

Audit Quality in Indonesia

Sekar Mayangsari*

Universitas Trisakti

Jakarta, Indonesia

*sekar_mayangsari@trisakti.ac.id

Abstract—Indonesia has a continuous concern on its audit quality since the impact of global changes on the accounting profession. The data was obtained from interviews with practitioners which have given the notion on how far Indonesia has already gone to improve audit quality. We also review several documentaries which was obtained from on the official websites of government, especially in financial ministry. Institutional analysis was derived directly from data obtained. The findings showed that regulators roles have created significant efforts to develop any regulations of audit. In addition, it also shows the implementation of audit quality conducted by practitioners in their audit firm, even though there were still several fraud cases happen. This paper is a contribution to the literature on the subject of audit quality especially how Indonesia responded to the global demands on audit quality improvements and the expectation of the practitioners regarding to the changes.

Keywords—audit quality, Indonesia, regulation, qualitative, institutional

I. INTRODUCTION

The purpose of this study is to provide qualitative analysis on the practitioners' expectations and influence their practice in audit firms regarding the regulators' efforts in order to enhance audit quality in Indonesia. Adopting institutional theory will be the method of analysis to address the data obtained. Therefore, this study contributes to the literature by providing further insight into the contextual condition that prompts the regulatory efforts, which will enhance the understanding on the impact of these efforts and the improvements on audit quality in Indonesia. This study also provides contribution to the institutional theory by showing how institutions in Indonesia regulate auditing in its own legal structure. In addition, this paper will also provide the insights of the practitioners' expectations and influence of their practices on the regulatory efforts through in-depth interviews with the global and local practitioners. This approach will clearly illustrate a comprehensive phenomenon rather than relying on the secondary data. Thus, this paper is organized as follows: The first section is the introduction and the second section explains the context of institutional theory. The third section discusses the literature review, the fourth section justifies the research questions and methodology and lastly, the fifth section presents the result including the discussion on the implication of the research.

The aim of this paper is to investigate how the practitioners' expectations and practices are influenced by the regulators' efforts in order to enhance audit quality in Indonesia. Hence, as to fulfil the aim of the study, the research questions are addressed as follows: 1) How do the regulators efforts enhance audit quality? 2) how do the regulatory efforts influence practice in audit firms?; and 3) what are the practitioners' expectation towards the efforts?. In order to answer these questions, institutional analysis is used and it concerns institutional change. In order to identify the pattern of institutional change, a starting point need to be determined at which the change occurs as a result of specifying dimension of the institutions [1]. Therefore, the identifying pattern started from the year 2007 to 2016 and the regulators used coercive theoretical perspective dimensions. As mention above, coercive pressure comes from the regulators to the audit firms' environment which creates direct rules, and the practitioners must comply with or else they will be penalized. In short, the regulators used their power to force practitioners to engage in certain actions or activities.

II. LITERATURE REVIEW

The grand theory is Institutional theory is used to develop a theoretical framework that will help to understand the process of the regulatory changes that influence audit quality in Indonesia. The process by which organizations tend to adopt the same structures and practice is known as isomorphism or described as a homogenization of organizations [2]. The definition of isomorphism itself is a process that causes one unit in a population to resemble other units in the same population that share the same set of environmental condition [2]. Thus, in order to obtain legitimacy, access facility to resources and risk avoidance, conforming to institutional rules and norms should be confirmed [2,3]. Previous researchers have studied audit quality with various dimensions or factors that influence it either with consistent or different results [4]. They have identified and categorized audit quality in various views, whether direct or indirect measure of audit quality; studies that are based on sources of differentiation; studies that rely on input, process, output; behavioural perspectives; market based perspectives; organizational aspects and others [4]. Most of the studies relate audit quality to regulators and practitioners and is relevant as to what the International

Auditing and Assurance Standard Board (IAASB) refers as among the audit quality elements in their Framework of audit quality-Key Elements [5]. According to IAASB audit quality is the best achieved in an environment where there is support from, and appropriate interactions among the elements and participants in the financial reporting supply chain. The past decade has seen a lot of changes in the regulations of the auditing profession, including in Indonesia. The changes serve as a guide for practitioners to perform the best approach in regards to accomplish AQ. Practitioners are required to comply with the relevant auditing standards, ethics and regulatory requirements within their audit firms. As a result the practitioners sometimes faced challenges due to the regulatory changes [5,6].

Accounting practitioners and their services cannot be separated from the related regulations since the profession directly affects public interest [7-9]. New accounting regulation is inevitable as the necessity to change has taken place since the advent of the profession. The transpires within the profession. Regulations are also inseparable from government's intervention as well as the professional bodies, because regulations exist to protect the interests of the many, and serve as a response to the current events. The most popular regulatory changes were The Sarbanes-Oxley Act (SOX) of 2002 in the US [1]. Since then there were many researches that studied the impact of SOX and relate it to in a AQ whether in a direct or indirect relationship [6,7,10,11]. Based on the studies mentioned, it can be summarized that there are two different points of views, on whether regulatory changes influence the audit quality directly and significantly or otherwise, by using various dimensions. The methodological approaches used by prior literature also differs significantly with regards to population, sample, scope, adopted approach, and data analysis method which had led to differences in conclusions. Most of the discussions revolve around the impact of regulatory changes on audit quality. Additionally, most of these studies were conducted in developed countries.

