



## **Does Audit Quality Mediate the Effect of Auditor Tenure, Abnormal Audit Fee and Auditor's Reputation on Giving Going Concern Opinion?**

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### **ABSTRACT**

The increased fraud of financial statements shows the low role of external auditors in providing a quality audit report. The purpose of this paper is to analyze the effect of the length of the audit firm-client relationship, abnormal audit fees (ABFE) and auditor reputation on giving of going concern opinion mediated by audit quality. The sample consists of 185 firm years. Sample companies listed on the Indonesian stock exchange from 2012 to 2016. Data analysis techniques using structural equation modeling based partial least square. The result of the indirect effect test shows that auditor tenure and auditor reputation have a positive effect on audit quality while ABFE has a negative effect to audit quality and audit quality has a negative effect on giving of going concern opinion. The results of this study also show that the company's financial condition does not moderate the effect of audit quality on giving going concern opinion.

**Keywords:** Audit Quality, Auditor Tenure, Abnormal Audit Fee, Auditor's Reputation, Going Concern Opinion

**JEL Classification:** M42

### **1. INTRODUCTION**

Responsibility for the reliability of any information presented in the financial statements is very important because the value of information contained in the financial statements associated with the purpose of making investment decisions to be taken. The information generated by the financial statements may mislead the users if the information presented is unreliable even though the information is relevant. The business world was thrown with the accounting scandal that happened to some big companies like Enron, Worldcom and Citigroup around 2001. Another case was experienced by Lehman Brothers who dragged the famous Public Accounting Firm (KAP) Ernst and Young, who was considered negligent in examining the financial statements, thereby issuing false audit results to Lehman Brothers' financial statements. The Lehman Brothers bankruptcy case is one example of the failure of the auditor to assess the company's ability to maintain its business continuity.

The Association of Certified Fraud Examiners (ACFE) in Report to Nation 2016 revealed that Asia-Pacific ranks third of nine research

areas after the United States and Africa in fraud cases, which is about 221 cases or 10.4%. The fraud can be divided into three, namely asset misappropriation, corruption, and financial statement fraud. The case of fraudulent presentation of financial statements in 2016 amounted to 9.8% increased by 0.8% when compared to the year 2014 which is only 9%. The biggest losses incurred in the case of fraud in the presentation of financial statements amounted to US \$ 975,000.

ACFE states that fraud in many countries can be detected because tips. While tips are consistently the top detection method in every region. For the Asia-Pacific region, almost 45.20% of fraud were detected because of tips, 15.80% of fraud detected by internal auditors while external auditors only able to uncover fraud by 5.9%. The results of this study indicate the low of external auditor role in the disclosure of fraud.

The other cases involving auditor roles in the conduct of the audit took place in the Toshiba Company. Recently, the Japanese electronics giant (Toshiba) stated that the losses experienced in

2016 are greater than previous predictions. This stems from the unfolding of the accounting scandal in 2015, leaving the CEO and some Toshiba senior managers to resign. In the scandal, Toshiba proved to inflate earnings in the last 7 years of 1.2 billion US dollars (Kompas, June 26, 2017). This indicates that Ernst and Young as Toshiba's external auditor was unable to find any accounting fraud practices performed by Toshiba's management. This shows that reputed KAP are unable to provide high audit quality to maintain their reputation.

In 2017, Ernst and Young's affiliate KAP in Indonesia, KAP Purwantono, Suherman & Surja has agreed to pay a fine of \$1 million after the U.S. audit regulator labeled lapses in its checks of a client's books "audit failure." The agreement was announced by Public Company Accounting Oversight Board (PCAOB) on February 9, 2017. They found that the audit results of one telecommunication company in Indonesia are not supported with accurate data for the accounting of over 4,000 leases for space in its cellular towers. However, the affiliate Ernst and Young in Indonesia released an audit report with unqualified status (Reuters, Feb. 10, 2017).

Two months before the Ernst and Young case erupted, KAP Deloitte and Touche through its affiliates in Brazil agree to pay a PCAOB fine \$ 8 million to settle civil charges that it issued and tried to cover up false audit reports. This case is the latest incident that hit the KAP, raising concerns that KAP can run its business practices, according to the code of conduct (Reuters, Feb. 10, 2017).

AAA Financial Standard Committee (2001) states that audit quality is determined by competent (expertise) and independence. Auditor independence is the cornerstone of the audit profession (Mohamed and Habib, 2013). Blandon and Bosch (2013); Mgbame et al. (2012) and Al-Thuneibat et al. (2011) states that one way to improve audit quality is to make a change of auditors. The close relationship to management leads the auditor to better identify with management interests than with the public interest (Giri, 2010; Blandon and Bosch, 2013). However, Jackson et al. (2008) concluded that the change of auditors performed would result in unnecessary costs (the cost of introducing new auditors with clients), both for KAP and for companies with minimal benefits. Furthermore, the auditor's knowledge of the company's performance will be better when the involvement occurs over a long period of time. In Indonesia, the provisions concerning the audit work are regulated in Peraturan Menteri Keuangan Republik Indonesia Nomor 17/PMK.01/2008.

