

## The Effect of Auditor Rotation and Auditor Reputation on Audit Quality in Companies Registered Banking Sub-Sectors on Bursa Efek Indonesia Period 2017-2019

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**Abstract.** *This research aims to analyze the effect of auditor rotation and auditor reputation on audit quality in banking sub-sector companies listed on the Indonesia Stock Exchange (BEI). Several previous studies regarding audit quality have shown different results. Therefore, other research needs to be conducted to retest theories about audit quality. The population of this research was 43 banking sub-sector companies. The sampling method used was a purposive sampling method so 24 sample companies were obtained for 3 years of observation (2017-2019) with 72 observations (observations). Research data was obtained from sample companies downloaded from the website Indonesia Stock Exchange. The data analysis techniques used are descriptive statistical analysis and logistic regression analysis. The data analysis process carried out first is descriptive statistical analysis, logistic regression analysis, and then hypothesis testing. The results of this research partially show that auditor rotation does not have a significant effect on audit quality. Meanwhile, the auditor's reputation partially has a significant effect on audit quality. The results of this research indicate that auditor rotation and auditor reputation simultaneously have a simultaneous effect on audit quality.*

**Keywords:** *Audit Quality, Auditor Rotation, Auditor Reputation.*

### INTRODUCTION

De Angelo (1981) defines audit quality as the probability that an auditor finds and reports a violation in his auditee's accounting system. The results of his research show that large KAPs will try to present greater audit quality compared to small KAPs. In carrying out their duties as an auditor, the most important thing for public accountants to pay attention to is the quality of the audit they produce. The Indonesian Accountants Association states that an audit carried out by an auditor is said to be of quality if it meets auditing standards and quality control standards. Auditor rotation is a change of Public Accounting Firm or Public Accountant by a company in accordance with rotation

obligations (Aldona and Trisnawati, 2018). Auditor rotation is carried out to maintain public trust in auditors and to improve audit quality.

The large number of fraud cases that occur involving public accountants are considered to be very detrimental to company owners and external parties, causing the public to question the quality of audits carried out by independent auditors. Cases of manipulation of financial reports carried out by Bank Bukopin for the last 3 (three) years, so that Bank Bukopin had to correct financial reports in 2015, 2016 and 2017. Bank Bukopin is suspected of manipulating credit card data for approximately 5 years ago. The number of credit cards modified was 100,000 credit cards. This caused Bukopin's credit position and commission-based income to increase unreasonably (m.detik.com.2018). This financial report was handled by auditor Ernst & Young (EY), one of the big four the largest accounting and consulting firm in the world. This tarnished the reputation of the Public Accounting Firm (CNCB Indonesia 2018). It can be seen in the case of Bank Bukopin that the reputation of an auditor with a large KAP does not guarantee that he will produce good quality audits, because if the public is aware of fraud committed by the auditor to cover up the financial reports client company, the auditor's reputation could be threatened, as in the case of Bank Bukopin, and in this case, Bank Bukopin continues to use the Big Four KAP, namely Ernst and Young (EY) in 2015, 2016, 2017. This shows that by changing the auditor, it is possible to minimize the occurrence of fraud. in a company and will maintain the independence of auditors in conducting audits of clients.

Bank Bukopin in 2017 showed poor bank performance. One of the things highlighted in this regard is that the bank's Non-Performing Loan (NPL) level has increased quite significantly. The level of non-performing loans for issuers coded BBKP reached 6.37% or an increase of almost 128% compared to the previous year's NPL which was only around 2.79%. If calculated from the total amount of financing disbursed by Bank Bukopin in that year, it reached Rp. 74 trillion, then the amount of non-performing loans achieved by the bank is around Rp. 3 trillion.

This situation needs to be watched out for, if you look at the NPL regulator's regulations which are above the 'safe' threshold, it could affect the level of supervision carried out by the authorities. Based on Financial Services Authority regulation number 15/POJK.03/2017 article 3 paragraph 1, OJK determines that banks are under intensive supervision if the bank is deemed to have potential difficulties that endanger business

continuity. One of the criteria for potential difficulties is explained in the next paragraph, namely: net non-performing credit ratio (Non-Performing Loan/NPL net) or net non-performing financing ratio (Non-Performing Financing/NPF net) is greater than 5% (five percent) of total credit or total financing. (Source: cnbcindonesia.com). Results of a survey conducted by the Association of Certified Fraud Examiner proves that banking and financial companies in Indonesia are still vulnerable to fraud cases. It is no longer something that happens in banking and financial companies. In 1997, Lippo Bank reported that the company was at a loss with assets that were smaller than the actual value of the assets, Tuanakotta (in Sihombing, 2014). Reporting from kompas.com (2011), in the first quarter of 2011 there were nine cases of crime in banking companies caused by fraud.

So that problem audit quality becomes low caused because low auditor rotation due to auditor turnover that is not in accordance with the rules or regulations of PP 20/2015, low auditor reputation because it is not included in the big four public accounting firm, and a decrease in audit quality caused by low disclosure of the company's survival or going concern.

