Audit Report (Relative to Annual Report)

Audit reports are typically issued concurrently with annuals reports. In our earlier analyses, we attempt to isolate the effects of investors' reactions to the expanded audit reports by using difference-in-differences research designs (i.e., we compare A+H share firms with expanded audit reports to A share firms with old audit reports while the annual report format remains the same in the pre- and post-adoption periods). To afford stronger inference that the investors' reaction that we documented earlier are more likely attributable to the expanded audit reports rather than the annual reports, we examine the number of downloads of the audit reports relative to the number of downloads of the annual reports in both the pre- and post-adoption periods. The information "downloads" are obtained from the platform "JuChao" ("www.chinfo.com.cn"), in which all Chinese listed companies are required to timely disclose all their regulatory fillings or any announcements (i.e., annual report and audit report are separately disclosed). We define *RD* (i.e. relative downloads) as the number of downloads of auditor's report divided by the number of downloads of annual report for each listed company and replace *CAR* in Model 1.1 and 1.2 with *RD*.[16] Table 8 presents the regression results. We find that the coefficients on *POST* and *TREAT*POST* are all positive and statistically significant ($p<0.01$), suggesting that audit reports downloads relative to annual reports downloads significantly increase in the post-adoption periods relative to the pre-adoption periods. This finding provides some support that the increased trading volume and ERC, as well as the decreased

[16] We randomly select 200 firms from our full sample and calculate RD during the period 2014 to 2017. We find that these 200 firms have generally similar characteristics (e.g. *LnMV* and other control variables included in this table) as those in our main analyses.

stock price synchronicity, in the post-adoption periods are more likely due to the information content of the expanded audit report rather than the annual reports *per se*.

Informativeness of Modified Audit Opinions

Prior studies show that audit opinions are informative to investors (e.g., Chen, Su, and Zhao 2000; Ogneva and Subramanyam 2007; Kausar, Taffler, and Tan 2009; Menon and Williams 2010). Hence, if the expanded audit report is informative and useful to investors in evaluating financial reporting quality as we have earlier documented, we should expect the negative market reaction to modified audit opinions to be more pronounced in the post- relative to the pre-adoption periods as well. To test this hypothesis, we include *MAO*, an indicator variable that signifies if the audit opinion is modified (i.e., unqualified opinions with explanatory notes, qualified opinions, and disclaimers or adverse opinions) and its interaction with *POST* (i.e., *MAO*POST*) in Model 1.1 and present the regression results in Table 9. Column 1 shows that the coefficient on *MAO*POST* is significantly positive when *ABCAR* is the dependent variable, suggesting that the market reacts more strongly to modified audit opinions in the post-adoption periods. When we split *ABCAR* according to the direction of market reaction (Columns 2 and 3), we find that the issuance of modified audit opinions induces negative market reaction in the post-adoption period mainly in the sample of firms with negative CAR. This result suggests that when investors are perceiving modified audit opinions negatively, the additional risks disclosure information in the expanded audit report becomes more useful to investors in evaluating the implications of modified audit opinions; as a result, the negative market reaction to the modified audit opinions becomes stronger. Taken together, these results provide some

support for regulators' expectation that the expanded audit report enables investors to better understand the auditor's work.

Effect of New Audit Reporting Requirements on Audit Quality

Our earlier results suggest that the expanded audit report are informative to investors, which is consistent with regulators' expectation that the new audit report should improve transparency and usefulness of the auditor' work. In addition, increased oversight and investors' attention on the auditor's work may increase audit quality even though the new rule *per se* does not change specific rules on audit procedures. Hence, we examine whether the increased informativeness of the expanded audit report is at least partially due to an increase in audit quality.

Our first proxy for audit quality is the value of the performance-adjusted accrual (*DACC*) in Kothari, Leone, and Wasley (2005).[17] We regress *DACC* on *POST* and other controls that have shown to affect accruals in prior studies (e.g. Reid et al., 2019). Table 10 presents the results. We find that the coefficients on *POST* (Column 1) and *TREAT*POST* (Column 3) are significantly negative ($p<0.10$), while the coefficient of *TREAT*POST* (Column 2) is negative but not significant at the conventional level. These results provide some support that auditors curb discretionary accruals after the adoption of the expanded audit report.

[17] Following Guan et al. (2016), we decompose total accruals into normal and discretionary components: $TACC=a_0+a_1 1/TAST+a_2 \Delta Sales+a_3 PPE+a_4 ROA+\varepsilon$, where *TACC* is total accruals defined as the difference between operating income and operating cash flow; $\Delta Sales$ is growth in sales from year t-1 to year t; *PPE* represents the gross value of fixed assets; and *ROA* is the net income. All the above variables are deflated by the average of beginning and ending total assets, *TAST*. Following KLW, we also include a constant intercept term in our model.

Effect of New Audit Reporting Regime on Audit Fees

Although there is no ex ante expectation that audit fees will increase upon the enactment of new audit rule, our earlier results suggest that auditors may exert more effort to select the most important audit matters to explain to investors. In addition, the heightened exposure and scrutiny to audit work should lead to an increase in audit fees. Hence, we examine whether audit fees increase in the post-adoption periods. Our measure of audit fees, *LAF*, is the logarithm of total fees paid to the auditor for audit services in each year. Table 11 reports the regression results when we replace *CAR* in Model 1.1 and 1.2 with *LAF*, including other control variables that affect audit fees (e.g. Reid et al., 2019). Column 1 shows that the coefficient on *POST* is positive and significant ($p<0.01$), indicating that firms pay higher audit fees in the post-adoption periods relative to the pre-adoption periods, after controlling for such factors as size, profitability, and complexity. The coefficient on *TREAT*POST* is positive and significant in Column 3 ($p<0.05$) but not in Column 2. These results suggest that audit fees for A share firms increase after the initial adoption of the expanded audit report. Together with the results in the preceding section, this finding suggests that the informativeness of the expanded audit report could be in part due to an increase in the quality of the auditor's work.

