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Audit Quality: Analysis Auditor and Auditee's Factor in Signaling Theory Perspective

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Abstract

The purpose of this research is to examine the effect of the other services, audit tenure and audit firms size toward audit quality, and client firm size as control variable. The variables above mentioned were retested because there's a research gap on the prior researchs. Mostly the researchs about quality audit only investigate auditor's view, meanwhile this research also investigate from auditee's view because two of three audit risk come from auditee. The samples of this research are 101 accountants in many profession around Jakarta which selected by purposive sampling. Multiple regressions is used in this research. The results shown that other services do not have an effect toward audit quality, audit tenure do not have an effect toward audit quality, the audit firms size do not have an effect toward audit quality and the client firm size have an effect toward audit quality.

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Keywords: Other services, audit tenure, audit firms size, client firm size, audit quality.

I. INTRODUCTION

Different interpretations to different people (Wooten, 2003), hot topic in the United States and elsewhere (Oliverio, 2007) and a decrease in audit quality due to conflict of interest (Krisnan and Gul, 2009; Francis, 2004) makes the quality of audit topics that are worthy to be studied.

Conflicts of interest and ambivalence triggered by increased bargaining power due to the intensity of the auditee the relationship between auditor-auditee which further resulted in the erosion of auditor independence, decreased partner criticality assessment (Carrey and Simnett, 2006) and economic hardship factor auditor / economic bonding (Hoitash *et al.* (2007). This shows that the auditee factor in determining the quality of these two audit. In line with the audit risk inherent risks and control risks originating from internal / auditee.

Unlike most related research audit quality, this study considers the auditee as a control variable. In addition to research different Al-Thunabait *et.al* (2011). In this study, the addition of variable other services based research Wooten (2003) and the difference in location of the sample / respondents in Jakarta, Indonesia. The difference in the location becomes important in research quality audit as differences between countries in terms of the legal system and

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legislation in force in the country (Francis, 2004), and geographic location (Choi *et al.*, 2007; Choi *et al.*, 2010) could affect audit quality.

II. LITERATURE REVIEW

Effect of Other Services Toward Audit Quality

Elstein (2001) which states that the consultation fee (other services) A large negative impact on auditor independence and audit quality decrease (Wooten, 2003). This occurs because of a conflict of interest and ambivalence and prejudice that audit quality has declined (Krisnan and Gul, 2009) and anxiety the SEC as stated Kinney (2004) and DeFond (2002) which requires disclosing the information and non-audit fees restrictions on the provision of audit and non-audit services (Watkins *et al.*, 2004). Anxiety showed that in the context of signal theory, providing other services outside of the audit (other services) be a negative signal for stakeholders.

However, additional service providing access auditor to gain a better understanding of the client and the business process (Wooten, 2003). Simunic (1984) argued that as a audit firm can provide non-audit services to audit clients, there may be a knowledge / information to be leaking, creating and efficiencies for the audit (Watkins *et al.*, 2004).

Based on the statement above, where there are groups who claim there is a negative influence (Elstein, 2001) and a group that claimed there is a positive influence (Wooten, 2003; Simunic, 1984) other services the quality of the audit, the hypothesis raised is:

H1 : Other services positive effect toward audit quality

Effect of Audit Tenure Toward Audit Quality

Research Carey and Simnett (2006) discloses two main reasons supporting the negative relationship between the length of audit partner tenure with audit quality, namely: (1) erosion of auditor independence (2) decline in the assessment of partner criticality. Their results state that for the long-term observations found a lower propensity to issue opinions *going concern*. In the Indonesian context, long term audit partner has been addressed with the issuance of the Minister of Finance No. 17/PMK.01/2008 and Law No. 5 of 2011, which manages limitations on the provision of services by the auditor and the Firm. Determination PMK suggests that in the context of signal theory, long term assignments auditor / audit partner to be a negative signal for stakeholders.

Then the results of Al-Thunabait *et.al* (2011) showed that the length of the cooperative relationship between the client and the auditor will give a negative effect on the quality of the resulting audit. Audit quality will decrease as the length of the working relationship going longer and widespread. Bedard and Johnstone (2010) predicts that the relationship will be negative for two reasons. The first reason, a partner will manage the relationship with the client's involvement in a longer period of time into something that is more efficient. The second reason is the reduction in testing because of excessive confidence or reduced skepticism. The end result they claim that it is significant that such a rotation partner is very costly for the audit firm, and no significant advantages can be achieved, and will not be different for clients who have partnerships with a duration of more than five years versus partnerships with a shorter duration.

