

## THE EFFECT OF FINANCIAL DISTRESS AND AUDIT DELAY ON AUDITOR SWITCHING

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### Abstract

This study aims to prove the effect of financial distress and audit delay on auditor switching. The study was conducted in banking companies listed on the Indonesia Stock Exchange. The population of this study is the financial statements of banking companies listed on the Indonesia Stock Exchange. in 2016-2019 as many as 45 companies. Determination of the sample using purposive sampling using certain criteria, companies that meet the criteria are 37 companies with 4 years of observation, so the number of observations in this research is 148. Tests were carried out using logistic regression analysis with the help of SPSS software. The results of this study indicate that financial distress and audit delay have no effect on auditor switching.

**Keywords :** *financial distress, audit delay, auditor switching.*

### 1. INTRODUCTION

Auditor switching is a change of auditor or KAP in a company. Mandatory (mandatory) and voluntary (voluntary) are characteristics of auditor turnover. Mandatory is auditor change which is carried out to comply with applicable regulations, while voluntary is auditor change which is carried out because the existence of certain elements outside of the applicable regulations (Pawitri & Yadnyana, 2015). Every company has the right to choose KAP big four atau KAP non big four. Auditors in agencies/companies, especially go-public companies, have an important role, to produce a financial report, which is reliable and trustworthy. One of the roles of auditors is to reduce information risk, which is the main economic reason behind the demand for audit services (Chadegani et. al., 2011). The development of go-public companies that is growing rapidly, has an influence on an auditor

or KAP, this is influential because every go-public company requires an examination from an independent auditor to audit the financial statements published by the company. The last few years starting from 2017 to 2019 go-public companies experienced a significant increase as recorded on the Indonesia Stock Exchange website.



Source: Data Processed, 2020.

**Figure 1. Development of Go-Public Companies in Indonesia**

The development of go-public companies is increasing, reaching 632 companies in 2019. This brings many benefits, especially in the economic field, but all companies that have been listed on the Indonesian capital market also have obligations that cannot be released. The obligation is to publish the company's financial statements, this aims to provide information to every party in need. Financial statements have meaning about the performance of the company, especially the financial performance of the company (Kasmir, 2012: 7).

Auditor changes are carried out to maintain the reliability of the company's financial statements, and auditor independence (Putra & Suryanawa, 2016). Companies that go public are obliged to publish their financial statements, the financial statements that are prepared must be trusted by stakeholders, to answer this need an independent auditor is needed. Independent auditors are very much needed, so that the financial reports that have been made by management can be trusted by the public and make quality financial reports

in accordance with generally accepted accounting standards (Kholipah & Suryandari, 2019).

The stipulations regarding the change of auditors that have been ratified by the Indonesian government make every company, especially a go-public company, have to change auditors so that the level of auditor independence is maintained so that it does not violate the professional code of ethics in carrying out audit tasks, but in fact, even though the regulations that have been set are so strict, companies that violate regulations are still found. Financial reports published by PT Asuransi Jiwasyara (Persero) at the end of 2019 do not match the truth, the company also changes auditors frequently. Since 2006 – 2014 PT Asuransi Jiwasyara (Persero) has changed auditors 4 times, but the Public Accounting Firm that carried out the audit assignment could not find the problem (Berita Satu, 2019).

Many factors cause companies to change auditors, one of which is financial distress. Financial Distress is a condition that describes that an entity is experiencing financial difficulties. The occurrence of financial distress in a company allows auditor switching to occur in the company (Sari & Astika, 2018). In addition, audit delay is also a factor causing auditor turnover. The audit completion process affects the timeliness of information, to publish financial reports, so this has an effect on related parties (Simatupang, et. al, 2018). The importance of punctuality in completing audits, making a company, will prefer auditors who can complete their responsibilities on time, so that the publication of financial statements is not too late to make the company's image remain good in the eyes of stakeholders.

Many studies related to auditor switching have been carried out, Nasser et. al. (2006); Wea & Murdiawati (2015); Minaryanti and Muchammad (2017) proved that financial distress had an effect on auditor switching, while Kurniaty, et. al. (2014); Augustyvena & Wilopo (2017); and Muawanah (2019) which states that financial distress is not a factor that affects the occurrence of auditor switching. Furthermore, the research of Dwiphayana & Saputra (2019); Yanti & Badera (2018); Hidayati (2018) states that audit delay affects auditor switching. This study wants to prove that financial distress and audit delay affect auditor switching.