VI. CONCLUSION

In this study, we examine the informativeness of the expanded audit report in the setting of an emerging economy. We hypothesize that the poor information environment and the prevalence of earnings management in China engender a greater demand for the risk disclosures information in the expanded audit report, and consequently, investors

would find the new report incrementally informative. Exploiting the staggered adoption of the expanded audit report in China and using both pre-post and difference-in-differences research designs, we find that abnormal trading volume and ERC increase, and stock price synchronicity decreases, in the post-adoption periods compared to the pre-adoption periods. These results are robust to various alterative measures of abnormal trading volume, ERC, and stock price synchronicity. They are also robust to using entropy balancing technique and PSM method. We also test the parallel trend assumption and find supportive evidence.

We conduct additional analyses to enrich our analyses. First, we examine whether investors would find the expanded audit report more informative in circumstances where there is a greater demand for the information in the audit report for decision making. We find that the expanded audit report is more informative for non-SOEs and for firms with higher information asymmetry. Second, we investigate and find that audit reports downloads relative to annual reports downloads significantly increase in the post-adoption periods. This finding provides further support that the capital market effects that we document earlier are more likely attributable to the information content of the expanded audit report rather than the annual reports. Third, we also find that the expanded audit report is more informative in terms of helping investors understand the implications of modified audit opinions. Finally, we document that the value of discretionary accruals decreases and audit fees increase in the post periods, suggesting that the increased informativeness of the expanded audit report is at least partially due to an increase in the quality of the auditor's work.

To the best of our knowledge, our study is the first to examine the informativeness of the auditor risk disclosures in an emerging economy. Our findings extend and complement existing studies such as Gutierrez et al., (2018) and Lennox et al. (2018) who generally find the lack of informativeness of the expanded audit report in a large and developed economy such as the U.K. Together, their studies and our study can help inform standard-setters and regulators around the world, especially those in developing economies, who would otherwise be skeptical about the usefulness of the risk disclosures in the expanded audit report. Our findings should also be useful to standard-setters in terms of issuing implementation guidance and conducting post-implementation review.

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Figure 1
Timeline of Research Design

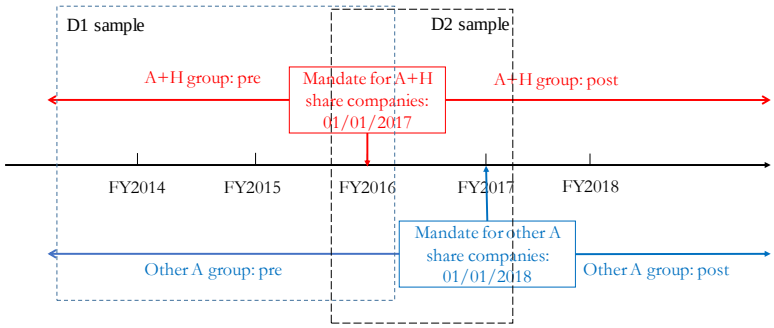

TABLE 1
Sample

Panel A Sample selection process

Sample selection criteria	Firm-years from FY2014 to 2018 (Full sample)	Firm-years from FY2014 to 2016 (D1 sample)	Firm-years from FY2016 to 2017 (D2 sample)
All listed companies in China A share	15,679	8,268	6,512
Retained: companies listed before 2014	12,200	7,320	4,880
Retained: non-financial companies	11,870	7,122	4,748
Retained: non-missing data to calculate stock return, trading volume, and stock price synchronicity around the release of the report.	10,661	6,234	4,284
Retained: all data exists for five years, i.e. a balanced panel sample.	7,325	4,395	2,930
Final sample	7,325	4,395	2,930
A+H share firms	300 (=60*5)	180 (=60*3)	120 (=60*2)
other A share firms	7,025 (=1405*5)	4,215 (=1405*3)	2,810 (=1405*2)

Panel B Sample distribution by industry

Industry classification by China regulator (CSRC)		Composition in final sample	Composition in initial sample
A	Agriculture, forestry, animal husbandry and fishery	1.57%	1.10%
B	Mining	3.07%	2.06%
C1	Manufacturing sector1	6.62%	6.05%
C2	Manufacturing sector2	18.43%	18.08%
C3	Manufacturing sector3	35.43%	36.74%
C4	Manufacturing sector4	1.37%	1.97%
D	Electricity, heat, gas and water production and supply	4.30%	2.91%
E	Construction	2.73%	2.54%
F	Wholesale and retail trade	5.60%	4.42%
G	Transportation, warehousing and postal services	4.16%	2.76%
H	Accommodation and Catering	0.34%	0.24%
I	Software and Information Technology Services	6.14%	7.83%
J	Financials	N/A	2.89%
K	Real estate	4.85%	3.35%
L	Leasing and business services	1.23%	1.44%
M	Scientific research and technical services	0.68%	1.54%
N	Water conservancy and public facilities management	1.16%	1.37%
O	Residential services, repairs and other services	N/A	0.03%
P	Education	0.27%	0.21%
Q	Health and social work	0.27%	0.32%
R	Culture, sports and entertainment	1.16%	1.58%
S	Others	0.61%	0.58%
		100%	100%

TABLE 2
Descriptive Statistics Comparing Pre-adoption vs. Post-adoption periods

	Post adoption period (2990 obs.)		Pre-adoption period (4335 obs.)			
	(1)	(2)	(3)	(4)	(1)-(3)	
Variables	Mean	Median	Mean	Median	Mean diff.	
Market Reaction Analyses						
ABCAR	0.036	0.026	0.036	0.027	-0.001	
AVOL	0.006	-0.220	-0.096	-0.427	0.103	***
LnMV	22.78	22.59	22.95	22.83	-0.174	***
LEV	0.440	0.436	0.427	0.417	0.013	***
INST	0.446	0.463	0.433	0.451	0.013	**
Analysts	5.087	2.000	4.621	3.000	0.466	***
MTB	2.643	2.008	4.616	3.535	-1.974	***
ΔEPS	-0.318	0.027	-0.488	-0.104	0.170	**
ROA	0.040	0.035	0.043	0.036	-0.004	***
SDRET	0.359	0.343	0.524	0.476	-0.165	***
BETA	1.237	1.203	1.012	1.084	0.224	***
MAO	0.017	0.000	0.013	0.000	0.004	
Earnings Response Coefficient Analyses						
CAR	0.001	-0.004	0.001	-0.003	0.001	
UE	-0.001	0.000	-0.003	-0.001	0.002	***
CFO	0.045	0.044	0.050	0.048	-0.005	***
SDSales	0.171	0.038	0.089	0.022	0.083	***
Loss	0.079	0.000	0.069	0.000	0.010	*
Price Synchronicity Analyses						
SYNC	0.065	0.086	0.157	0.215	-0.092	***
TOPHOLD	0.337	0.318	0.351	0.333	-0.014	***
TOPHOLD2	0.134	0.101	0.145	0.111	-0.012	***
QFII	0.002	0.000	0.002	0.000	0.000	
SIZE	22.76	22.58	22.37	22.19	0.393	***
VOL	1.494	1.451	2.208	2.235	-0.714	***
SOE	0.457	0.000	0.444	0.000	0.014	
BSHARE	0.038	0.000	0.037	0.000	0.000	