Another study which was conducted in China had examined two rules issued by China's State-owned Assets Supervision and Administration Commission of the State Council (SASAC) whether the regulations that limit management influence over auditors improve audit quality [12]. It was found that limiting management influence over auditors does improve audit quality, in this case especially for state-owned enterprises that are ultimately controlled by the central government (CSOEs). Similar study regarding regulatory changes and audit quality in emerging country was also conducted in China [13]. They examined the legal and regulatory changes that affect the relationship between audit quality and the client's economic importance from 1995 to 2000 and 2001 to 2004. The results show significant differences and contradictory between the two periods of analysis. It can be summarized that the number of studies which focused on regulatory changes and audit quality in emerging countries is very limited. Most of the studies were conducted in China, and the main different among these studies was a diverse legal environment, in this case related to auditing profession. For example, the differences were in terms of statutory audit requirements, standards and

standards setting, the competence requirement of auditors, and reporting obligations. The difference may create differential of audit quality's atmosphere [9]. In the case of Indonesia, the empirical research on regulatory changes such as the regulators' effort and audit quality is low as well. Most of them were concerned with audit quality and similar dimensions such as: Auditor's Industry Specialization, Auditor's Procedures, audit's tenure [14], and auditors' competency, experience and independency [5]. In addition, most of the existing studies had utilized quantitative or experimental case approach to obtain data Hence, this study is designed to look into the views and expectations of the parties involved in auditing by conducting in-depth qualitative study, and to show the states' role, efforts and developments

III. METHODS

This study employs qualitative approach. Data was collected from face-to-face interviews, personal observations and secondary data sources. The institutional analyses were used to utilize it, to make sense of the data. The participants' selection for this study was practically and theoretically accomplished based on their experience. The participants are divided into two main groups which are; the regulators and professional bodies in one group; and the global practitioners and local practitioners in another group. For the purpose of this study, the definition of a global practitioner is a practitioner who works in an audit firm which has international professional service network. Each entered into an agreement with member firms in the network to share a common name, brand and quality standards. The total of participants selected were twenty-nine (29) participants of which eight (8) participants were regulators and the remaining twenty-one (21) were practitioners. The interviews duration varies from 38 to 100 minutes for every participant, and were conducted independently. The interviewer used key point's questions as the instrument. Additionally, in order to support the result of the interviews and strengthened the reliability of the conclusions, archival material such as annual reports and other confidential documents from the officers were reviewed as well.

IV. RESULTS AND DISCUSSION

Regulators play significant role in showing Indonesia's commitment to improve and enhance audit quality. The efforts are not only conducted at the country level, but also at the ASEAN regional level. One of the collaborative activities with other ASEAN countries was the ASEAN Audit Regulators Group (AARG) meeting and inspection workshop conducted in 2016 [9,15]. The workshop focused on information and knowledge sharing activities on guidance and supervision of Independent Audit Regulators and the Public Accounting Firm. In addition, it was a platform of collaboration and dialogue between ASEAN audit regulators, aiming at achieving consistent cooperation and increasing audit quality provided by Independent Audit Regulators and accounting firms [13]. The activity not only portrays the roles and efforts performed by the Indonesia, but also shows part of the collaborative efforts among ASEAN countries.

At the country level, the regulators focus on the enhancement of the statutory and institutional framework. It means that how the basis of effective regulations is put in place. The purpose of the rule to monitor and supervise the practitioners, and to improve the accounting and the auditing mechanism. These regulations are regarding the accountancy profession and expected to impact the audit quality. Instead of having enhancement to statutory and institutional framework, the regulators have restructured the audit supervisory board such as the Pusat Pembinaan Pofesi Keuangan (P2PK) and the Otoritas Jasa Keuangan (OJK). In addition, the regulators have decided to adopt international standards and given the task to the standard setters to move toward the convergence to these standards [16]. As stated, the current task is still being in progress which is the re-evaluation of the 2006 version of the ethics code to update it in line with the Handbook of The Code of Ethics for Professional Accountants 2016 Edition, issued by the IESBA, and Kode Etik Profesi Akuntan Publik by Institut of Indonesia Public Accountant [17]. Besides preparing the standards, the professional bodies have identified five main aspects of improvements as well as preparing the draft of Audit Quality Indicators (AQIs):

“(..) we have five major aspects of efforts in order to improve audit quality, namely: 1) improving individual quality and the competence of public accountant profession; 2) providing and improving the auditing standards (SPAP) and code of conduct referring to international standards; 3) encouraging to improve the capacity and quality of public accountant and audit firm’s services; 4) improving and strengthening the practice of good governance in within an organization; and 5) improving the involvement and legal advocacy regarding the relevant regulations for this profession (...).The most current progress that the professional bodies consistently support and significantly involve in enhancing AQ is the socialization of the IAPI’s Statutes and Bylaws’ Revision draft, in order to establish Public Interest Oversight, and the issuing of the exposure draft of Audit Quality Indicators (AQIs) from October to November 2016 (...).”

