

The Determinant Of Audit Fee For Micro, Small And Medium Enterprise : Evidence From Indonesia

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Abstract

The importance of this research is conducted to determine the determinants of audit fees to micro, small, and medium enterprises in Indonesia. This research uses multiple regression analysis. The research sample of 444 public accounting firms in Indonesia at 104 MSMEs. The results showed that company size variables affected audit fees, profitability affected audit fees, company risk influenced audit fees, company complexity affected audit fees, industry influenced audit fees, Public Accountant Office status affected to audit fees, and audit report lag affects the audit fee.

Keywords: *Audit Fee, Small and Medium Micro Business, Public Accounting Firm*

Introduction

In the Era of Globalization, the field of accounting is the field that plays the most role in decision making by companies, especially financial statements (Arsyad & Ghozali, 2017). Therefore to improve the credibility and quality of financial reports, external audits are needed (Beasley & Salterio 2001; Hallak & Silva 2012), audited financial statements can reduce information asymmetry and conflicts between managers and stakeholders (Bealty 1989; Willenborg 1999). However, audit quality can be measured by the amount of audit fees paid by companies to external auditors (Hallak & Silva, 2012). In addition, agency theory also shows that the separation between ownership and management creates conflict between managers who might be involved in activities for personal and stakeholder interests (Hassan & Naser 2016).

Determination of the external audit fee is based on a contractual agreement between the auditor and the auditee according to the time spent in an audit process, the services required and the number of staff needed for the audit process (Gammal, 2012; Willy, 2016; IAPI, 2016). In this context, Angelo (1981) also believes that audit costs correlate with audit quality, the reason being that shareholders are willing to pay high audit fees to obtain high audit quality (Choi et al., 2010). However according to IAPI (2016), that the fees for auditing financial statements that are too low can pose a threat to personal interests which has the potential to cause non-compliance with the professional public accountant's code of ethics, therefore public accountants must make precautions by applying a service fee for auditing adequate financial statements, so that it is sufficient to carry out adequate audit procedures, even in order to realize me Public integrity with integrity, quality, and competing with international standards, encourages the independence of a healthy and conducive profession for the public accountant profession and maintains the dignity of public accountants and public trust.

Therefore, this study was conducted to investigate empirically the factors that affect the determinants of audit fees for the company's SME sector. This research was conducted because, firstly, it helped and expanded the existing literature, due to the limitations of the determinants of audit fees in Indonesia, let alone the audit fee standards in Indonesia based on working hour rates, Secondly, helped the Public Accountant Organization in Indonesia in making policies to determine how many standards ideal audit fee, Third, Encourage to add a Public Accounting Firm in Indonesia, so that the ratio between MSME sector companies is comparable to the Public Accounting Firm in Indonesia and there is no longer an imbalance between demand and supply. Fourth, examine the extent to which Law No. 40 of 2007 concerning the obligation of MSME sector companies to be audited with the aim of financial statements to be transparent and accountable, although so far the MSME sector companies are not obliged to publish their financial statements. This research is motivated by audit market interests (Gerakos & Syverson, 2013), where the audit market aims to

create transparency and improve capital markets (Watts & Zimmerman, 1993; Ball, 2001), besides that in Indonesia all companies are required to be audited (SPAP, 2011).

Research related to audit fees that have been carried out is still limited to companies listed on the Indonesia Stock Exchange, while research conducted on the micro and small business sector (MSME) is still very rarely done. This research aims to determine the determinants of audit fees for micro, small, and medium enterprises in Indonesia. The determinants of audit fees include Company Size, Profitability, Risk, Company Complexity, Industry, Public Accountant Office Status, and audit report lag.

