CHAPTER ONE

INTRODUCTION

1.1 Background

Management in public company must annually submit annual report on the closing date of the book, usually on December 31. The annual report is prepared in accordance with financial accounting standards. This report will be used by a current and potential investor or a creditor before making a decision. The company, therefore, needs an auditor from the public accounting firm (PAF) to audit the financial statements. The audit results have huge consequences and bring responsibilities which will trigger auditors to work professionally. One of the criteria of professionalism of the auditor is the timely delivery of financial statements to the general public. The timely delivery of financial statements is one of the key quality factors of financial reporting. This timeliness is related to the benefits of the financial statements themselves. If there is an undue delay in the financial statements, the resulting information will lose its relevance (Subeki and Widiyanti, 2004).

The time difference between the date of the financial statements and the date of the audit opinion in the financial statements indicates the length of time for completion of its audit. The important thing is how to make the presentation of the financial statements can be timely or not too late and the confidentiality of information to the financial statements is not leaked to other parties who are not competent to influence it.

Regulations on the delivery of financial reports have been regulated by Bapepam in Law no. 8 of 1995 concerning Capital Market. It is stating that public companies are required to submit periodic financial statements to Bapepam and announce the report to the public. On July 5, 2011, Badan Pengawas Pasar Modal dan Lembaga Keuangan issued Peraturan Nomor: X.K.2, Lampiran Keputusan Ketua Bapepam dan LK Nomor: Kep-346/BL/2011 concerning Submission of Periodic Issuer Financial Statement Or Public Company, stating that the annual financial report submitted to Bapepam and Financial Institutions and announced to the public no later than the end of the third month (90 days) after the date of the annual financial statements. The issuance of this regulation revokes Keputusan Ketua Bapepam and LK Nomor: KEP-36/PM/2003 regarding Obligation of Financial Statement Submission and Keputusan Ketua Bapepam and LK Nomor: Kep-40/BL/2007 on Period of Periodical Financial Reporting and Annual Report for Issuer or a Public Company with Securities Listed on Indonesia Stock Exchange and Stock Exchange in Other Countries. If the financial year closes on 31 December, the financial statements should be submitted no later than 30 March of the following year. Therefore, if the auditor of the relevant public accounting firm (PAF) submits annual report to Bapepam exceeding the time limit, more than 90 days, then it is called audit delay.

Several factors affecting audit delay have been studied by previous researchers, e.g. Countis (1976), Whittred (1980), Givoly (1982), Carslaw and Kaplan (1991), and Halim (2000). Several factors affecting audit delay have been studied in several previous studies, such as company size, total revenue, profitability level, length of client of PAF, and company book year. The direction of the relationship of these factors is a very strong positive correlation with audit delay.

Other factor affecting the duration of audit completion is mandatory audit rotation. Mandatory audit rotation is the government's effort to limit the cooperative engagement between the auditor or the public accounting firm with its client or a company's business so as to prevent the occurrence of overfamiliarity that interferes with the independence of the auditor. On the other side, voluntary change has a difference in the focus of attention and issues. Voluntary change focuses on client side. Voluntary change might occurs, among other things, due to a client dispute with the auditor or incompatibility between the auditor and the client, while the mandatory change occurs due to the limiting law between the client and the auditor (Widiastuty & Febrianto, 2010).

In Indonesia, the audit rotation regulations were first issued in 2002, i.e. in KMK No.423/KMK.06/2002 dated September 30, 2002. The regulation states that the provision of general audit services to the financial statements of an entity may be performed by the public accountant office as long as five consecutive years and by an individual public accountant for a maximum of three consecutive years. This regulation was then updated with KMK No.359/KMK.06/2003 and updated again with PMK No.17/PMK.01/2008. The PMK states that the provision of public audit services to the financial statements of an entity shall be conducted by the public accounting firm for the maximum of six consecutive years and by an individual public accountant for the maximum of three consecutive years.

Research, however, found that lengthy auditor tenure is associated with fewer audit reporting failures (Geiger & Raghunandan, 2002) and fewer restatements (Lazer et al., 2004; Myers et al., 2005). Because auditors have much more understanding of the circumstances clients and clients already feel fit with the performance of auditors. According to DeFond & Francis (2005), each time an auditor audits a new client, two costs arise: costs associated with studying the client's business and litigation costs. These two costs can be interconnected: if the auditor fails to understand the client's business (including business risks), there is the possibility that the client will cheat and the auditor can not discover the fraud if the fraud has a negative impact on the users of the financial statements, the auditor should bear the litigation fee on his opinion because the management financial statements should be viewed as joint reporting between the auditor and the client management (Kinney, 1999).