Table 2 reports descriptive statistics of our variables of interests and control variables in pre-adoption vs. post-adoption period, and t-tests of the differences between the two groups. Variable definitions are detailed in the Appendix. Mean difference T-test are provided: ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 3
Market Reaction Analyses

Panel A Stock price reaction to the issuance of expanded audit report

	Pre-Post analyses	Difference-in-Differences analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*ABCAR*	*ABCAR*	*ABCAR*
TREAT		0.0023	0.0013
		(0.996)	(0.311)
POST	0.0022	-0.0074***	-0.0010
	(1.152)	(-3.718)	(-0.181)
*TREAT*POST*		0.0028	0.0063
		(0.642)	(1.216)
LnMV	-0.0053***	-0.0065***	-0.0013
	(-7.270)	(-7.756)	(-1.341)
LEV	0.0018	0.0022	0.0024
	(0.682)	(0.680)	(0.718)
INST	-0.0023	-0.0035	-0.0044
	(-1.185)	(-1.418)	(-1.507)
Analysts	0.0004***	0.0003**	0.0001
	(3.659)	(2.158)	(0.909)
MTB	0.0000	0.0001	0.0004**
	(0.315)	(0.966)	(2.322)
⊿EPS	-0.0001	-0.0000	0.0000
	(-0.476)	(-0.206)	(0.280)
ROA	0.0069	0.0279*	0.0311*
	(0.483)	(1.953)	(1.742)
SDRET	0.0109***	-0.0041	0.0218***
	(2.658)	(-0.833)	(3.447)
BETA	-0.0084***	-0.0047***	-0.0039***
	(-6.974)	(-2.602)	(-2.869)
MAO	0.0094*	-0.0031	-0.0016
	(1.792)	(-0.659)	(-0.359)
Constant	0.1594***	0.1917***	0.0518**
	(9.308)	(9.701)	(2.261)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	4395	2930
R^2	0.041	0.068	0.044

Panel B Abnormal trading volume around the issuance of expanded audit report

	Pre-Post analyses	Difference-in-Differences analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*AVOL*	*AVOL*	*AVOL*
TREAT		-0.0402	0.0720
		(-0.595)	(0.906)
POST	**0.1543*** **	0.2274***	0.0657
	(3.350)	(4.603)	(1.051)
TREAT*POST		**0.2232****	**0.0463*****
		(2.597)	**(3.530)**
ABCAR	9.2692***	7.6771***	11.7177***
	(15.313)	(11.847)	(20.656)
LnMV	-0.1853***	-0.1662***	-0.1773***
	(-9.560)	(-6.062)	(-7.037)
LEV	0.3126***	0.2909***	0.1736*
	(3.523)	(2.735)	(1.658)
INST	-0.7055***	-0.7961***	-0.3064***
	(-8.969)	(-8.206)	(-3.480)
Analysts	0.0021	-0.0028	0.0065**
	(0.843)	(-0.775)	(2.486)
MTB	-0.0006	0.0044	-0.0048
	(-0.120)	(0.800)	(-1.029)
⊿EPS	0.0145***	0.0201***	0.0082
	(4.157)	(4.423)	(1.271)
ROA	-0.4870	-1.7668***	-0.3838
	(-1.310)	(-4.002)	(-0.849)
SDRET	1.0448***	0.5961***	0.8863***
	(9.499)	(4.488)	(3.959)
BETA	-0.1002***	-0.0757	-0.0679*
	(-3.307)	(-1.555)	(-1.826)
MAO	0.0796	0.1101	0.1070
	(0.612)	(0.720)	(0.615)
Constant	3.7279***	3.7120***	3.4080***
	(8.679)	(6.130)	(5.698)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	4395	2930
R^2	0.260	0.241	0.295

Table 3 reports the regression results of the analyses on the market reaction to expanded audit reports. The dependent variable is absolute cumulative abnormal returns (*ABCAR*) in Panel A, and abnormal trading volume (*AVOL*) in Panel B. In both panels, Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 4
Earnings Response Coefficient Analyses