## 2. LITERTURE REVIEW

### *Auditor switching*

Auditor switching is an activity of changing auditors or KAP, which occurs in a company (Sari & Astika, 2018). Karina, et. al (2014) define auditor switching is an important decision in a client company and must be considered wisely about which auditor will be selected to partner with the client company. In addition, auditor switching is an action, taken by the company, to change the KAP or auditor in maintaining public trust and the level of auditor independence (Kusuma & Farida, 2019). In other words, it can be said that auditor switching is an action/decision taken by the client company to switch KAP/auditor, in terms of conducting audit assignments for the company with the aim of increasing the independence between the Public Accounting Firm and the client company.

### *Financial Distress*

Financial distress is an increase in excessive debt (Szilagjova, 2015), then Ally and Bwana (2019) say that the condition of financial difficulties that occurs in a company, resulting in failure to carry out operating activities is financial distress. In addition, Abubakar et. al., (2018) defines financial distress as a company's condition, which is unable to pay its obligations. When a company is experiencing financial distress, it can also be seen from the company's treatment in the context of laying off workers, inability to pay dividends, an insignificant amount of cash flow to pay long-term debt (Kusuma & Farida, 2019). In addition, financial distress can be viewed from the composition of the company's balance sheet, L/R reports, and cash flow reports (Kamaludin & Pribadi, 2011).

Financial distress can occur because of a supporting factor both internally and externally, such as total debt, difficulties in cash flow, and losses in operations that occur in a company for several years (Wulandari, 2016). Failure in product promotion activities is an impact that causes companies to be unable to maintain financial performance stability, resulting in decreased income and sales that are not optimal, this is also the cause of financial distress (Assaji & Machmuddah, 2017). When financial distress occurs in a company, management is expected to be able to take the right decision because if

management makes the wrong decision with this condition, it can result in a fatal error, namely the bankruptcy of the company.

### ***Audit Delay***

Audit delay is the time span, from the closing date of the financial statement books to the date of giving the opinion and audit report that has been completed by the auditor (Irman, 2017). According to Santosa & Kurnia (2013) audit delay is a condition that indicates the process of completing the audit report carried out by the auditor. Hidayati (2018) also revealed that audit delay is the time span of audit completion, which is measured from the closing date of the financial year, to the date of completion of the independent auditor's report. Audit delay is an important part for companies because the length or speed of the audit delay will affect the company in issuing financial reports to the capital market (Yanti & Badera, 2018). The right time to publish the company's financial statements to the capital market is also an assessment in the eyes of the public, to see the company's performance, in good or bad condition. Stakeholder decisions in investing are also seen from the accuracy of a company to publish the company's financial statements, if the company is late in publication, the stakeholders will feel suspicious of the company (Robbitasari & Wiratmaja, 2013).

### ***Effect of Financial Distress on Auditor Switching***

Financial distress that occurs in an entity illustrates that the company's financial condition is not healthy. The reason for unhealthy financial conditions is a factor that influences companies to make decisions in the form of auditor switching (Augustyvena & Wilopo, 2017). The condition of the company will be worse if more additional costs occur in the company such as expensive financial costs, project opportunity costs and less productive employees, this will also make the company's ability to decrease, so the company will take action to perform auditor switching, which according to their abilities (Kusuma & Farida, 2019).

A financial position that is experiencing difficulties will increase the evaluation of subjectivity, and caution, in choosing a public accounting firm, and take more action to perform auditor switching, because the company is no longer again have the ability to pay

the audit fees charged by the previous KAP (Kurniaty et. al, 2014). The company's inability to pay its obligations to the auditor creates a sense of insecurity for the company and this can have an effect for the company to perform auditor switching (Kusuma & Farida, 2019). Financial distress is a driving factor, which affects companies to perform auditor switching, this is due to the higher audit fees charged to companies that are experiencing Financial distress makes the company perform auditor switching by choosing a public accounting firm that provides audit services at a cost that is not too high (Wea & Murdiawati, 2015). This is supported by the results of research by Nasser et al. (2006); Wea & Murdiawati (2015); Minaryanti & Muchammad (2017); Puspayanti & Saputra (2018); Kusuma & Farida (2019).