Literature Review

Relationship of Company Size with audit fees

Company size is one of the main attributes used by most researchers before determining what determines audit fees. It is found that large companies tend to pay higher audit fees than small companies (Anderson & Zeghal 1994; Mike et al., 1997; Ashbaugh et al., 2003; Whisenant, et al., 2003; Naser & Nuseibh, 2008; Ellis & Booker 2011; Hassan and Nase, 2013; Ulhaq & Leghari, 2015). Large companies also tend to disclose more financial and non-financial information (Cornier & Magnan, 2003; Othman et al., 2009). In addition, large companies are expected to initiate transactions that are more in number and value than those carried out by smaller companies and will have the resources to recruit prestigious external auditors (Palmrose, 1986; Carson et al., 2004; Vermeer et al., 2009). As a result, external auditors require more audit effort and time to audit large companies, and audit fees are also high. In a variety of literature, the proxy used to measure firm size is total assets (Owusu, Ansah, 1998; Menara et al, 1999; Nasser et al, 2002; Haniffa & Cooke, 2005; Barako et al, 2006; Othman et al, 2009; Khan, 2010; Prencipe, 2004; Rouf, 2011; Hassan, & Naser 2016; Alhassan, 2017; Nishtiman, et al, 2018; Aliu, et al; 2018).

Relationship of Profitability to audit fees

Many previous studies have revealed that companies report higher profits, because it will show the efficiency of company management in allocating available resources, and company management tends to reveal more information to see the company's performance and reduce agency costs (Watts & Zimmerman, 1986) and to strengthen position and compensation (Inchausti, 1997). The company will disclose more information about its activities in increasing auditor risk, and this will lead to an intensive audit of revenue audits and company expenses, which will increase audit fees (Joshi & Albastaki, 2000). External auditors are expected to conduct intensive tests of performance, which will be used as a basis in the company's compensation system (Zukarnain & Shamsheer, 2008). Previous research uses Profitability with Net Profit Margin Proxies (Alburime, 2009; Amba & Almurkharreq, 2013; Return on assets (ROA) (Alanazi et al, 2011; Tamimi and Charif, 2011; Hassan & Naser 2016; Alhassan 2017) and Return on assets (ROA) Equity (Tamimi & Charif, 2011).

Relationship of Company Risk to audit fees

According to agency theory, companies with very high levels of leverage must disclose more information in order to meet the needs of their creditors (Jansen & Meckling, 1976). In general, the company's capital structure is directed to be stable because the leverage ratio measures the level of company risk. Companies will run the risk of bankruptcy if they fail to meet short-term obligations, including short-term obligations that originate from loan interest. Therefore, the external auditor will take more time in the audit period to conduct the examination. The more time spent in the process, the higher the audit fee. Thus, company risk is positively related to audit fees (Francis & Simon, 1987; Craswell & Francis, 1999; Simunic 1980; Francis & Stokes, 1986; Josh & Bastaki, 2000; Gonthier, Besacier & Schatt, 2007). However, some other researchers showed no influence between company risk and audit fees (Vermeer et al., 2009; Ellis & Booker, 2011). In this study, company risk is indicated by total debt to total assets (Coulter, 2015; Bukair & Abdul Rahman, 2016; Hassan, Y, & Naser, K, 2016).

Relationship of complexity to audit fees

One dominant determinant of audit fees is complexity. Researchers are even aware of a significant and positive relationship between client complexity and audit fees (Simunic, 1980; Brinn

et al., 1994; C Exhibition, 2005; Josh & Bastaki, 2000; Clatworthy & Peel, 2006; Thinggaard & Kiertzner, 2008; Vermeer et al., 2009; Ellis & Booker, 2011; Verbruggen et al, 2011). This is reasonable because companies with more extended audit periods with uncomplicated companies require high audit fees (Sandra & Patrick, 1996; Hoitash et al., 2007; Hackenbrack & Knechel, 1997). In addition, auditors can be exposed to professional liability claims more when compared to uncomplicated auditing companies (Clatworthy & Peel, 2006). In the literature, complexity is measured by the number of products, the geographical place of the client, the proportion of foreign assets and the number of business segments. However, in this study the complexity of the indicators measured by the number of subsidiaries and a number of foreign subsidiaries (Hay et al, 2006; Hey, 2013; Coulier, 2015; Hassan and Naser 2016).