	Pre-Post analyses	Difference-in-Difference analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*CAR*	*CAR*	*CAR*
UE	0.0000	-0.9369	0.3428
	(-1.186)	(-0.572)	(0.000)
POST	0.0012	-0.0038	-0.0044
	(0.447)	(-1.287)	(-1.015)
TREAT		-0.0034	0.0007
		(-0.785)	(0.161)
*UE*TREAT*		0.2311	-0.3151
		(1.228)	(-1.273)
UE*POST	**0.1878****	-0.0101	-0.3152
	(2.185)	(-0.115)	(-0.805)
*POST*TREAT*		0.0069	0.0108**
		(1.041)	(2.033)
UE*POST*TREAT		**0.0638***	**0.4759****
		(1.730)	**(2.215)**
LnMV	0.0027**	0.0032*	0.0023
	(2.062)	(1.865)	(1.274)
*LnMV*UE*	0.0590	0.0326	-0.0085
	(1.146)	(0.463)	(-0.111)
MTB	0.0004*	0.0002	-0.0001
	(1.795)	(0.861)	(-0.427)
*MTB*UE*	0.0294*	0.0384**	0.0454
	(1.821)	(1.982)	(1.564)
LEV	0.0003	0.0029	0.0020
	(0.069)	(0.642)	(0.386)
*LEV*UE*	-0.1053	0.0684	0.0343
	(-0.561)	(0.244)	(0.131)
CFO	0.0073	0.0090	0.0130
	(0.778)	(0.768)	(1.054)
*CFO*UE*	-0.4109	0.1506	-0.0688
	(-0.761)	(0.208)	(-0.081)
SDSales	-0.0042**	-0.0021	-0.0035
	(-2.327)	(-0.595)	(-1.092)
*SDSales*UE*	-0.0413	-0.0410	-0.0060
	(-0.422)	(-0.175)	(-0.050)
Analysts	0.0001	0.0000	0.0001
	(0.618)	(0.066)	(0.838)
*Analysts *UE*	0.0057	0.0070	0.0089
	(0.660)	(0.692)	(0.922)
Loss	-0.0056	0.0022	0.0022
	(-1.265)	(0.539)	(0.340)
*Loss*UE*	-0.1770	0.0461	-0.1333
	(-1.408)	(0.296)	(-0.565)
Constant	-0.0636**	-0.0737*	-0.0568
	(-2.081)	(-1.834)	(-1.352)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	4395	2930
R^2	0.017	0.022	0.031

Table 4 reports the regression results of the earnings response coefficients around the issuance of expanded audit reports. The dependent variable is cumulative abnormal returns (*CAR*). Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. T-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 5
Price Synchronicity Analyses

	Pre-Post analyses	Difference-in-Difference analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*SYNC*	*SYNC*	*SYNC*
TREAT		-0.0251	0.2550***
		(-0.274)	(2.625)
POST	**-0.0442***	-0.6374***	0.5523
	(-1.997)	(-15.041)	(1.171)
TREAT*POST		**-0.2460****	**-0.2747***
		(-2.018)	**(-1.896)**
TOPHOLD	0.0708	0.0159	0.5646
	(0.225)	(0.040)	(1.207)
TOPHOLD2	-0.3119	-0.2922	-0.9546
	(-0.778)	(-0.595)	(-1.537)
QFII	-3.9682***	-4.5868***	-5.4168***
	(-3.202)	(-3.513)	(-2.803)
SIZE	-0.0362**	-0.0432**	-0.0487**
	(-2.100)	(-2.131)	(-2.048)
MTB	-0.0309***	-0.0259***	-0.0411***
	(-6.291)	(-5.539)	(-5.992)
LEV	0.0517	-0.0196	-0.0117
	(0.639)	(-0.226)	(-0.101)
VOL	0.1276***	0.1195***	0.2332***
	(4.167)	(3.708)	(6.993)
ROA	0.1382	-0.4126	-1.0948**
	(0.502)	(-1.015)	(-2.357)
SOE	0.1134***	0.0938***	0.1004***
	(4.469)	(3.308)	(2.891)
BSHARE	-0.1009*	-0.1180**	-0.1088
	(-1.885)	(-1.996)	(-1.463)
Constant	0.7770**	1.2198***	0.2154
	(1.982)	(2.612)	(0.376)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	4395	2930
R^2	0.061	0.219	0.158

Table 5 reports the regression results of the stock price synchronicity around the issuance of expanded audit reports. The dependent variable is stock price synchronicity (*SYNC*). Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 6
Sensitivity Analyses

Panel A Alternative measures of cumulative abnormal returns

Dep. Var.=	(1) Full sample *Signed CAR*	(2) Full sample $ABCAR_{[-2,2]}$	(3) Full sample $ABCAR_{adj}$
POST	0.0006	0.0027	0.0022
	(0.208)	(1.288)	(1.210)
Controls	Yes	Yes	Yes
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	7325	7325
R^2	0.015	0.044	0.039

This panel reports the results of market reaction to expanded audit reports, using various alternative measures of cumulative abnormal returns. Column (1) is based on unsigned *CAR*. Column (2) is based on $ABCAR_{[-2, 2]}$, which is estimated in the five-day window surrounding the issuance of the expanded audit report. Column (3) is based on firm-specific adjusted cumulative abnormal returns. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel B Alternative measures of abnormal trading volume

Dep. Var.=	(1) Full sample $AVOL_{[-2, 2]}$	(2) Full sample $AVOL_{adj}$	(3) Full sample $AVOL_{adj\_median}$
POST	**0.1690*** **	**0.1783*** **	**0.1582*** **
	(3.164)	**(3.350)**	**(2.680)**
Controls	Yes	Yes	Yes
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	7325	7325
R^2	0.255	0.202	0.198

This panel reports the results of abnormal trading volume around the issuance expanded audit reports, using various alternative measures of abnormal trading volume. Column (1) is based on $AVOL_{[-2, 2]}$, which is estimated in the five-day window around the issuance of the expanded audit report. Column (2) is based on firm-specific adjusted $AVOL_{adj}$. Column (3) is based on $AVOL_{median\text{-}adj}$, which is similar to $AVOL_{adj}$ except that it uses median value, instead of mean value, of trading volume over the estimation window. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel C Alternative measures of ERC

Dep. Var.=	(1) Full sample *CAR*		(2) Full sample *CAR*	(3) Full sample *CAR*
$UE_{alternative}$	-7.5653**	*UE*	-0.9823	-1.4531
	(-2.167)		(-0.946)	(-1.228)
POST	0.0060**	*EAR*	0.0025**	0.0008
	(2.086)		(2.219)	(0.290)
$UE_{alternative}$*POST	**0.2131****	***UE*POST***	**0.2072*****	**0.4613*****
	(2.271)		**(3.209)**	**(2.994)**
		NLUE		-0.8954
				(-0.299)
		*NLUE*EAR*		-7.1216*
				(-1.882)

Controls	Yes	Yes	Yes
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	No	Yes
Obs.	4370	7325	7325
R^2	0.033	0.026	0.018

This panel reports results of the ERCs around the issuance of expanded audit reports, using alternative specifications to capture ERCs. Column (1) is based on $UE_{alternative}$, which uses prior-disclosure analysts' forecasts as earnings benchmark. Column (2) is based on *UE* but is estimated using robust regression. Column (3) is based on further controlling for *NLUE* (i.e. *UE* times absolute value of *UE*) and its interaction with *POST*. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel D Measurement issue related to price synchronicity