*H<sub>1</sub> : Financial distress affects auditor switching*

### ***Effect of Audit Delay on Auditor Switching***

Audit delay is related to the determination of the company to publish its financial statements in the capital market. Publication of financial statements, for go-public companies, is very important, therefore go-public companies do not want to be late in publishing their financial statements so that the company's image is maintained in the eyes of investors. Every company wants that an auditor can carry out audit tasks on the company's financial statements without experiencing delay. Delay in publishing financial statements will cause negative things, audit delay is also detrimental to users of financial statements such as investors, creditors, the public, the government, and other parties as the basis for accounting decision making (Wiryakriyana & Widhiyani, 2017). Sooner or later an auditor, in carrying out audit assignments, determines the feasibility of the auditor being reused or not, to audit the company's financial statements (Hidayati, 2018). This shows that the audit delay that has a long time will make the company decide to do auditor switching, so that in the following year the company is not too late to publish financial statements, so that it can add investors to invest their funds in the company. This is supported by research by Dwiphayana & Saputra (2019); Yanti & Badera (2018); Pawitri & Yadnyana (2015); Robbitasari & Wiratmaja (2013).

*H<sub>2</sub> : Audit delay affects auditor switching*

### 3. RESEARCH METHODS

The population of this study is all banking companies listed on the Indonesia Stock Exchange from 2016 - 2019 as many as 45 companies. Determination of the sample using purposive sampling technique, with criteria for 2016 – 2019; Banking companies listed on the Indonesia Stock Exchange, consistent listings of banking companies, publish annual financial reports on the company's website or the IDX website, present independent auditor reports, display information related to research variables. Companies that meet the sampling criteria are 37 companies and observed for 4 years, so the number of samples for this study is 148. The procedure for collecting data in this study uses the documentation method. Data collection is by accessing data from the financial statements of banking companies listed on the Indonesia Stock Exchange. The method is carried out by collecting all secondary data from [www.idx.co.id](http://www.idx.co.id).

The dependent variable used in this study is auditor switching. Auditor switching is the transfer of a public accounting firm or auditor (Kusuma & Farida, 2019). This variable uses a dummy variable (categorical variable), if the client company performs auditor switching, it is given a value of 1, and if the client company does not perform auditor switching, it is given a value of 0 (Nasser et. al., (2006); Lin & Liu (2010)); Augustyvena & Wilopo (2017); Sari & Astika (2018); Manto & Wanda (2018)). The independent variables in this study are financial distress and audit delay. Financial distress is proxied by the ratio of DER (Debt to Equity Ratio),  $DER = (\text{Total Debt}) / (\text{Total Equity}) \times 100\%$ . Audit delay uses a Dummy variable, if the client company experiences audit delay = 1 and if the client company does not perform auditor switching = 0.

### 4. RESULTS AND DISCUSSION

This study uses descriptive analysis and statistical analysis using logistic regression analysis equations.

### *Descriptive Analysis*

Descriptive statistical analysis was used to provide an overview of the sample data studied. Data management for descriptive statistical analysis using IBM SPSS Statistics 26. The following are the results of descriptive statistical analysis for each variable:

**Table 1**  
**Descriptive Statistic**

	<b>N</b>	<b>Minimum</b>	<b>Maximum</b>	<b>Mean</b>	<b>Std. Deviation</b>
Financial Distress	148	1.53	14.75	5.9938	2.50275
Audit Delay	148	0	1	.06	.240
Auditor Switching	148	0	1	.57	.497
Valid N (listwise)	148				

Source: Output SPSS 26

Based on the descriptive statistical table 1 above, the results of the descriptive analysis of the variables are as follows:

#### *Auditor Switching*

The dependent variable, namely auditor switching, was measured using a dummy variable. Companies that perform auditor switching will be given a value of one (1), while if the company does not perform auditor switching it will get a value of zero (0). Based on the results of descriptive statistical analysis, the lowest value on the dependent variable is zero (0), while the highest value is one (1). The average value of the auditor switching variable is 0.57 which means that the auditor switching is carried out in banking companies by 57% and the remaining 43% does not do auditor switching. The standard deviation of 0.49 indicates that the average value is greater than the deviation value, meaning that banking companies listed on the Indonesia Stock Exchange in 2016 – 2019 performed more auditor switching.