Dopuch et al. (2001) found evidence that the existence of a rotational obligation provides a lower auditor reporting bias compared to the absence of a rotational obligation. Johnson et al. (2002) found evidence that firms with shorter auditor engagements (2-3 years) exhibited higher levels of expected accruals than firms with medium auditor engagements (4-8 years). Meanwhile, for sample companies with long auditor engagements (> 9 years), they found no evidence that there was a statistically significant increase in expected accruals compared with sample firms with a medium auditor engagement. Myers et al. (2003) found that longer auditor engagement is associated with higher earnings quality. They measure the quality of earnings using absolute abnormal accruals and absolute present accruals. According to them, there is no evidence that mandatory turnover of auditors and accounting firms can improve the quality of financial statements. The evidence suggests that a short engagement is associated with higher audit fraud and the likelihood of fraud decreases as the audit engagement grows longer (Carcello& Nagy, 2004). However, it is not true that there is no research that proves that rotation will increase independence. Dopuch et al. (2001) above clearly proves that mandatory rotation actually makes auditor independence higher than if there is no auditor rotation rules or auditor retention at all.

Research on audit delay influenced by pseudo rotation has not been much in Indonesia. The phenomenon of pseudo rotation auditor in Indonesia has been quite a lot since Ministry of Finance issued KMK No.423/KMK.06/2002. Pseudo rotation indicates a condition that conceptually there has been a change of auditor mandatorily and auditor relationship with client disconnected, whereas substantively client relationship and auditor still continue. Some researchers like Siregar et al. (2011), Febrianto & Sugiri (2014), and Junaidi et al. (2014) provide evidence that the auditors actually "pretend" to make mandatory rotations. Noting article 3 paragraph 5 and 6 of PMK No. 17/2008, the new PAF that changes the composition of its public accountant so that 50% or more comes from the old PAF, then the new PAF is considered to be a continuation of the old PAF, whereas if, after the establishment of a new PAF or change of name of PAF, only 50% or more comes from the old PAF, then the new PAF is considered a continuation of the old PAF. One of these two modes is preferred by the local PAF in Indonesia compared to performing a client "daycare" for one year-while maintaining their foreign affiliated PAF. This mode is referred to by the three studies above as pseudo-mandatory rotation of the auditor.

In this study, I will measure the length of audit delay that occurs in companies that perform real-mandatory, pseudo-mandatory, and volutary rotation. Testing is on whether or not there is a difference audit delay in the company with the conditions previously mentioned.

1.2 Research Question

1. Does audit rotation affect the company's audit delay
2. Does the length of audit time is related to the type of audit rotation

1.3 Research Objectives

1. Academically to meet one of the requirements to achieve a bachelor's degree (S1) in Accounting Department Faculty of Economics Andalas University.
2. As empirical evidence for the academic world and regulators on the company's audit delay when it performs pseudo rotations. With that knowledge, academics can determine time lapsed if the company makes a pseudo rotation or other type of rotations.

1.4 Writing Systematic

In preparing this study, systematic discussion of the problem starts from the background of the problem to the conclusions and suggestions, then writing systematic is as follows.

BAB I: BACKGROUND

It is an opening chapter that describes the background of the problem, the formulation of the problem, the purpose of research, the benefits of research, and systematics of writing.

BAB II: LITERATURE REVIEW

This chapter discusses the theories that will be used as the basics for discussion of this writing which includes the theoretical base, framework of thinking, and formulation of hypotheses.

BAB III: RESEARCH METHODS

This chapter discusses the research methods used in the implementation of this study. Some of the things described in this chapter are the operational definitions of variables, population, and sample determination procedures, types and methods of data collection, as well as analytical techniques.

BAB IV: RESULTS AND DISCUSSION

In this chapter we discuss the description of the research object consisting of the description of the variables, data analysis, and interpretation of the results of the analysis based on the tools and analytical methods used in this study.

BAB V: CONCLUSION

This chapter discusses the conclusions about the results of research and also described the limitations of the study.