Later research from Taiwan by Chen (2008) found that the value of abnormal accruals decreases with the length of the relationship between the auditor partnership with the client's progress (it implies that earnings quality increases). The findings Bedard and Johnstone (2010) and Chen (2008) is different from the Carey and Simnett (2006). This is in line with the statement Geiger and Raghunandan (2002) which states that the number of audits failure exactly happened in the early years of the auditor-client relationship. So we need additional time for some auditors to be able to avoid failure of the audit. Based on the statement above, the hypothesis raised is:

H2 : Audit Tenure negative effect toward audit quality

Effect of Audit Firm Size Toward Audit Quality

The results DeAngelo (1981) states that when the auditor to get clients, audit quality can not be separated from the auditor firm size. Accordingly, the results of research Francis and Yu (2009) stated that the audit results a larger office produces a higher audit quality. Similarly, the results of the study Choi *et al.*, (2010) which states that the firm size is positively related to audit quality is proxied by unsigned abnormal accruals. The results showed that the size of the audit firm be a signal to investors and creditors stakeholders especially relevant given the quality auditor. The use of auditors big can give a positive signal and instead uses auditor non big give a negative signals to stakeholders.

Then the results of Al-Thunabait *et.al* (2011) shows that the size of audit firm will provide a significant impact on the correlation or relationship between the length of audit quality working relationship between the auditor to the client (tenure). However, the research Lawrence *et al.* (2011) found that the effect of the action of the Big 4 auditors are not significantly different from non-Big 4 auditors. This indicates that the size of the Firm did not effect to audit quality. Based on the statement above, the hypothesis raised is:

H3: Audit firm size effect toward audit quality

Effect of Client Firm Size Toward Audit Quality

Research Fernando *et al.* (2010) relate to the quality of the audit client size and cost of equity capital. In addition, research Chen *et al.* (2008) also attributed client importance to the quality of the audit. Overarching further related research audit quality, Al-Thunabait *et.al* (2011) have used firm size as a control variable in research. In the context of signal theory, the larger the size of the company's clients are able to pay the auditor with a good reputation and increasing bargaining power client to the auditor. Based on the statement above, the hypothesis raised is:

H4: Clint firm size effect toward audit quality

III. METHODOLOGY

Population and Sample

The population in this study is an accountant in various professions who are in Indonesia, while the sample in this study was the accountant in various professions located in Jakarta and surrounding areas which include auditor, the auditee, regulators, accountants and educators. This is because audit quality interpreted differently by many parties (Wooten, 2003). The election of auditors in different professions located in Jakarta and surrounding areas due to the largest population of audit firm (external auditor), internal audit, the accounting firm (auditee), regulator and educator accountants located in Jakarta and surrounding areas.

Sampling is done by purposive sampling with criteria: (1) Accountant in Indonesia, (2) Working in Jakarta and surrounding areas, (3) a minimum of 1 year experience in the field, (4) Available sampled.

Data Analysis Techniques

Multiple regression is used to describe the influence of other services, audit tenur, firm size and the size of the client company to audit quality by using primary data.

IV. FINDINGS AND DISCUSSION

Effect of Other Services toward Audit Quality

Based on the test results obtained hypothesis t value of -0.171. When compared with 1.9837 for the t table t count <table which means that Ho is accepted. This suggests that other services does not affect the quality of the audit. These results are in contrast to Elstein (2001) which states that the consultation fee (other services) a large negative effect on auditor independence and audit quality decrease (Wooten, 2003) and groups who claim there is a positive effect other services on audit quality (Frankel, 2002; Wooten, 2003; Simunic, 1984).

This means that the quality would be similar to the auditor (audit firm) which provide versus that do not provide other services. These results are dismissed fears the negative impact the provision of other services by the auditor (audit firm) and yet the need for regulation of the provision of other services outside audit. It shows also that auditor independence was not compromised because the working relationship outside audit. This result is evidence that the auditor (audit firm) began to be careful and take the lessons learned from audit failure cases in the past.