#### *Financial Distress*

The financial distress variable (X1) is proxied by the DER ratio (Debt to Equity Ratio). The minimum value of the financial distress variable is 1.53 and the maximum value is 14.75. The average value of financial distress is 5.99. This illustrates that 5.99% of



companies are experiencing financial difficulties and the remaining 94.11% are not experiencing financial difficulties. The standard deviation value of the financial distress variable is 2.50 which explains that the average value of the financial distress variable is smaller than the standard deviation value, which means that there are fewer financial difficulties in banking companies listed on the Indonesia Stock Exchange in 2016 – 2019

### ***Audit Delay***

The Audit Delay Variable (X2) is a dummy variable. Number one (1) explains that the company experiences audit delay and zero (0) explains that the company does not experience audit delay. The highest value of audit delay is one (1) and the lowest value is (0). The audit delay variable has an average value of 0.06, meaning that 6% of banking companies listed on the Indonesia Stock Exchange in 2016 – 2019 experienced audit delays. The standard deviation value is 0.24 which shows that the average value is smaller than the standard deviation, this means that the audit delay that occurs in banking companies listed on the Indonesia Stock Exchange in 2016 – 2019 is less.

### **Hypothesis testing**

Hypothesis testing was carried out using a logistic regression model to examine the effect of financial distress and audit delay on auditor switching in banking companies for the 2016-2019 period. The stages in the hypothesis testing process are as follows:

#### **Assessing the Overall Model (Overall Model Fit)**

Assessing the overall model of the model is used to determine the fit of the model with the data. The hypotheses for assessing model fit are:

H<sub>0</sub> : The model is hypothesized to fit the data

H<sub>a</sub> : The hypothesized model does not fit the data

This means that H<sub>0</sub> must be accepted so that the model fits the data (Ghozali, 2018). Testing in this model is done by comparing the value between the initial -2 log likelihood (-2LL) (block number = 0) with the final -2 log likelihood (-2LL) (block number = 1). If in the test results there is a decrease in value between the initial -2 LL (Block Number = 0) and the final -2LL (Block Number = 1), it indicates that the hypothesized model fits the

data. The decrease in the Log Likelihood value explains that the regression model used is getting better. The following are the results of the model fit test:

**Table 2**  
**Fit 1 Test Results (Block 0 : Beginning Block)**

Iteration	Iteration History		Coefficients Constant
		-2 Log likelihood	
Step 1	1	202.461	.270
0	2	202.461	.272
	3	202.461	.272

Source: Output SPSS 26

**Table 3**  
**Test Fit 2 (Block 1: Method = Enter )**

Iteration	Iteration History			Coefficients	
		-2 Log likelihood	Constant	Financial Distress	Audit Delay
Step 1	1	200.501	.071	.024	.868
	2	200.468	.067	.025	1.003
	3	200.468	.067	.025	1.008
	4	200.468	.067	.025	1.008

Source: Output SPSS 26

Based on table 2 and table 3, it can be seen that there is a decrease in the value of -2 LL in the early stages (Block Number = 0) by 202.46 and in the final stage (Block Number = 1) has a value of 200.50. This means that the model fits the data because there is a decrease in value from the first block to the second block.

**Table 4**  
**Hosmer and Lemeshow Goodness Of Fit Test Results**

Hosmer and Lemeshow Test			
Step	Chi-square	df	Sig.
1	8.097	8	.424

Source: Output SPSS 26

Based on table 4 shows that the Hosmer and Lemeshow test obtained Chi - square of 8.097 with a significance value of 0.424 and df 8. These results show that the significance value is greater than 0.05 so that H0 is accepted and this means that the model used is able to predict the observed value. and the regression model is feasible to use in the next analysis stage.

**Table 5**  
**Results of the Coefficient of Determination**

Step	Model Summary		
	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	200.468 <sup>a</sup>	.013	.018

Source: Output SPSS 26

Table 5 explains that the Nagelkerke R Square value is 0.018 (1.8%) and the Cox & Snell R Square value is 0.982 (98.2%). This shows that the independent variables of financial distress and audit delay are able to explain the dependent variable, namely auditor switching by 1.8%, while the rest is explained by other factors outside the research model.

### Testing Regression Feasibility

The second stage of logistic regression analysis is to test the feasibility of the regression. Feasibility testing using the Goodness of Fit Test. If the statistical value of Hosmer and Lemeshow Goodness of fit Test is greater than 0.05, then the null hypothesis can be accepted and means that the model is able to predict the value of its observations (Ghozali, 2018). The statistical results of Hosmer and Lemeshow Goodness of fit Test are as follows:

**Table 6**  
**Hosmer and Lemeshow Goodness Of Fit Test**

Step	Hosmer and Lemeshow Test		
	Chi-square	df	Sig.
1	8.097	8	.424

Source: Output SPSS 26

Based on table 6 the results show that the Hosmer and Lemeshow test obtained Chi - square of 8.097 with a significance value of 0.424 and df 8. These results show that the significance value is greater than 0.05 so that H0 is accepted and it means that the model used is able to predict the value observations and regression models are feasible to use in the next analysis stage.