Problems can occur if the auditor is required to make decisions contrary to his or her independence. An auditor is required to always be independent of the client, but at the same time the auditor must also be able to fulfill the decision desired by the client because their economic needs depend on the fee paid by the client. This is evidenced by research Fitriany and Anggraita (2016); Kraub et al. (2015) and Choi et al. (2010) stating that positive abnormal audit fees (ABFE) negatively affect audit quality. However, on the other hand Eshleman and Guo (2014) revealed that high audit fees will increase the quality of the audit.

Audit quality is often associated with the reputation of the audit firm. However, Boone et al. (2010) shows that KAP Big 4 and KAP two tier both show the same efficiency and audit quality. Craswell et al. (1995) argue that the auditor's reputation is less valuable when an industry, there is also a specialist auditor because industry specialist auditors have superior knowledge and more experience in a particular industry, so as to better detect earnings management compared to auditor industry non-specialization and may Improve earnings quality (Kanagaretnam et al., 2010). Meza (2013) shows that there is no difference in the quality of audits produced by auditor industry specialization and auditor industry non-socialization.

Auditors are considered to have the ability to provide a signal to the market. The ability to provide this signal is obtained from the auditor's authority to access company information and the auditor's ability to assess going concern issues. Over the past two decades, the auditor's responsibility to assess the viability of going concerns in the client's financial statements has been the subject of much debate in the audit and research profession by academics (Vanstraelen, 2002). O'Reilly (2009) and Chen and Church (1996) argue that going concern opinion is useful for investors because it is an early warning about the survival of the company. On the one hand, the auditor's consideration in providing a going concern audit opinion can accelerate the bankruptcy process of the company (Gallizo and Saladrignes, 2016).

Generally, research on audit quality that focuses on the impact of giving going concern opinion still shows result which is not unidirectional. Barbadillo et al. (2004) revealed that the quality of audit affects the probability of companies experiencing financial difficulties will receive a going concern opinion. However, Vanstraelen's (2002) study shows that auditors in Belgium are significantly less likely to issue a going concern opinion for clients who pay higher audit fees and audit quality does not affect the giving of going concern opinion. This is likely due to the use of different audit quality proxies. In this study audit quality will be proxied with discretionary accruals.

Previous research on the influence of audit tenure, audit fees and auditor reputation on audit quality and its impact on giving of going concern opinion still shows unrelated results. In addition, previous studies only conducted partial testing of each variable. This research is done by integrating the variables that have been studied before into a path analysis. In addition, prior research on ABFE largely focuses on audit markets in the United States (US), China and Germany. There is little research on ABFE performed in developing countries such as Indonesia.

## 2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

### 2.1. Agency Theory

Jensen and Meckling (1976) disclose that agency relationship are a contract by one or more principals that involve agents to carry out some activities by delegating decision-making powers to agents. Eisenhardt (1989) explains that the problem that can occur in an

agency relationship is that there is a conflicting interest between the principal and the agent so that the principal cannot verify that the agent has performed his or her duties properly. Conflicts over differences in importance and asymmetric information create a shared need to audit financial statements by a competent and independent third party (Al-Thuneibat et al., 2011). In other words, the auditor is a party that is considered capable of being an independent party for the interests of the stakeholders (principal) with the manager (agent) in managing corporate finance.

According to Committee Reports (1972), the main criterion of auditing focuses on oversight and or bias disclosure in accounting information to be communicated to interested parties. Auditing is based on four criteria used in evaluating potential accounting information, namely: Relevance, verifiability, freedom from bias and quantifiability. DeAngelo (1981) defines audit quality as an auditor's probability of finding mistakes in the client's accounting system and reporting errors. Audit quality is one of the important issues facing the audit profession (Vanstraelen, 2000). Audit quality is used to improve the credibility of financial statements so as to reduce the risk of non-credible information for users of financial statements, especially investors (Mgbame et al., 2012).

Auditors are considered to have the ability to provide a signal to the market. The ability to provide this signal is derived from the auditor's authority to access company information and the auditor's ability to assess going concern issues (O'Reilly, 2009). The auditor is responsible for evaluating whether there is any substantial doubt about the entity's ability to maintain its viability within a reasonable period of time, not later than 1 year from the date of the audited financial statements (then the specified period will be called a reasonable period of time) (SA Seksi 341 No. 02).

