

CHAPTER I

INTRODUCTION

I.1 Background

A higher quality of audit is vital for the reliability of financial reports. It will safeguard the interest of all parties. Therefore, auditors as client partners should pay attention to the quality of their audits by maintaining their performance during the audit period. Moreover, a high-quality of external auditing is a central component of well-functioning capital market (Skinner et al, 2012).

Audit quality is a basic ingredient in enhancing the credibility of financial statements to users of accounting information. Consequently, Coate, Florence and Kral (2002) noted that audits add credibility to financial information by providing an independent verification of management-provided financial reports, thus reducing investor's risk. Financial reporting credibility is reflected in the confidence of users in audited financial reports. According to Levitt (2000), the perception of audit quality plays a critical role in maintaining systematic confidence in the integrity of financial reporting.

Bank management has a primary responsibility for the preparation and quality of financial statements and reports, valuations and risk disclosures and for the effectiveness of related internal controls. At the same time, sound audits provide a number of benefits to institutions, financial systems and supervisors. External audits performed in accordance with high-quality globally accepted audit and ethical standards are critical to the appropriate implementation of accounting standards. They help ensure that financial statements and reports are reliable, transparent and useful to the marketplace. This enhances market confidence and improves the quality of information relied on by banking supervisors. Sound audits may help to identify weaknesses in internal controls relating to financial reporting and risk management at banks and reinforce corrective measures, thus complementing supervisory efforts in contributing to safe and sound banking systems.

There are some factors which affects the quality of audit. Auditor's reputation has been one of the major considerations in clients' selection of audit firms (Copley & Douthett, 2002). This characteristic pushes the auditor's reputation in a spotlight when to acquiring new engagements (Kronenberger & Plietzsch, 2017). It includes several scopes namely, audit firm size, industry specialization and other value drivers, including audit technology, branding efforts and human resource management. However, studies on auditor's reputation are under-researched. Few studies that have examined auditor's reputation have mainly used auditor's size as a representation of auditor's reputation. For example, DeAngelo (1981) found that auditor size is associated with a higher number of client engagements and ergo a higher amount of audit rents, which incentivizes bigger auditors to work harder. Otley & Pierce (1996) stated that "the importance of an auditor's reputation stems from the fact that the quality of audit cannot readily be inspected; reputation therefore acts as a surrogate for quality".

Another factors that influence the quality of audit is audit tenure. It is the period of engagement between the auditor and client regarding audit services agreed upon as the period of the auditor's relationship with the client. The audit tenure becomes a polemic when the audit tenure is brief or the tenure is long-term. The tenure can have an impact on auditor performance on client companies such as independency (Pertiwi, Hasan and Hardi 2016). According to Nugroho (2018), the concept of audit tenure and audit quality can be interpreted if there has been a prior engagement between the auditor and his client, then the auditor will be easier to understand the presentation and recording made by the client so that it can help the audit process to improve audit quality. Research conducted by Puspitasari (2017), Lee and Sukartha (2017), and Ardani (2017) show that audit tenure affects audit quality because longer audit tenure can increase auditor competence.

Studies have also suggested that the diversity of audit committee as part of board of directors (BOD) may affect the audit quality. According to Abbassi (2019) female directors on audit committees are positively and significantly associated with

audit quality. Further, it evidences that female accounting experts on audit committees have a positive and significant association with audit quality, while female non accounting experts on audit committees are insignificantly associated with audit quality. Furthermore, the study supports policy-makers' efforts towards greater presence of female directors, however, it recommends that they should also consider the public accounting expertise of female directors. According to Nielsen & Huse (2010), women on the council create greater vitality and facilitate a more complete and comprehensive process. So, it can be seen from previous studies that showing gender diversity on the board can improve not only decision making but also the role of board oversight which has the main benefit of increasing the level of bank efficiency (Ramly et al., 2015).

Bohren & Strom (2010) found that relatively few studies linking gender diversity and company performance and the results are conflicting. Gul et al. (2011) stated that the addition of women to board would increase internal divisions, which could limit the council's ability to act. As a result the board becomes ineffective and does not produce significant abnormal returns for the company (Farrell & Hersch, 2005). Most empirical results show a positive relationship between gender diversity and company performance (Krishnan & Park, 2005; Nguyen & Nghiem, 2015). Recent studies have shown that gender diversity will improve performance in weak corporate governance arrangements because companies will benefit from woman directors who can provide additional monitoring of the board of directors (Adams & Ferreira, 2009; Gul et al., 2011).

Moreover, Indonesia, as one of the country that conducts patriarch community, where the male is more favored and dominated in all of sectors of business and government. This believes make the assumption in the society that women are not better doing their job if men are pretty good at handling it. Thus, there are several contradictions where women can also do a better job in the same sector as men do. This several factors considered for a woman to be one of the board directors in audit committee affect the audit quality.

The first factor is the regulations and encouragement to rise women awareness to participate as one of the board direction members. This proposition based on the assumption that female directors will do a better job in sensing risk, and monitoring. Female directors tend to follow the rule of ethical standards and more trustworthy as stated by Lai et al. (2017). Second, in Indonesia even though gender diversity role in board directors is implemented in a developed country, there will be concern regarding women role in a patriarch environment. Third, the effectiveness of female board directors in audit committee are usually restrained by families. In some other words, gender diversity in board directors of audit committee will result higher earnings (Oradi & Darjezi, 2019), that eventually will scale down conflicts between board directors, and Improve disclosure quality (Gul et al. 2011).