Based on the description the problems that have been described, hence the question study this is:

1. Does auditor rotation affect audit quality in banking sub-sector companies listed on the IDX for the 2017-2019 period?
2. Does auditor reputation affect audit quality in banking sub-sector companies listed on the IDX for the 2017-2019 period?
3. Do auditor rotation and auditor reputation simultaneously influence audit quality in banking sub-sector companies listed on the IDX for the 2017-2019 period?

## **LITERATURE REVIEW**

### **Theory (*Agency Theory*)**

The theory underlying this research is agency theory theory). Agency theory (agency theory) discusses the relationship between the principal and the agent. An agency relationship is a contract in which one or more principals hire another person (agent) to perform some service for their benefit, namely by delegating some decision-making authority to the agent. The principal is the party who gives the mandate to the agent, in this case the shareholder, while what is called the agent is the party who carries out the

mandate from the principal. Namely the management that manages the company. Agency theory (agency theory) is emphasized to overcome two problems that can occur in agency relationships. The first is the agency problem which arises when the desires or goals of the principal and agent conflict with each other and it is difficult for the principal to verify whether the agent has done something correctly. Second, there is the problem of sharing where to bear the risks that arise the principal and agent have different attitudes towards risk. The essence of the agency relationship is that in the agency relationship there is a separation between ownership (the principal), namely the shareholders, and control (the agent), namely the manager who manages the company.

### **Audit Quality**

Audit quality is the auditor's ability to detect errors in financial reports and report them to financial report users. The opportunity to detect errors depends on the auditor's competence. The auditor's courage to report errors in the financial statements depends on the auditor's independence (De Angelo, 1981). Meanwhile, according to Hartadi (2012), audit quality is work professionalism that must be truly maintained by professional public accountants.

Audit quality is the probability that an auditor finds and reports a violation in his client's accounting system (Kurnia, Khomsiyah, & Sofie 2014).

### **Auditor Rotation**

Auditor rotation can be interpreted as changing public accounting firms that provide audit services to their clients (Prasetia and Rozali, 2016). The longer the engagement period between the auditor and the client can cause the auditor to have a relationship that is too close and can reduce the auditor's independent attitude and reduce the professionalism of the auditor's work, resulting in low auditor quality (Prasetia and Rozali, 2016). Changing auditor services in auditing financial reports is very necessary to reduce the closeness that exists between the two parties. Rotation is related to the time limit for Public Accountants in working to provide audit services to a company. The rotation of auditors in auditing companies aims to prevent clients and auditors from having excessive closeness (Myers , 2013). Based on Minister of Finance Regulation (PMK) No.17/PMK.01/2008 concerning Public Accounting Services dated 5 February 2008 in article 3 paragraph (1) it is regulated that: Providing general audit services for the financial statements of an entity as intended in Article 2 paragraph (1) letter a is carried

out by a KAP for a maximum of 6 (six) consecutive financial years and by a Public Accountant for a maximum of 3 (three) consecutive financial years. Based on the regulations in PMK N0.17 above, a Public Accounting Firm (KAP) may only audit a company for a maximum of 6 (six) consecutive financial years, while Public Accountants (AP) within the KAP are only permitted to audit a maximum of 3 (three) consecutive financial years.

On April 6 2015, the government issued Government Regulation (PP) No. 20 of 2015 concerning Public Accounting Practices (PP 20/2015) which is a further regulation of Law No. 5 of 2011 concerning Public Accountants. In connection with the rules for rotation of public accounting services regulated in Article 11 PP 20/2015, Article 11 paragraph (1) explains that: Providing audit services for historical financial information as intended in Article 10 paragraph (1) letter a to an entity by a Public Accountant is limited to a maximum of 5 (five) consecutive financial years.

### **Auditor's Reputation**

An auditor's reputation is the public's achievements and trust held by an auditor based on the big name that the auditor has (Sari and Widanaputra , 2016). Auditors are responsible for providing high quality information because this information is the basis for users of financial reports for company decision making. An auditor's reputation can be seen from the way he works and his independence. An auditor who can produce quality audits can boost the good name of the auditor himself and the KAP he oversees. Therefore, auditors must be fair (not take sides) towards either party in carrying out the audit process (Yanti, et al , 2018).

### **RESEARCH METHOD(S)**

This research is causality research, namely research that aims to determine the relationship and influence between two or more variables. According to Sugiyono (2016:37) "Casual associative research is research that aims to determine whether or not there is an influence and relationship between independent variables on variables. bound and if there is how much influence or relationship and whether the relationship is meaningful or not."

This research discusses Auditor Rotation and Auditor Reputation on Audit Quality in Banking Sub-Sector Companies Listed on the IDX for the 2017-2019 Period. The

population of this research is banking sub-sector manufacturing companies listed on the IDX for the 2017-2019 period, namely 43 companies.