## 2.2. The Effect of Audit Tenure on Audit Quality

The assignment period is defined as the number of years the auditor is maintained by the company (Myers et al., 2003). In Indonesia, the audit tenure provisions have been regulated in Peraturan Menteri Keuangan Republik Indonesia Nomor 17/PMK.01/2008. In article 3 explained that the general audit service of an entity's financial statement shall be executed by the KAP for a maximum of six consecutive years and for the auditor three consecutive years for the longest.

Jackson et al. (2008) concluded that the change of auditors performed would result in unnecessary costs (the cost of introducing new auditors with clients), both for KAP and for companies with minimal benefits. Furthermore, the auditor's knowledge of the company's performance will improve when engagement occurs over a considerable period of time. Thus, the quality of audit reporting will increase as the auditor's competency increases over the client's performance. Therefore, hypotheses can be formulated as follows:

H<sub>1</sub>: Auditor tenure has a positive effect on audit quality

## 2.3. The Effect of ABFE on Audit Quality

Choi et al. (2010) revealed that audit fees can be divided into two components, namely the component of normal fee (supposed) and

abnormal fee components. Normal fees are mainly determined by factors that are common across different clients, such as client size, client complexity and client-specific risk, while abnormal fees are determined by factors that are idiosyncratic to a specific auditor-client relationship. In Indonesia, the determination of the fees has been set in Peraturan Pengurus Nomor 2 Tahun 2016 Tentang Penentuan Imbalan Jasa Audit Laporan Keuangan issued by Indonesia Public Accountant Institute (IAPI).

Hoitash et al. (2007) said that high audit fees can improve the efforts made by auditors, thereby improving audit quality. On the other hand, the existence of financial dependence (economic ties between auditors and clients) may cause auditors to be reluctant to make appropriate inquiries during the audit process because they are afraid of losing beneficial audit fees received from clients. Choi et al. (2010) found in the sample with negative ABFE, there was no correlation between ABFE and audit quality, but in the sample with a positive abnormal audit fee, the ABFE had a negative effect on audit quality. Therefore, hypotheses can be formulated as follows:

H<sub>2</sub>: ABFE have a negative effect on audit quality

## 2.4. The Effect of Auditor Reputation on Audit Quality

Mayhew (2001) states that reputation serves as an endogenous mechanism that results in high audit efforts and high audit quality when demand for auditor services depends on reputation to support high quality audit reporting. Choi et al. (2010) states that large KAP produce better audit quality than small KAP. Large KAP tend to be independent in disclosing and reporting fraud committed by clients. Kanagaretnam et al. (2010) argue that firms audited by large KAP will result in lower discretionary accruals compared to small KAP, so large KAP can increase reported credibility of accruals and thereby increase the value of discretionary accrual information.

O'Reilly and Reisch (2002) explain that KAP with specific knowledge about a particular industry will produce high audit quality so that it will improve audit effectiveness. Auditors with good industry knowledge will easily detect problems that exist within the client industry, thereby limiting the practice of earnings management (Kanagaretnam et al., 2010). In this study, the auditor reputation is divided into two, such as size of auditor and auditor industry specialization. Therefore, hypotheses can be formulated as follows:

H<sub>3a</sub>: Auditor size has a positive effect on audit quality

H<sub>3b</sub>: Auditor industry specialization has a positive effect on audit quality.

## 2.5. The Effect of Audit Quality on Giving Going Concern Opinion

Audit quality is used to improve the credibility of financial statements so as to reduce the risk of non-credible information for users of financial statements, especially investors (Mgbame et al., 2012). Auditors are considered to have the ability to provide a signal to the market. The ability to provide this signal is derived from the auditor's authority to access company information and the ability of auditors to assess going-concern issues (O'Reilly, 2009).

Mutchler (1985) stated that smaller firms would be more at risk of receiving going concern audit opinion than larger companies. This is possible because the auditor believes that a larger company can solve the financial difficulties it faces than smaller companies. Francis and Yu (2009) argue that KAP Big 4 will provide a high quality audit that reflects the quality of auditors in giving a going concern opinion. Therefore, hypotheses can be formulated as follows:

H<sub>4</sub>: Audit quality has a positive effect on giving going concern opinion

### 2.6. Audit Quality Mediating Impact of Audit Tenure, ABFE and Auditor Reputation on Giving Opinion Going Concern

The auditor's knowledge of the company's performance will be better when the auditor has a long-term engagement (Jackson et al., 2008). On the other hand, the existence of financial dependence (economic ties between auditors and clients) may cause auditors to be reluctant to make appropriate inquiries during the audit process because they are afraid of losing the favorable audit fees received from clients (Hoitash et al., 2007).