Dep. Var.=	(1) Full sample *Rsquare*	(2) Full sample $SYNC_{[0, 90]}$	(3) Full sample $Rsquare_{[0, 90]}$	(4) Full sample *SYNC*
POST	**-0.0117****	**-0.1672*****	**-0.0402*****	**-0.0402***
	(-2.212)	**(-2.600)**	**(-2.826)**	**(-1.852)**
AVOL				**-0.0315*****
				(-2.859)
Controls	Yes	Yes	Yes	Yes
Industry Effect	Yes	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes	Yes
Obs.	7325	7325	7325	7325
R^2	0.061	0.074	0.074	0.063

This panel reports the results of stock price synchronicity around the release of expanded audit reports, using various alternative measures of stock price synchronicity. Column (1) is based on *Rsquare*, i.e., raw R^2. Column (2) is based on $SYNC_{[0, 90]}$, which is estimated over 90 days following the issuance of expanded audit reports. Column (3) is based on $Rsquare_{[0, 90]}$, i.e. , raw R^2 relating to $SYNC_{[0, 90]}$. Column (4) is based on *SYNC* but further controlling for abnormal trading volume. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel E1 Covariate balance after Entropy Balancing

	Pre-adoption period	Post-adoption period	
Control Variables	Mean	Mean	Mean Diff
LnMV	22.78	22.78	0.000
LEV	0.440	0.440	0.000
INST	0.446	0.446	0.000
Analysts	5.087	5.087	0.000
MTB	2.643	2.643	0.000
⊿EPS	-0.318	-0.318	0.000
ROA	0.039	0.039	0.000
SDRET	0.359	0.359	0.000
BETA	1.237	1.237	0.000
MAO	0.017	0.017	0.000

Entropy balancing is a quasi-matching approach which re-weights each control observation so that post-weighting distributional properties of matched variables of treatment and control observations are virtually identical, thereby ensuring covariate balance (Hainmueller 2012; McMullin and Schonberger 2015). This panel reports the matched variables of treatment (i.e., pre-adoption period) and control (i.e., post-adoption period) observations to check for covariate balance.

Panel E2 Regression results using Entropy balancing

Dep. Var.=	(1) Trading volume test *AVOL*	(2) ERC test *CAR*	(3) Price synchronicity test *SYNC*
POST	**0.1658****	**-2.1746**	**-0.1426****
	(2.475)	**(-1.600)**	**(-2.212)**
UE		-0.0019	
		(-0.700)	
POST*UE		**0.1436***	
		(1.800)	
Controls	Yes	Yes	Yes
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Obs.	7325	7325	7325
R^2	0.225	0.128	0.151

Columns (1), (2), and (3) of this panel reports the entropy balancing results of the three main tests, using *AVOL*, *CAR* and *SYNC* as dependent variable, respectively. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel F1 Covariate balance after PSM

	Treatment group	Control group		
Control Variables	Mean	Mean	Mean Diff	P-value
LnMV	24.36	24.38	-0.018	0.814
LEV	0.563	0.568	-0.004	0.766
INST	0.677	0.663	0.014	0.354
Analysts	8.544	8.308	0.236	0.681
MTB	2.625	2.636	-0.011	0.963
ΔEPS	-0.461	-0.374	-0.087	0.771
ROA	0.039	0.041	-0.002	0.664
SDRET	0.398	0.391	0.007	0.620
BETA	1.060	1.079	-0.019	0.587
MAO	0.004	0.004	-0.001	0.893

This panel reports covariate balance after propensity score matching (PSM) procedure. We first use a logit regression to estimate the probability of being a treatment firm (i.e. A+H share firm). The variables we include in the logit regression are covariate shown in this panel. We then create the matched sample using the 1:5 nearest neighbor matching technique without replacement and a caliper set at 0.03 following Shipman, Swanquist and Whited (2017).

Panel F2 Regression results using PSM

Dep. Var.=	(1) Trading volume test *AVOL*	(2) ERC test *CAR*	(3) Price synchronicity test *SYNC*
POST	**0.2479****	0.9483	**-0.0864****
	(2.303)	(0.498)	**(-2.312)**
UE		0.0036	
		(1.384)	
POST*UE		**0.2707***	
		(1.666)	
Controls	Yes	Yes	Yes
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	1015	1015	1015
R^2	0.285	0.091	0.174

Columns (1), (2), and (3) of this panel reports the PSM results of the three main tests, using *AVOL*, *CAR* and *SYNC* as dependent variable, respectively. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

Panel G Testing parallel trends assumption

	(1) Trading volume test	(2) ERC test	(3) Price synchronicity test
Dep. Var.=	*AVOL*	*CAR*	*SYNC*
*FY2015*TREAT*	-0.0915	-0.0058	-0.1141
	(-1.047)	(-0.773)	(-0.701)
*FY2016*TREAT*	0.1930**	0.0005	-0.2513*
	(2.545)	(0.058)	(-1.819)
UE		-0.9652	
		(-0.517)	
*UE*FY2015*TREAT*		-0.7404	
		(-1.067)	
*UE*FY2016*TREAT*		0.2280*	
		(1.859)	
Controls	Yes	Yes	Yes
Fixed Effects	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	4395	4395	4395
R^2	0.253	0.023	0.233

This panel reports the regression results when we test for the parallel trends assumption. If the parallel trends assumption is supported, we expect the coefficient on *FY2015*TREAT* in Columns (1) or (3) or *UE*FY2015*TREAT* in Column (2) to be insignificant. Coefficients on industry and audit firm effects, interactions include *FY2015*UE (FY2016*UE)*, *TREAT*UE, TREAT, FY2015,* and *FY2016* are not tabulated for brevity. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 7
Informativeness of the Expanded Audit Report – Moderating Effects of Non-SOE versus SOE firms, Firm Size, and Analyst Following