### **Coefficient of Determination (Nagelkerke's R<sup>2</sup>)**

The next stage of analysis is the coefficient of determination test (Nagelkerke's R<sup>2</sup>). The coefficient of determination test was conducted to find out how much the independent variables, namely financial distress and audit delay, were able to explain the dependent variable, namely auditor switching. The coefficient of determination in logistic regression can be seen from the value of Nagelkerke R Square. The results of the coefficient of determination can be seen as follows:

**Table 7**  
**Coefficient of Determination Results**

Step	Model Summary		
	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	200.468 <sup>a</sup>	.013	.018

Source: Output SPSS 26

Table 7 explains that the Nagelkerke R Square value is 0.018 (1.8%) and the Cox & Snell R Square value is 0.982 (98.2%). This shows that the independent variables of financial distress and audit delay are able to explain the dependent variable, namely auditor switching by 1.8%, while the rest is explained by other factors outside the research model.

### **Testing the Regression Coefficient**

Testing the regression coefficient is the last stage in logical regression analysis. Regression coefficient test can be done by looking at the variables in the equation column and comparing the significant column with an error rate of 0.05 (5%). If the level < 0.05 then H0 is accepted. The following table of variables in the equation:

**Table 8**  
**Regression Coefficient Test**

		Variables in the Equation					
		B	S.E.	Wald	Df	Sig.	Exp(B)
Step 1 <sup>a</sup>	Financial	.025	.068	.139	1	.709	1.026
	Distress						
	Audit Delay	1.008	.823	1.501	1	.221	2.741
	Constant	.067	.435	.024	1	.877	1.070

Source: Output SPSS 26

Based on table 8 above, the logistic regression model obtained is as follows:

$$\text{SWITCH} = 0,067 + 0,025 + 1,008 + e$$

### *Discussion*

#### *Effect of Financial Distress on Auditor Switching*

The results showed that the financial distress variable obtained a significant value of 0.709 which was greater than 0.05 (5%), this indicates that financial distress has no effect on auditor switching. The good or bad financial condition of the company describes the company's condition. Financial distress has no effect on auditor switching because if auditor switching is carried out by a company that is experiencing financial distress, it will result in higher audit fees. The results of this study are supported by the research of Kurniaty, et. al (2014), Augustyvena & Wilopo (2017), Safriliana & Muawanah (2019). When there is financial distress in a company, sometimes it is better for the company to improve its financial condition compared to changing auditors, because the initial costs incurred by the company to find a new auditor are very high, so sometimes the company will retain the old auditor (Augustyvena & Wilopo, 2017). In addition, when the company prefers a new auditor, it will allow a high error rate because this is the first assignment (Hidayati, 2018).

#### *Effect of Audit Delay on Auditor Switching*

The test results on the audit delay variable show a positive coefficient of 1.008 with a significant level of 0.22. The significant level of the audit delay variable is greater than

0.05 (5%), this indicates that the audit delay variable has no effect on auditor switching. This is because most of the banking companies that were sampled in this study did not experience audit delay, so there were not many companies that did auditor switching. The sooner or later the completion of an auditor to complete the independent auditor's report will affect the company to switch to another auditor or remain with the old auditor, but this statement is not always the case. As long as the auditor completes the independent auditor's report, it does not exceed the number of days set by BAPEPAM-LK, it will allow the company to think again if it wants to replace its independent auditor (Hidayati, 2018). Therefore, as long as the auditor's report completion time does not exceed ninety days, the company will retain the old auditor.

## 5. CONCLUSIONS

Financial distress and have no effect on auditor switching in banking companies listed on the Indonesia Stock Exchange in 2016-2019, The good or bad financial condition of the company describes the company's condition, financial distress has no effect on auditor switching because if auditor switching is carried out by a company that is experiencing financial distress, it will result in higher audit fees.

Audit delay have no effect on auditor switching in banking companies listed on the Indonesia Stock Exchange in 2016 -2019, The sooner or later the completion of an auditor to complete the independent auditor's report will affect the company to switch to another auditor or remain with the old auditor, but this statement is not always the case.

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