Choi et al. (2010) suggests that large KAP produce better audit quality compared to small KAP. Large KAP tend to be more independent in disclosing and reporting fraud committed by clients. O'Reilly and Reisch (2002) explain that KAP with specific knowledge about a particular industry will produce high audit quality so that it will improve audit effectiveness. Francis and Yu (2009) argue that KAP Big 4 will provide a high quality audit that reflects the quality of auditors in giving going concern opinion. However, Blay et al. (2016) found that Non-Big 4 auditors in countries with relatively high rates of going concerns in the previous year were 6% more likely to issue going concerns. Therefore, hypotheses can be formulated as follows:

H<sub>5</sub>: Audit quality mediates the effect of auditor tenure, ABFE and auditor reputation on giving going concern opinion.

### 2.7. Financial Condition Moderating Impact of Audit Quality on Giving Opinion Going Concern

Platt and Platt (2002) define financial distress as a condition of decreased performance of companies that will lead the company into bankruptcy or liquidation. Financial distress conditions of a company are also associated with fiscal crisis issues, fiscal distress, financial risk or fiscal strain (Cohen et al., 2017).

Geiger et al. (2014) stated that the increasing tendency of auditors to issue going-concern opinion occurs because of the financial crisis of the company. Koh (1991) states that the use of bankruptcy prediction models will assist auditors in providing a going concern assessment. Setyarno et al. (2006) indicates that the financial condition has a significant effect on the acceptance of going concern. Therefore, hypotheses can be formulated as follows:

H<sub>6</sub>: Financial conditions moderate the effect of audit quality on giving going concern opinion.

## 3. STUDY DESIGN AND METHODOLOGY

### 3.1. Population and Sample

The population in this study are all companies listed in Indonesia stock exchange (IDX) period 2012–2015. This research used purposive sampling method or sampling based on certain considerations: (1) A non-financial company listed on the IDX (BEI) and publishes an annual report within the study period, (2) the company includes audited financial statements by an independent auditor, (3) the company discloses audit fees, (4) the company has experienced loss of at least 2 consecutive years or has negative retained earnings, (5) the company has completed data used in research for 5 years. Based on the criteria set, then obtained the final sample of 185 sample companies. The analytical method used in this research is by using partial least square analysis model (PLS) following the pattern of structural equation modeling model based on variance which can simultaneously perform testing of measurement model as well as testing of structural model (Ghozali and Latan, 2015).

### 3.2. Dependent Variables

#### 3.2.1. Going concern opinion (GCOP)

This variable is measured using the dummy variable. The going concern (GCOP) is coded 1, whereas non-going concern opinion is coded 0.

### 3.3. Independent Variables

#### 3.3.1. Audit tenure (TENA)

Audit tenure is the period of assignment of auditors in a company. According to Al-Thuneibat et al. (2011), the calculation of audit tenure variables by counting the number of years the auditor performs an audit of a company's financial statements in sequence.

#### 3.3.2. ABFE

ABFE calculation uses the residual value of the normal OLS fee audit regression (Eshleman and Guo, 2014). Normal audit fee calculations into: (1) Client size, (2) client complexity, (3) specific risks to audit engagement such as client and auditor risk (Fitriany and Anggraita, 2016; Eshleman and Guo, 2014; Choi et al., 2010).

$$ABFE = \beta_0 + \beta_1 LNTA + \beta_2 EMPLOY + \beta_3 NBS + \beta_4 NGS + \beta_5 INVREC + \beta_6 QUAL + \beta_7 LOSSLAG + \beta_8 LEVE + \beta_9 LIQUID + \beta_{10} ROA + \beta_{11} BIG4 + \beta_{12} Short\_Ten + \beta_{13} BTM + \beta_{14} CHGSALE$$

ABFE = Natural logarithm for factual audit fees

LNTA = Natural logarithm of total assets

EMPLOY = The square root of the employee

NBS = Natural logarithm above 1 plus number of business segments

NGS = Natural top logarithm 1 plus number of geographical segments

INVREC = Inventories and receivables divided by assets

QUAL = 1 if the opinion is going concern, 0 others.

LOSSLAG = 1 if net income period t-1 is negative, 0 others

LEV = Leverage (total liabilities divided by total assets)

ROA = Return on assets (net income divided by average total assets)

LIQUID = Current assets divided by current liabilities

BIG4 = 1 if the auditors Deloitte and Touche, Ernst and Young, KPMG, and Price Waterhouse Coopers, 0 others

Short\_Ten = 1 if the engagement period at the beginning of the year, 0 others

BTM = Book to market ratio

CHGSALE = Changes in sales for the current year divided by total assets.

### 3.4. Auditor Reputation

Auditor reputation is divided into two aspects, such as auditor size and auditor industry specialization.

### 3.5. Auditor Size (BIG4)

In this study the auditor size measures using dummy variables, the value of 1 if the company is audited by KAP Big 4 and 0 if audited by KAP Non-Big 4.