Effect of Audit Tenure toward Audit Quality

Based on the test results obtained hypothesis t value of 0.639. When compared with 1.9837 for the t table t count <table which means that Ho is accepted. This suggests that audit tenure has no effect on audit quality. These results are in line with Bedard and Johnstone (2010) which states that the quality will not be different for clients who have partnerships with duration of more than five years versus partnerships with shorter duration, but in contrast to Carey and Simnett (2006) and Al-Thuneibat *et al.*, (2011) which states there is a negative influence and Chen (2008) which states there is a positive influence.

This means that the quality will not be different for the assignment of auditors (audit firm) with a duration of longer versus shorter. These results are dismissed fears the negative impact of the length of the assignment of the auditor independence and decrease erosion criticality assessment audit partner. It shows also that auditor independence was not compromised because within it working relationship auditor-auditee.

Effect of Auditor Size toward Audit Quality

Based on the test results obtained hypothesis t value of 1.818. When compared with 1.9837 for the t table t count <table which means that Ho is accepted. This indicates that the size of the auditor (audit firm size) does not affect the quality of the audit. These results are consistent with Lawrance *et al.*, (2011) which states that the effect of the action of the Big 4 auditors are not significantly different from non-Big 4 auditors and the result is different from the DeAngelo (1981), Francis and Yu (2009), Choi *et al.*, (2010) and Al-Thuneibat *et al.*, (2011).

This means that there is no difference in the quality of audits provided by the auditor (audit firm) Big and Non-Big and auditee to reduce reliance on auditors (audit firm) Big who tend to set higher rates.

Effect of Client Firm Size toward Audit Quality

Based on the test results obtained hypothesis t value of 2.226. When compared with 1.9837 for the t table t count > table which means that Ho is rejected. This shows that the size of the client firm affect audit quality. This proves that there are factors other than the client's auditor (auditee) That affect the quality of the audit.

**Table t test
Coefficients^a**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
(Constant)	34,780	6,105		5,697	,000		
Otherseviles	-,055	,324	-,017	-,171	,865	,913	1,096
Audittenuur	,096	,149	,067	,639	,524	,859	1,165
Auditfirm	,419	,230	,188	1,818	,072	,871	1,149
clientfirm	,536	,241	,222	2,226	,028	,939	1,065

a. Dependent Variable: Auditqual

V. CONCLUSION AND RECOMMENDATIONS

Based on the above results it can be concluded:

1. Other Services does not affect toward audit quality. It shows also that auditor independence was not compromised because the working relationship outside audit.
2. Audit tenure does not affect toward audit quality. This means that the quality will not be different for the assignment of auditors (audit firm) with a duration of longer versus shorter and led to erosion of the independence and decrease the criticality assessment audit partner. It shows also that auditor independence was not compromised because within it working relationship auditor-auditee.
3. Audit firm size does not affect toward audit quality. This means that there is no difference in the quality of audits provided by the auditor (audit firm) Big and Non-Big and auditee to reduce reliance on auditors (audit firm) Big who tend to set higher rates.
4. Client firm size affects toward audit quality. This proves that there are factors other than auditor (client/auditee) that affect toward audit quality, in this study is represented by the variable size of the client company.

The research was conducted in Indonesia and the results of this study may differ and do not apply in other countries.

For policy makers (Regulator): (1) Not need to set policy on the provision of other services outside the audit because there is no effect on audit quality or in other words, although a negative impact on one side, but have a positive impact on the other; (2) Should be reexamined policy restrictions auditor duties, as both auditor and serve longer or shorter no difference in the quality of the audit. It can be caused due to the need for high-quality audits are not always due to legislation.

For Audit Services Users: Choose auditor at low cost. No influence auditor size (audit firm size) on audit quality, because they work with the same standards.

For Auditor: Independensi in order to be maintained, because the size of the client company proved to affect the quality of the audit. Non big auditor reliance on the client and the company's large-scale ability to affect independence auditor (Bounded Economy & Bounded Rasonality) the impact on audit outcomes.

For the future research. (1) Add moderating variable to overcome research gap; (2) Distributing questionnaires avoided the busy start of the year due to the auditor; (3) Use other theory perspective to research audit quality.

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