Panel A Trading volume to issuance of report

Dep. Var.=	(1) Full sample *AVOL*	(2) Full sample *AVOL*	(3) Full sample *AVOL*
POST	0.1635**	0.1002**	0.0947**
	(2.039)	(2.408)	(2.275)
NSOE	-0.0137		
	(-0.622)		
POST*NSOE	**0.3178****		
	(2.193)		
MV_median		0.1598***	
		(4.082)	
POST* MV_median		**0.1096****	
		(2.322)	
Analysts_median			0.1036***
			(2.928)
POST* Analysts_median			**0.1125****
			(2.507)
Controls	Yes	Yes	Yes
Fixed Effects	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	7325	7325
R^2	0.249	0.265	0.264

Panel B ERC around the issuance of report

Dep. Var.=	(1) Full sample *CAR*	(3) Full sample *CAR*	(5) Full sample *CAR*
UE	-0.0443	0.4544	1.5472
	(-0.029)	(0.243)	(0.845)
POST	0.0036	0.0004	0.0034
	(1.541)	(0.149)	(1.189)
UE POST*	0.0714	0.1594	0.0784
	(0.693)	(1.486)	(0.702)
NSOE	0.0160		
	(0.346)		
*NSOE*UE*	-2.3455		
	(-1.085)		
*POST*NSOE*	-0.0039		
	(-1.412)		
POST*NSOE*UE	**0.2191***		
	(1.749)		
MV_median		-0.0664	
		(-0.907)	
*MV_median *UE*		-7.9862**	
		(-2.085)	
POST MV_median*		0.0025	
		(0.733)	

POST*MV_median *UE		**0.1392**	
		(1.574)	
Analysts_median			0.0045
			(0.094)
*Analysts_median*UE*			-6.2971**
			(-2.460)
*POST*Analysts_median*			-0.0033
			(-1.214)
POST* Analysts_median *UE			**0.1844***
			(1.717)
Controls	Yes	Yes	Yes
Fixed Effects	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	7325	7325
R^2	0.019	0.020	0.020

Panel C Price synchronicity following the issuance of report

Dep. Var.=	(1) Full sample *SYNC*	(2) Full sample *SYNC*	(3) Full sample *SYNC*
POST	-0.0108	-0.0181	-0.0526
	(-0.390)	(-0.290)	(-0.852)
NSOE	-0.0877***		
	(-3.346)		
POST*NSOE	**-0.0622***		
	(-1.847)		
MV_median		0.1008***	
		(3.053)	
POST* MV_median		**-0.0583****	
		(-2.352)	
Analysts_median			0.0547**
			(2.005)
POST* Analysts_median			**-0.0139**
			(-1.586)
Controls	Yes	Yes	Yes
Fixed Effects	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	7325	7325
R^2	0.062	0.063	0.062

This table reports the regression results of the moderating effects of Non-SOE versus SOE firms, Firm Size, and Analyst Following on the informativeness of the expanded audit report, captured by *AVOL* (Panel A), *CAR* (Panel B) and *SYNC* (Panel C). *NSOE* is an indicator variable that equals to 1 if the controlling shareholder is not state-owned, and 0 otherwise. *MV_median* is an indicator variable that equals to 1 if the firm's market value is below the sample median, and 0 otherwise. *Analysts_median* is an indicator that equals 1 if the number of analysts following the firm is below the sample median, and 0 otherwise. For brevity, we only present the results for our variables of interests. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 8
Investor's Attention to Audit Report Relative to Annual Report

	Pre-Post analyses	Difference-in-Difference analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*RD*	*RD*	*RD*
TREAT		0.0124	-0.0345*
		(0.793)	(-1.964)
POST	**0.0647*** **	0.0058	0.0318***
	(14.642)	(1.507)	(2.665)
TREAT*POST		**0.0225*** **	**0.0345*** **
		(3.400)	**(2.772)**
LnMV	-0.0055***	-0.0036	-0.0087**
	(-2.638)	(-1.449)	(-2.392)
LEV	-0.0055	-0.0149	-0.0023
	(-0.569)	(-1.327)	(-0.214)
INST	-0.0050	-0.0076	0.0058
	(-0.594)	(-0.854)	(0.547)
Analysts	-0.0003	-0.0001	-0.0003
	(-0.813)	(-0.165)	(-0.717)
MTB	0.0002	0.0004	-0.0006
	(0.389)	(0.700)	(-0.679)
⊿EPS	0.0000	-0.0001	-0.0006
	(0.077)	(-0.244)	(-0.803)
ROA	-0.0223	-0.0300	-0.0384
	(-0.591)	(-0.725)	(-0.740)
SDRET	0.0087	0.0027	0.0643***
	(0.927)	(0.246)	(2.785)
BETA	0.0024	0.0020	-0.0076
	(0.596)	(0.452)	(-1.156)
MAO	0.0298*	0.0124	0.0529**
	(1.889)	(1.142)	(2.242)
Constant	0.1949***	0.1576***	0.2929***
	(4.335)	(2.834)	(3.354)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	788	591	394
R^2	0.450	0.219	0.500

This table reports the regression results of investor's attention to audit report (relative to annual report) before and after the issuance of expanded audit reports. The dependent variable is relative downloads (*RD*), measured by the number of downloads of the audit reports relative to the number of downloads of the annual reports. Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 9
Informativeness of Modified Audit Opinions

Dep. Var. =	(1) Full sample *ABCAR*	(2) CAR>=0 sample *ABCAR*	(3) CAR<0 sample *ABCAR*
POST	0.0018	0.0028	0.0008
	(0.969)	(1.282)	(0.334)
MAO	-0.0030	0.0006	-0.0069
	(-0.666)	(0.084)	(-1.629)
POST*MAO	**0.0262*** **	**0.0272**	**0.0291*** **
	(2.944)	**(1.430)**	**(2.965)**
LnMV	-0.0054***	-0.0051***	-0.0057***
	(-7.375)	(-4.472)	(-6.655)
LEV	0.0023	0.0027	0.0018
	(0.852)	(0.571)	(0.600)
INST	-0.0023	-0.0011	-0.0034
	(-1.151)	(-0.347)	(-1.430)
Analysts	0.0004***	0.0003*	0.0005***
	(3.580)	(1.794)	(4.000)
MTB	0.0001	0.0002	-0.0000
	(0.556)	(0.632)	(-0.186)
ΔEPS	-0.0001	0.0001	-0.0001
	(-0.447)	(0.335)	(-0.755)
ROA	0.0086	0.0195	-0.0041
	(0.610)	(1.002)	(-0.252)
SDRET	0.0106***	0.0117**	0.0094*
	(2.634)	(2.060)	(1.926)
BETA	-0.0084***	-0.0076***	-0.0088***
	(-6.989)	(-4.382)	(-5.662)
Constant	0.1600***	0.1564***	0.1662***
	(9.403)	(5.993)	(8.153)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7325	3351	3974
R^2	0.043	0.040	0.073