### 3.6. Auditor Industry Specialization (SPEC)

According to Rusmin (2010), auditor industry specialization is auditors who have a market share of at least 20% of the total number of clients received in certain groups. The amount of market share is determined by the part of the audit fee received by the firm in a particular industry compared to the total audit fees that all KAP in certain industries receive.

### 3.7. Mediating Variables

#### 3.8. Audit quality (KUAD)

This study uses an accrual discretionary (DA) as a proxy for audit quality. Kasznik (1999) states that non-discretionary accruals are a function of income changes adjusted for changes in accounts receivable, PPE and CFO.

$$\frac{TA_{it}}{A_{it-1}} = \alpha_0 \left( \frac{1}{A_{it-1}} \right) + \alpha_1 \left( \frac{\Delta REV_{it} - \Delta REC_{it}}{A_{it-1}} \right) + \alpha_2 \left( \frac{PPE_{it}}{A_{it-1}} \right) + \alpha_3 \left( \frac{\Delta CFO_{it}}{A_{it-1}} \right) + e_{it}$$

$TA_{it}/A_{it-1}$  = Total accrual of the firm i in period t

$\Delta REV$  = Change of income from year t-1 to year t ( $REV_t - REV_{t-1}$ )

$\Delta REC$  = Change of net of receivable value from year t-1 to year t ( $REC_t - REC_{t-1}$ )

PPE = Fixed asset value in year t

$\Delta CFO$  = Changes in operating cash flow from year t-1 to year t ( $CFO_t - CFO_{t-1}$ ).

## 3.9. Moderating Variables

### 3.9.1. Financial condition (ZSCR)

The revised model of Altman (1993) is as follows:

$$Z\text{-score} = 0.717Z_1 + 0.874Z_2 + 3.107Z_3 + 0.420Z_4 + 0.998Z_5$$

$Z_1$  = Working capital/total asset

$Z_2$  = Retained earnings/total asset

$Z_3$  = Earnings before interest and taxes/total asset

$Z_4$  = Market value of equity/book value of debt

$Z_5$  = Sales/total asset.

## 3.10. Control Variables

### 3.10.1. Client size (LNTA)

According to Al-Thuneibat et al. (2011), large companies tend to act cautiously in managing companies and tend to manage earnings efficiently. The client size is calculated using the natural log of total assets.

### 3.10.2. Leverage (LEVE)

Researchers control the leverage of firms to be studied because high levels of financial leverage can increase the risk that companies will face (Al-Thuneibat et al., 2011). Leverage is the ratio between total debt and total assets showing the amount of assets used to guarantee debt.

### 3.10.3. Company growth (GRWT)

Rusmin (2010) states that companies that have high growth companies are likely to be motivated to take profit management action. Company growth is calculated as follows:

$$\text{Growth} = \frac{\text{Sales}_t - \text{Sales}_{t-1}}{\text{Sales}_{t-1}}$$

### 3.10.4. Liquidity (LIKU)

Liquidity ratio is a ratio that describes the ability of the company in meeting short-term liabilities (debt). If the company is unable to meet its short-term debt, it can be assumed that the company is facing a problem that could disrupt its business continuity. Liquidity is the ratio between current assets and current debt.

## 4. RESULTS AND DISCUSSIONS

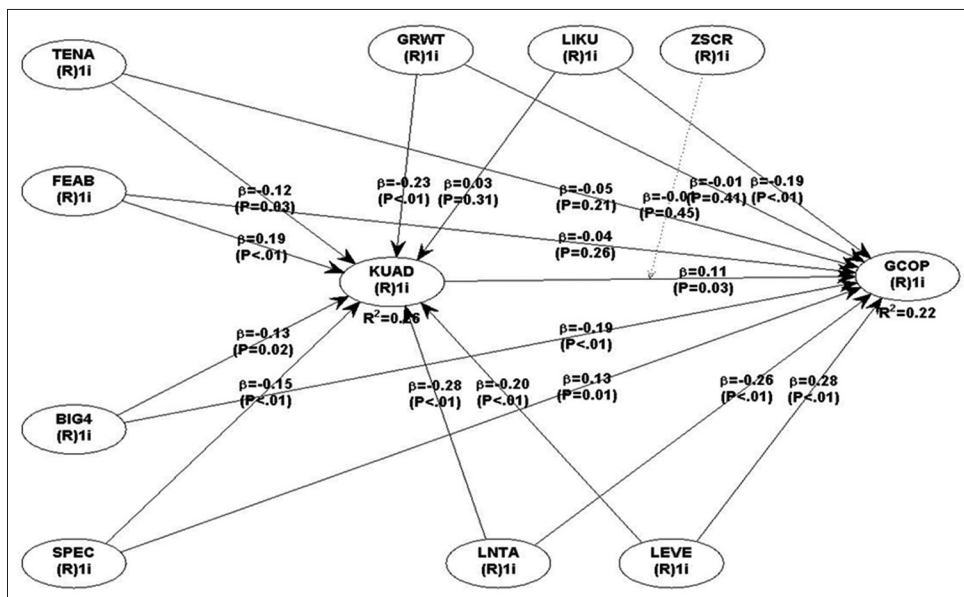
The magnitude of the suitability of the model can be determined by looking at the average R-squared (ARS) calculation. Average path