The sampling technique in this research was using a purposive method sampling, where purposive sampling is determining the sample considering certain criteria that have been created for the object in accordance with the research objectives. The sample criteria in this research are:

1. Manufacturing companies in the banking sub sector listed on the BEI (Indonesian Stock Exchange) as of January 1 2017-2019.
2. Companies that do not provide financial reports that have been audited by independent auditors during the research period (2017-2019).
3. Companies that provide an unqualified opinion with *going forward disclosure concerns* during the research period (2017-2019).

Based on these criteria, the number of samples is 24 banking sector companies on the Indonesia Stock Exchange.

The analytical tool used in the research is logistic regression analysis regression). The reason for using logistic regression analysis is (logistic regression) is because the dependent variable is measured on a nominal scale using dummy variables.

## FINDINGS AND DUSCUSSION

### Partial Model Significance Test (Wald Test)

Statistical value from the Wald Test distribute chi -square. Decision making on hypotheses can be done using the probability value approach from the Wald test. The following are decision making rules based on the probability value approach.

**Tabel 1. Partial Model Significance Test**

		Variables in the Equations							
		B	S.E	Wald	Df	Sig.	Exp (B)	95% CI for EXP(B)	
								Lower	Upper
Step 1	Rotation AuditorX1	-.975	,927	1,105	1	,293	,377	,061	2,323
	Reputatio nAuditor X2	1,824	,570	10,248	1	,001	6,198	2,029	18,938
	Constant	-.997	,486	4,216	1	,040	,369		

Source: SPSS Version 23.0 Processing Results

Based on the table, it states that:

1. Auditor Rotation shows a negative regression coefficient of -0.975 with a probability value (Sig.) 0.293 which is greater than 0.05, so auditor rotation has no effect on Audit Quality.
2. Auditor Reputation shows a positive regression coefficient value of 1.824 with a probability value (Sig.) 0.001 which is smaller than 0.05, so the auditor's reputation has an effect on audit quality.

**Simultaneous Model Significance Test (Omnibus Test)**

To assess whether the logistic regression model involving significant independent variables (simultaneously) is better than the previous model (simple model) in terms of fitting the data, compare the Sig values. For Step 1 (Step) in the Omnibus Table Test of Model Coefficients to the significance level of 0.05. Sig value. also called probability value.

**Tabel 2. Simultaneous Model Significance Test**

Omnibus Tests of Model Coefficients				
		Chi- square	Df	Sig .
Step 1	Step	14,355	2	,001
	Block	14,355	2	,001
	Model	14,355	2	,001

Source: SPSS Version 23.0 Processing Results

**The Effect of Auditor Rotation on Audit Quality**

Wald test, it shows a negative regression coefficient of 0.293 with a probability value (Sig.) greater than 0.05, so it has no effect on audit quality. This result is in contrast to research conducted by Indah et al (2017) and Adib (2017) which shows that the results of auditor rotation have an effect on audit quality.

**The Effect of Auditor Reputation on Audit Quality**

Wald test, it shows a positive regression coefficient of 0.001 with a probability value (Sig.) that is smaller than 0.05, so the auditor's reputation has an effect on audit quality.

This result is in contrast to research conducted by Nursiam (2017) and Yanti, et al (2018) which shows that the auditor's reputation has no effect on audit quality.

### **The Effect of Auditor Rotation and Auditor Reputation Simultaneously (Together) on Audit Quality**

Based on the Omnibus test, auditor rotation and auditor reputation show value Sig.  $0.001 < 0.05$ , then auditor rotation and auditor reputation have a simultaneous effect on audit quality.

### **CONCLUSION AND RECOMMENDATION**

This research study about the influence of auditor rotation and auditor reputation in the banking sub-sector listed on the Indonesia Stock Exchange in 2017-2019 produces the conclusions below.

1. Based on testing using the logistic regression method using the Wald test, auditor rotation shows a negative regression coefficient of -0.975 with a probability value (Sig.) of 0.293 which is greater than 0.05, then auditor rotation has no effect on audit quality
2. Based on testing using the logistic regression method using the Wald test, the auditor's reputation shows a regression coefficient value of 1.824 with a probability value (Sig.) of 0.001 which is smaller than 0.05, so the auditor's reputation has an effect on audit quality
3. Based on the omnibus test, auditor rotation and auditor rerouting show a Sig value.  $0.001 < 0.05$ , then auditor rotation and auditor reputation have a simultaneous effect on audit quality

As for suggestions from study This are:

1. For future researchers, they can extend the observation year so they can see the possibility of audit quality in the long term.
2. Including additional variables such as the characteristics of the independent auditor, size of the board of commissioners, independence of the board of commissioners, external costs and so on so that research is better able to produce research that is more representative and able to predict audit quality accurately.
3. Expanding the population is not only limited to banking sub-sector companies so that the sample will be larger and can see a wider range of audit quality possibilities.



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