This reports the regression results of the market reaction to modified audit opinions before and after the issuance of expanded audit reports. The dependent variable is absolute cumulative abnormal returns (*ABCAR*). Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 10
Effect of Expanded Audit Report Requirements on Audit Quality

	Pre-Post analyses	Difference-in-Difference analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*DACC*	*DACC*	*DACC*
TREAT		-0.0009	0.0046
		(-0.354)	(1.405)
POST	**-0.0018***	0.0017	-0.0004
	(-1.710)	(1.606)	(-0.100)
TREAT*POST		**-0.0003**	**-0.0084****
		(-0.121)	**(-2.260)**
SIZE	0.0020***	0.0006	0.0024***
	(3.697)	(1.014)	(2.869)
ROA	0.3050***	0.3144***	0.3472***
	(22.060)	(18.447)	(18.630)
Loss	0.0025*	0.0021	-0.0014
	(1.658)	(1.210)	(-0.465)
MTB	-0.0004***	-0.0002	-0.0005
	(-2.595)	(-0.963)	(-1.542)
LEV	0.0124***	0.0145***	0.0134***
	(4.199)	(4.041)	(3.026)
PRIOR_ACC	-0.0235***	-0.0255***	-0.0353***
	(-4.153)	(-3.720)	(-4.457)
CFO	-0.8842***	-0.8820***	-0.8803***
	(-119.180)	(-95.389)	(-77.302)
SDSales	-0.0033**	0.0001	-0.0064***
	(-1.996)	(0.034)	(-2.688)
Constant	-0.0197*	0.0064	-0.0342*
	(-1.745)	(0.479)	(-1.845)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7205	4381	2873
R^2	0.820	0.826	0.810

This table reports the regression results of the discretionary accruals before and after the issuance of expanded audit reports. The dependent variable is discretionary accruals (*DACC*), measured as Kothari et al. (2005). Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

TABLE 11
Effect of Expanded Audit Report Requirements on Audit Fees

	Pre-Post analyses	Difference-in-Difference analyses	
	(1) Full sample	(2) D1 sample	(3) D2 sample
Dep. Var. =	*LAF*	*LAF*	*LAF*
TREAT		0.5454***	-0.5910***
		(7.149)	(-6.991)
POST	**0.0932*** **	0.0333***	-0.1106*
	(8.164)	(4.243)	(-1.842)
TREAT*POST		**0.0002**	**0.1612** **
		(0.003)	**(2.537)**
SIZE	0.4059***	0.3901***	0.3858***
	(30.306)	(28.040)	(27.093)
ROA	-1.1314***	-0.9104***	-0.7251**
	(-5.458)	(-3.904)	(-2.397)
Loss	0.0125	0.0273	0.0475
	(0.488)	(0.980)	(1.212)
MTB	0.0157***	0.0141***	0.0136***
	(5.497)	(5.195)	(3.487)
CFO	-0.0245	-0.0087	0.0208
	(-0.383)	(-0.135)	(0.305)
SDSales	0.2736***	0.2990***	0.2467*
	(2.836)	(2.846)	(1.760)
INV	0.1868***	0.2322***	0.1413***
	(5.942)	(4.566)	(3.963)
REC	-0.0930	-0.0572	-0.0992
	(-1.030)	(-0.660)	(-0.933)
Constant	4.6896***	4.9948***	5.7035***
	(16.081)	(16.518)	(17.092)
Industry Effect	Yes	Yes	Yes
Audit firm Effect	Yes	Yes	Yes
Two-way Cluster	Yes	Yes	Yes
Obs.	7305	4382	2923
R^2	0.712	0.734	0.717

This table reports the regression results of audit fees before and after the issuance of expanded audit reports. The dependent variable is audit fees (*LAF*), measured as the natural log value of total audit fees. Columns (1), (2), and (3) are based on the full sample, D1 sample (i.e., A+H share firms as treatment firms), and D2 sample (i.e., A share firms as treatment firms), respectively. All t-statistics are computed using the standard errors adjusted for firm and annual report's announcement date clustering, and are based on two-tailed tests. ***, **, and * denote significance at the 1%, 5%, and 10% levels, respectively.