**Table 1: Value of goodness of fit model**

Result	P value	Criteria	Explanation
ARS=0.243	P<0.001	P<0.05	Accepted
APC=0.145	P=0.004	P<0.05	Accepted
AVIF=1.386		AVIF<5	Accepted

Source: Output PLS. ARS: Average R-squared, APC: Average path coefficient, AVIF: Average variance inflation factor, PLS: Partial least square

Figure 1: Output results hypothesis test



coefficient (APC) shows the interrelationship between variables. Average variance inflation factor (AVIF) shows correlation or multicollinearity among independent variables.

Table 1 shows that all goodness of fit criteria in WarpPLS is accepted. ARS calculation shows that ARS value is significant and the influence of the independent variable to dependent variable is 24.3% and the rest equal to 75.7% influenced by other independent variable. APC value of 0.145 and significant. It indicates that there is a causal relationship either directly or indirectly. In addition, this research model also shows the absence of multicollinearity as indicated by the AVIF value <5.

The result of hypothesis testing using WarpPLS 4.0 is shown in Figure 1.

The path coefficient is positive if beta ( $\beta$ ) is negative because the audit quality calculated using discretionary accruals indicates that if the discretionary accrual value is high, then the quality of the audit report is low. Thus, the value of a discretionary accrual has an inverse relationship with audit quality. Test results can be seen in Tables 2 and 3.

#### 4.1. The Effect of Audit Tenure on Audit Quality

The result of  $H_1$  test shows that the auditor has a positive effect on audit quality. This can be seen in Table 2 which shows a significance value of 0.028 and the beta coefficient ( $\beta$ ) of 0.116 (positive). This indicates that the auditor engagement period increases, the better the audit quality will be. Good audit quality is assessed with small discretionary accruals.  $H_1$  is accepted if the auditor's coefficient of positive marker and significant to audit quality. Based on this it can be concluded that  $H_1$  accepted.

This study supports the research of Jackson et al. (2008) which concluded that auditor turnover would lead to unnecessary costs (the cost of introducing new auditors with clients), both for KAP and for companies with minimal benefits. Furthermore, the auditor's knowledge of the company's performance will improve

when engagement occurs over a considerable period of time. Thus, the quality of audit reporting will increase as the auditor's understanding of client performance improves.

#### 4.2. The Effect of ABFE on Audit Quality

The result of  $H_2$  test shows that ABFE negatively affect audit quality. This can be seen in Table 2 which shows the significance value of 0.001 and the beta coefficient ( $\beta$ ) of  $-0.185$  (negative). This indicates that the greater the audit fees received by the auditor during the assignment period, the quality of the audit will be worse. Good audit quality is assessed with small discretionary accruals.  $H_2$  accepted if the coefficient of abnormal audit fee marked negative and significantly to audit quality. Based on this it can be concluded that  $H_2$  accepted.

This research supports the results of Fitriany's research (2016); Kraub et al. (2015) and Choi et al. (2010) stating that audit fees above normal causes bonding auditors to be stronger, thus decreasing auditor independence and degrading audit quality.

#### 4.3. The Effect of Auditor Reputation on Audit Quality

The auditor reputation is divided into two aspects, namely auditor size and auditor industry specialization.

#### 4.4. The Effect of Auditor Size on Audit Quality

The  $H_{3a}$  test result shows that the auditor size has a positive effect on audit quality. This can be seen in Table 2 which shows a significance value of 0.015 and the beta coefficient ( $\beta$ ) of 0.131 (positive). This shows that Big 4 KAP will provide better audit quality than Non-Big KAP 4. Good audit quality is assessed with small discretionary accrual value.  $H_{3a}$  is accepted if the KAP-size coefficient is positive and significant to audit quality. Based on this it can be concluded that  $H_{3a}$  accepted.