Most of the participants responded to the question about how the regulatory efforts influence their practice in audit firms. They claimed that the direct influence for them is the shift of their thinking, or which put them into applying the risk based thinking or “critical thinking” to some. Hence, 90% of the practitioners said that they need to prepare “a huge project or action plan” since they have lots of things to do; and one of the actions is to revise their internal audit manual to meet with the new auditing standards. Forty-eight percent of the global practitioners asserted that their manual book have high degree of compliance with the ISA, while the local claimed compliance with some significant differences and die to this they require more time to refine it. They said that their actions are not only focused on the auditing standards, but also fulfilling practice requirements, new enforcements approach, as mentioned on the new regulation for practitioners, and updating auditing standards as well, which until the last of 2016, the standard setter, including Indonesia standard setter [16], are still launching and updating these standards. Public accountant act consider that the practitioners have no choice except to comply, even

though the impact is hard and costly, especially for the small and medium audit firms, which are owned by the local practitioners. Most of the local practitioners have limited resources, and now they also have to be more careful in accepting assurance engagements due to the pressure of high quality output at lower fee. This section they claimed that there is a significant different between the global and local practitioners in reacting and responding to the changes. All agreed that the two parties may struggle to meet with the regulations as well as the new international standards based on the resources and capacity they owned.

The third question of this study explores whether different size of accounting firms reacted differently to the regulatory efforts in order to enhance audit quality in Indonesia. Although they reacted differently in response to the regulators’ efforts, but they shared the same opinion regarding their expectations. Most of them agreed that the regulatory efforts may offer the opportunity to engage with more clients, determine a minimum assurance fee and provide free or affordable professional training programs for the members, especially for the auditors not for the partners. They also expected that the new act and regulations will make auditing as a more desirable profession for the young accountants as the audit firms have higher possibility to earn higher turnover. These also will protect the profession legally and the finally, the practitioners expect that the regulatory efforts may help to decrease the gap among the practitioners i.e. the gap of having the resources and market share.

Hence, based on the explanations above, it finds that all of the participants also share a similar view about the expected benefit they can get by complying with the regulatory changes. This expectation can be divided into two categories, the first is monetary value added which is related to the quality of money. This refers to the value regarding the audit fee, or called as financial benefit, and the practitioners may possibly get more clients which will eventually increase their assurance revenue. The second is the non-monetary value added which include the awareness of being more professional as an accountant (improving the competency; good reputation; better attitude and mental; competitive). Besides that, the practitioners also expect that the regulatory efforts will protect the profession legally and decrease the gap among the global and local practitioners. In addition, the regulatory changes may improve the awareness of related the parties such as the clients, the stakeholders to be more confident with a business that employs qualified auditors. The practitioners also expect regulators to be consistent in promoting and realizing the enhancement of audit quality in Indonesia.

The empirical findings of audit quality in Indonesia show that the mean of compliance rate 63,04% [18]. Based on Data from Indonesia Finance Ministry, showed that some of auditors still reluctant to comply with the standards. Moreover, the items of input are the highest among others (41,38%), while the process’ factors are 30,77% [18]. Input’s factors including ethics, values, behaviour, competence and independence as well and process’ factors are quality control of audit firm, audit planning and documentation of audit evidence.

V. CONCLUSION

This study has investigated the practitioners' expectation qualitatively regarding the regulatory efforts to manage auditor and the compliance rate of auditors in Indonesia. Both of them are representative of audit quality measurement. Based on the analysis, it can be concluded that the regulators' efforts have created a significant impact on the practitioners in order to improve the audit quality. However, the practitioners react to the regulatory efforts differently. The global practitioners are always preparing to face the changes as they have strong connection with the professional international network services, while their local counterpart find it a challenge as they lack the necessary resources. However, the two group shares the same view that they may have to struggle to meet the regulations as well as the new international standards. In addition to that, all of them perceive similar views regarding the benefits that they may receive by having the regulatory changes, in the form of monetary and non- monetary value added. Finally, the practitioners expect that the regulators will keep on promoting and enhancing the practitioner's work quality in order to raise the confidence of the clients and other stakeholders. However, the finding of this study needs to be understood as the regulators efforts are still taking place since the year 2007. Therefore, the implementation of audit quality may show continues improvement and still requires the participations of all parties related to the accounting professions.

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