APPENDIX
Variable Definitions

Variables	Definitions
ABCAR, CAR	Absolute cumulative abnormal return is the absolute value of cumulative abnormal return (*CAR*). *CAR* is calculated as follow: $\sum_t^T (R_{it} - R_{mt})$, where R_{it} is daily stock return adjusted by cash dividends, R_{mt} is the daily market return weighted by firms' value. The event window *T* is the three-days [-1, 1] around the release of the audit report.
$ABCAR_{[-2, 2]}$	5-days absolute cumulative abnormal return, which is estimated as *ABCAR* except that the event window *T* is five-days [-2, 2] around the release of the audit report.
$ABCAR_{adj}$	Firm-specific adjusted absolute cumulative abnormal return is the absolute value of firm-specific adjusted cumulative abnormal return, which is calculated as follow: (1) we first estimate the correlation coefficients between R_{it} (i.e. individual stock return) and R_{mt} (i.e. market stock return) during non-disclosure window, i.e., [-60, -11] prior to the release of the audit report, using the regression specification $\mathrm{R}_{it} = \alpha_0 + \alpha_1 \mathrm{R}_{mt}$, (2) we then obtain expected $R_{it'}$ by calculating $\overline{\alpha_0} + \overline{\alpha_1} \mathrm{R}_{mt'}$, over the event window [-1, 1] around the release of the audit report. (3) *CAR* is sum of abnormal return that $\mathrm{R}_{it'} - (\overline{\alpha_0} + \overline{\alpha_1} \mathrm{R}_{mt'})$ over [-1, 1] three days.
Analysts	The number of analysts following the firm.
Analysts_median	An indicator that equals 1 if the number of analysts following the firm is below the sample median, and 0 otherwise.
AVOL	Abnormal trading volume calculated as follows: $\frac{1}{T}\sum_t^T (\frac{VOL_{it}}{OS_{it}} - \frac{MVOL_t}{MOS_t})$, where VOL_{it} is firm i's trading volume at day t, OS_{it} is firm i's outstanding share at day t; $MVOL_t$ represents markets' trading volume at day t, and MOS_t represents markets' outstanding share at day t. Event window *T* is the three-days window [-1, 1] around the release of the audit report. We standardize this variable.
$AVOL_{[-2, 2]}$	5-days abnormal trading volume, which is estimated as *AVOL* except that the event window *T* is five-days [-2, 2] around the release of the audit report.
$AVOL_{adj}$	Firm-specific adjusted abnormal trading volume calculated as follows: $\mathrm{Ln}\left(\frac{1/T_1 \sum_{t_1}^{T_1} VOL_{it1}}{1/T_2 \sum_{t_2}^{T_2} VOL_{it2}}\right)$, where VOL_{it} is firm i's trading volume at day t, and the event window T_1 is the three-days window [-1, 1] around the release of the audit report and the non-disclosure window T_2 is the 50-days window [-60, -11] prior to the release of the audit report.
$AVOL_{adj\_median}$	Firm-specific median-adjusted abnormal trading volume calculated as follows: $\mathrm{Ln}\left(\frac{1/T_1 \sum_{t_1}^{T_1} VOL_{it1}}{median\ value\ over\ T2\ of\ VOL_{it2}}\right)$, where VOL_{it} is firm i's trading volume at day t, and the event window T_1 is the three-days window [-1, 1] around the release of the audit report and the non-disclosure window T_2 is the 50-days window [-60, -11] prior to the release of the audit report.
BETA	The slope coefficient of the regression of weekly stock returns on equal-weighted market returns.
BSHARE	Indicator variable that equals to 1 if the A share firm also issues B shares (i.e. A+B share firms), and 0 otherwise.
CFO	The net operating cash flow divided by total asset.
⊿EPS	The change in basic earnings per share over the year.

DACC	Discretionary accruals estimated using the methodology in Kothari et al. (2005).
INV	Inventory intensity measured by total inventory divided by total assets.
INST	The percentage of institutional holding shares, that is, institutional holding shares divided by total outstanding shares.
LAF	The natural log of audit fees.
LEV	Leverage ratio, computed as total liabilities divided by total assets at the end of the year.
LnMV	The natural logarithm of year-end market value.
Loss	Indicator variable that equals to 1 if net income is zero or negative, and 0 otherwise.
MAO	Indicator variable that equals to 1 if the audit opinion is modified (i.e., unqualified opinions with explanatory notes, qualified opinions, and disclaimers or adverse opinions), and 0 otherwise.
MTB	Year-end market value divided by net equity value.
MV_median	An indicator variable that equals to 1 if the firm's market value is below the sample median, and 0 otherwise.
NSOE	Indicator variable that equals to 1 if the controlling shareholder is not state-owned, and 0 otherwise.
POST	For full sample, this indicator variable signifies the post-adoption periods of the expanded audit report. That is, it equals to 1 for A+H share firms in FY2016, FY2017, FY2018, or for other A share firms in FY2017, FY2018, and 0 otherwise. For D1 sample, this equals to 1 for FY2016, and 0 for FY2014 and FY2015. For D2 sample, this equals to 1 for FY2017, and 0 for FY2016.
PRIOR_ACC	Total current accruals for the prior year (measured as net income before extraordinary items plus depreciation and amortization less operating cash flows) scaled by total assets at the end of the prior year.
QFII	The percentage of qualified foreign investor holding.
REC	Accounts receivable intensity measured by total accounts receivable divided by total assets.
RD	The number of downloads of the auditor report divided by the number of downloads of annual report for each listed firm. The information "downloads" is obtained from the platform "JuChao" ("www.chinfo.com.cn").
ROA	Net income divided by total assets.
SDRET	Stock volatility, measured by the standard deviation of weekly stock returns over the year.
SDSales	Standard deviation of annual sales measured over the prior three years.
SIZE	The natural logarithm of total assets.
SYNC, Rsquare	Stock price synchronicity is the log transformation i.e. $\ln\left(R^2/1-R^2\right)$ of the goodness of regression fit R^2 (*Rsquare*) about stock return co-movement. We capture it using regression specification: $R_{it} = \beta_0 + \beta_1 R_{mt} + \beta_2 R_{mt-1} + \beta_3 R_{indt} + \beta_4 R_{indt-1} + \varepsilon_{it}$, where R_{it}, R_{mt}, and R_{indt}, represent (average) stock return for firm *i*, overall market, and its industry at day *t*. Estimation window is 30 days following the release of the audit report.
$SYNC_{[0,90]}$, $Rsquare_{[0,90]}$	90-days stock price synchronicity, which is estimated as *SYNC (Rsquare)* except that the estimation window is 90-days [0, 90] following the release of the audit report.
TOPHOLD	The percentage of shares held by top one shareholders.
TOPHOLD2	The square of *TOPHOLD*.
TREAT	In our "D1" sample, TREAT is an indicator variable that equals to 1 for A+H share firms, and 0 for A share firms. In our "D2" sample, TREAT is

	an indicator variable that equals to 1 for A share firms, and 0 for A+H share firms.
UE	Unexpected earnings is calculated as the change of earnings per share over the year, deflated by t-1 years' ending stock price.
$UE_{alternative}$	Alternative measure of unexpected earnings, calculated as current earnings per share minus the median value of analysts' forecasts prior to the release of the audit report, which is no earlier than 12 months its release, then deflated by ending stock price in year t-1.
NLUE	The nonlinear part of unexpected earnings, i.e., *UE* times absolute value of *UE*.
VOL	The natural log of firms' average stock turnover measured as the trading shares divided by total outstanding shares over the fiscal year.