This study supports the research of Choi et al. (2010) and Kanagaretnam et al. (2010) stating that large KAP produce better audit quality than small KAP. Large KAP tend to be independent

**Table 2: Hypothesis testing results H<sub>1</sub> to H<sub>4</sub> and H<sub>6</sub>**

Hypothesis	Prediction	Variable effect <sup>(*)</sup>	Path Coef <sup>(<math>\beta</math>)</sup>	P value	Significance	Result
H <sub>1</sub>	+	TENAD→KUAD	+0.116	0.028	Significant	Accepted
H <sub>2</sub>	-	FEAB→KUAD	-0.185	0.001	Significant	Accepted
H <sub>3a</sub>	+	BIG4→KUAD	+0.131	0.015	Significant	Accepted
H <sub>3b</sub>	+	SPEC→KUAD	+0.146	0.008	Significant	Accepted
H <sub>4</sub>	+	KUAD→GCOP	-0.114	0.029	Significant	Not accepted
H <sub>6</sub>	Moderating	KUAD*ZSCR→GCOP	+0.007	0.452	Not significant	Not accepted

Source: Data processed, WarpPLS 4.0. <sup>\*</sup>Indirect effect, <sup>\*</sup>path coefficient ( $\beta$ ) discretionary accrual to audit quality

**Table 3: Hypothesis testing result H<sub>5</sub> (mediating effect)**

Hypothesis	Variable effect <sup>**</sup>	Path Coef ( $\beta$ )	P value	Significance	Result	Mediating
H <sub>5</sub>	TENA→GCOP	-0.049	0.210	Not significant	Not accepted	Fully
	FEAB→GCOP	-0.038	0.262	Not significant	Not accepted	Fully
	BIG4→GCOP	-0.190	<0.001	Significant	Accepted	Partially
	SPEC→GCOP	+0.111	0.014	Significant	Accepted	Partially

Source: Data processed, WarpPLS 4.0. <sup>\*</sup>Indirect effect look at Table 2, <sup>\*\*</sup>direct effect

in disclosing and reporting fraud committed by clients. In addition, investors assume that larger KAP are more able to meet the lawsuits that occur than small KAP (Skinner and Srinivasan, 2012).

#### 4.5. The Effect Auditor Industry Specialization on Audit Quality

The H<sub>3b</sub> test result shows that auditor industry specialization has positive effects to audit quality. This can be seen in Table 2 which shows the significance value of 0.008 and the beta coefficient ( $\beta$ ) of 0.146 (positive). This suggests that auditor industry specialization will provide better audit quality than auditor industry non-specialization. Good audit quality is assessed with small discretionary accruals. H<sub>3b</sub> is accepted if the coefficient auditor industry specialization is marked positive and significant to audit quality. Based on this it can be concluded that H<sub>3b</sub> accepted.

This research supports Kanagaretnam et al. (2010) research which states that auditor industry specialization will limit earnings management practices. Furthermore, O'Reilly and Reisch (2002) explain that KAP with specific knowledge about a particular industry will result in high audit quality, thereby enhancing the effectiveness of the audit.

#### 4.6. The Effect of Audit Quality on Giving Opinion of Going Concern

H4 test result shows that audit quality has a negative effect on giving going concern opinion. This can be seen in Table 2 which shows the significance value of 0.029 and the beta coefficient ( $\beta$ ) of -0.114 (negative). This indicates that the greater the reported discretionary accruals, the lower the audit quality, so that the auditor is more likely to giving going concern opinion. Good audit quality is assessed with small discretionary accruals. H<sub>4</sub> accepted if the audit quality coefficient marked positive and significant to the giving going concern opinion. Based on this it can be concluded that H<sub>4</sub> rejected.

The results of this study indicate that high discretionary accruals indicate high management practices that can create auditor doubt, thus allowing auditors to provide a going concern opinion. Muramiya and Takada (2010) in his research found that the practice of earnings management is an indicator of the beginning for the auditor to issue a going concern opinion.

High discretionary accruals indicate the number of management interventions on the company's financial statements. The existence of management intervention indicates that management wants to achieve certain goals. Management interventions can be management plans that have been implemented. Companies experiencing poor financial conditions tend to conduct management planning in order to convince the auditors that the company is still capable of running its operations. SA Section 341 discloses that if the auditor has doubts about the entity's ability to maintain its survival and the auditor concludes that the management plan can be effectively implemented, the auditor will provide an unqualified opinion with an explanatory paragraph of the business unit's ability to maintain its viability. Furthermore, SA Seksi 341 discloses that the management plan may be an asset sale plan, a debt withdrawal plan or a debt restructuring, a plan to reduce or postpone spending and a plan to raise ownership.

The results of this study do not support the research of Barbadillo et al. (2004) indicating that audit quality (measured by the level of independence and knowledge of auditors) affects the probability that a company experiencing financial difficulties will receive a going concern opinion. It happens because of different audit quality measurement proxies.

#### 4.7. Audit Quality Mediating Impact of Audit Tenure, ABFE and Auditor Reputation on Giving Opinion Going Concern

H5 tested the effect of mediation variables. The test results show that audit quality is able to mediate the influence of audit tenure, ABFE and auditor reputation on giving going concern opinion. This can be seen in Table 3 which shows a significance value of 0.210 for audit tenure, 0.262 for ABFE, <0.001 for auditor size and 0.014 for auditor industry specialization. H5 is accepted if P value for direct testing is significant value, which means partial mediated audit quality or P value for direct testing is insignificant, which means the quality of the audit is fully mediated. Based on this it can be concluded that H<sub>5</sub> accepted.