Research on the quality of audits in banking companies are important because it relates to a variety of stakeholders, such as governments, employees, investors, creditors, customers and other parties so that it is the underlying of this research. The latest case in banking world occurred at Bank Bukopin reported net profit of 1.08 trillion before it was known by the OJK so that eventually Bank Bukopin revised its net income to 183.56 billion. Bank Bukopin has chosen KAP partner of Purwantono, Suherman, and Surja. If we look at this KAP, many of them use the services on the audit process such as Bank Rakyat Indonesia, Bank Central Asia, Bank Negara Indonesia, Bank Tabungan Negara, Bank Maybank, and so forth. In addition, this KAP is affiliated with big four namely Ernst & Young. This situation is interesting to learn because there are many banks that become partners with KAP Purwantono, Sungkoro, and Surja in the latest year. In addition, banks that registered in IDX that do not perform audit rotation so that there is a suspicion to the quality of the audit.

The study regarding analysis of audit quality in Indonesian banking sector is quite an interesting topic mainly because the amount of research regarding audit quality of bank is still limited rather than the research about audit quality in manufacturing company, especially in Indonesia. Thus, researcher thought that this

study will gain more attention from other researcher who wants to study the similar topic of audit quality. Therefore, the researcher is interested in to research how well the audit quality of Indonesia banking sector and whether there are some effects that may influence the quality of audit regarding audit tenure, audit reputation and audit committee gender diversity.



I.2 Problem Statement

1. Is there any effect of audit tenure on audit quality?

When the auditor has a long term relationship with the bank for a certain years, the probability of declining quality of audit is quite high. This research will determine whether audit tenure could affect the quality or not. Thus the first problem is occurred based on this situation.

2. Is there any effect of auditor reputation on audit quality?

Auditor reputation will help to increase the probability of audit quality based on how good the public accountant firm who handles the audit. This research will shows whether auditor reputation has an effect on audit quality.

3. Is there any effect of audit committee gender diversity on audit quality?

Audit committee gender diversity can be one of consideration whether it can affect audit quality or not. This is mainly because the ratio of audit committee male and female is not balanced well in the company. This research will find out will audit committee gender diversity could affect audit quality or not.

I.3. Research Objectives

1. To test whether the audit tenure affects the audit quality.

This research will show the whether audit tenure can affect the audit quality after the processed data.

2. To test whether the auditor reputation affects the audit quality.

In this research will find out whether the auditor reputation may have an effect on audit quality.

3. To test whether the audit committee gender diversity affects the audit quality.

In this research will find out whether the audit committee gender diversity may have an effect on audit quality looking at the audit committee structure in the bank company.

I.4. Research Benefits

Based on the research objectives above, it is expected to have the following benefits:

a. For writers

The results of this study may be useful for writers specifically to increase understanding, knowledge and provide confidence in the analysis of the factors that influence audit quality. The writers may use the audit quality as one of factor to increase other variables if the audit quality is positively affected. If the variables are not positively affected the audit quality, the writers can find another variables to contribute as the factors for increasing the audit quality.

b. For management of company

For the company, audit quality can enhanced the internal control, company performance, and to maintain the trust from the investors and creditors. If the research variables has an affect or not to increase the audit quality, the research variables can be the fundamental for the company to create the regulation in order to maintain the investor, creditor, customer trust and other which involved in business of the company.

c. For government

This research can be another input of suggestion for the government to create the regulation regarding audit quality to establish the regulations that associated to increase the audit quality.

a. IAPI

IAPI (Institute of Indonesian Public Accountant) is one of the organization that helps to regulate the Indonesian accounting standard for all of ublic accountant in Indonesia. The findings of this study might help IAPI to create and consider new adjustment for the regulation of audit in Indonesia.

b. PPPK Ministry of Finance

PPPK Ministry of Finance of the Republic of Indonesia, namely the Financial Profession Development Center from the Ministry of Finance which is owned by Indonesia to carry out the coaching process for every profession related to finance. In this case, accountants are one of the professions that are subject to PPPK of the Indonesian Ministry of Finance so that their quality and presence in Indonesia are improved. This is in line with PPPK's duties, namely coordinating and carrying out the preparation of policy formulation, guidance, development and supervision and information services for the financial profession, namely Accountants, Public Accountants, Accounting Technicians, Appraisers, Public Appraisers, Actuaries, and other financial professions. PPPK is responsible to the Ministry of Finance of the Republic of Indonesia through the Secretary General, and PPPK is also related to professional associations of accountants in Indonesia such as IAPI.

Therefore, the findings of this study might help ministry of finance to create and consider new adjustment for the regulation of audit in Indonesia.

1.5 Systematics of Writing

The systematic writing in this research are:

CHAPTER I INTRODUCTION

This chapter explains the background of the research, the factors related to audit quality such as audit reputation, audit tenure, and audit committee gender diversity that are suspected to influence audit quality. This chapter also includes the formulation of the problem, research objectives, research benefits, and systematic writing.

CHAPTER II LITERATURE REVIEW

This chapter contains the theoretical foundation that supports this research as well previous studies and also contains about research framework and hypothesis.

CHAPTER III RESEARCH METHOD

This chapter contains the background of the problem, the formulation of the problem, the purpose research, research benefits and systematic writing.

CHAPTER IV RESEARCH RESULTS AND DISCUSSION

This chapter will discuss the description of the research object, data analysis, interpretation of results and arguments for the results obtained following the techniques used in variables of the research.

CHAPTER V CONCLUSION

This chapter contains conclusions from the results of research that has been done and suggestions that are expected to be useful for those who are interested in the results of the research.