This study supports the Read and Yezegel (2016) studies which provide evidence that the length of the auditor's length is not associated with Type II errors. This shows that audit tenure and

ABFE affect the audit quality, so that will impact on decision of giving going concern opinion or not. Blay et al. (2016) found that Non-Big 4 auditors residing in countries with relatively high rates of going concerns in the previous year were six percent more likely to issue going concern opinions. Auditor industry specialization will provide a higher level of check guarantee than the audits performed by auditor industry non-specialization (Craswell et al., 1995). The guarantee of the examination is related to the giving going concern opinion.

#### 4.8. Financial Condition Moderating Effects of Audit Quality on Giving Going Concern Opinion

H<sub>6</sub> tested the effect of moderating variables. The test results show that the financial condition is not able to moderate the influence of audit quality on giving going-concern opinion. This can be seen in Table 2 which shows the interaction value of 0.452 and the beta coefficient ( $\beta$ ) of 0.007. H<sub>6</sub> accepted if P value significant moderation variable interaction value. Based on this it can be concluded that H<sub>6</sub> rejected.

It means that the company's financial condition does not moderate the effect of audit quality on giving going concern opinion. This can happen because the giving going concern opinion is not only based on the company's financial condition, but also internal and external issues of the company (SA Seksi 341). SA Seksi 341 mentions that internal company problems may include work strikes or labor difficulties, substantial reliance on certain projects, non-economic long-term commitments and resource requirements to significantly improve operations. Examples of external problems that have occurred are complaints of court suits, the release of laws or other matters which may jeopardize the entity's ability to operate; Loss of franchise, license or patent; loss of major customers or suppliers; And losses due to major disasters such as earthquakes, floods, uninsured or insured droughts but with an inadequate amount of coverage.

Blay et al. (2016) stated that giving going concern opinion, besides caused by economic factor also caused by a behavioral psychological factor of auditor. The giving going concern opinion is based on the auditor's belief about the presence or absence of things that may disrupt the entity's ability to maintain its survival within 1 year (Tanzil, 2016).

## 5. CLOSING

### 5.1. Conclusion

Based on the results obtained through statistical testing and the discussion described in the previous chapter, it can be concluded things as follows:

1. Audit tenure and auditor reputation positively affect audit quality, while ABFE negatively affect audit quality. This suggests that the quality of audits will increase as the auditor's understanding of client performance improves. In addition, firms audited by reputable firms tend to be independent in disclosing and reporting fraud committed by clients, resulting in high audit quality.
2. Audit quality negatively affects giving going concern opinion. This proves that companies experiencing poor financial

conditions tend to conduct management planning in order to convince the auditors that the company is still capable of running its operations. High discretionary accruals indicate high management practices that can create auditor doubt.

3. From the results of direct and indirect testing indicates that the audit quality can fully mediate the influence of audit tenure and ABFE on giving going concern opinion. This indicates that auditor tenure and ABFE have no significant effect on giving going concern opinion. While the reputation of auditors can significantly influence the giving of going concern opinion. This shows that audit quality mediates the partial influence of auditor reputation on giving going concern opinion.
4. Financial condition does not moderate the influence of audit quality on giving going concern opinion. This is caused by the giving going concern not only based on the company's financial condition, but also internal and external issues of the company (SA Seksi 341).

## 6. LIMITATIONS AND RECOMMENDATIONS

This study has the limitations, at least the company that explicitly disclosed its audit fees. It has an impact on the number of samples used too few companies. This study only focuses on the company's financial condition only, while other factors are not included in determining the giving going concern opinion. In addition, this study does not explain the impact of giving going concern opinion to the company and the market.

Further researcher can add other variables such as management strategy because in this study the financial condition has not moderate the effect of audit quality on giving going concern opinion. In addition, there necessary to evidence of the impact of going concern opinion on market players and companies, enabling the company to get the same opinion in the next year.

## 7. IMPLICATIONS

The results of this study indicate that ABFE have a negative effect on audit quality. Therefore, researchers advise governments and associations to periodically review the quality of KAP in relation to documentation related to the audit engagement, so it can produce a good quality audit. In addition, the auditor should be able to be professional in accordance with applicable standards in order not to be given written sanctions related to significant audit quality degradation because the fee received is too high or too low (IAPI, Peraturan Pengurus Nomor 2 Tahun, 2016). This study shows that the length of audit engagement provides high audit quality. This indicates that regulator should evaluate the rules regarding the duration of the engagement. Regulators should not only look at their independence, but also the time it takes the auditor to understand the client's business in order to create the proper audit procedures.

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