Industry type for audit fees

The type of industry is also one indicator of determining audit fees. Certain types of industries require sufficient time compared to other industries. This will result in higher audit fees compared to other industrial companies (Firth, 1985; Anderson & Zeghal, 1994). For example, manufacturing companies are more likely to disclose information than non-manufacturing companies (Camfferman & Cooke, 2002, Naser & Nuseibeh, 2008). Financial statements prepared by manufacturing companies are more complete than non-manufacturing financial statements, so companies ask for better audit quality, even manufacturing companies are more sensitive to the environment (Klassen & Whybark, 1999). Manufacturing companies can also social pressure from the community, so manufacturing companies must report on their social and environmental responsibilities to avoid pressures and regulations (Hackston & Milne, 1996; Tagesson et al., 2009), (Hassan, Y, & Naser, K, 2016). Therefore manufacturing companies hire high-quality external auditors, so that audit fees are also high.

Status of the Public Accounting Firm on audit fees

Public accounting firms affiliated with foreign countries have high audit quality (Lennox, 1999). Public accounting firms that audit large companies are also higher than small companies and usually better than public accounting firms that audit small companies (Hay et al., 2006), so public accounting firms that audit small companies are considered to be still small (Angelo, 1981; Haniffa & Cooke, 2002; Glaum & Street, 2003). Affiliated public accounting firms are expected to be of high quality because they already have a reputation (Becker et al., 1998; Jien et al., 2013). The reputation of its affiliated public accounting firm does not provide low audit quality (Angelo, 1981). Affiliated public accounting firms also provide high-quality services in order to minimize or avoid the risk of audit failure (Dye, 1993), (Hassan, & Naser, 2016).

Audit Lag Report on audit fees

Audit report lag is the period of time between the end date of the accounting year compared to the date of the audit report. Audit report lag has a positive effect on audit fees (Ghosh & Pawlewicz, 2009). When the client or company is constrained by financial difficulties, including difficulties in audit evidence, so that material errors that occur are greater and more complicated, then the external auditor also takes more time, resulting in a large audit fee (Bamber et al., 1993). Some audit report lag research is also a determinant of audit fees (Chan et al., 1993; Ezzamel et al., 1996; Hassan & Naser, 2013; Hassan & Naser, 2016).

Methodology

Descriptive statistical analysis is a descriptive technique that provides information about the data held and does not intend to test the variables in this study. This analysis is only used to present and analyze data along with calculations in order to clarify the condition or characteristics of the relevant data. Measurements used by this descriptive statistic include the number of samples, minimum value, maximum value, mean value, and standard deviation (Ghozali 2011). Regression analysis in this study was conducted to prove the relationship of determinants between auditing of company size, profitability, risk, company complexity, industry size, KAP status, and audit report lag. The research test was carried out by multiple regression analysis. The samples in this study were 104

Micro, Small, and Medium Enterprises by checking financial statements at public accounting firms in Indonesia.

Results and Discussion

The results of descriptive statistics in this study, namely, show in tables 1 and 2. Descriptive statistics for continuous variables (Table 1) while descriptive statistics for discontinuous variables (Table 2). Audit fees with a minimum value range from 6.30 to 8.14 with an average value of 7.24. The average value for company size calculated using the natural logarithm of the company's total assets is 9.97. The profitability value ranges from -11.57 to 7.41, with an average value of 0.11. The audit report lag variable has an average of 102 days to complete an audit of the sample company's financial statements. Table 2 shows the majority of the sample of companies audited by non-affiliated KAP with a figure of 89.4%. Only about 10.6% of the sample of companies audited by affiliated KAP. Industry variables show that there are 40 industries, while 64 others are not industries. The complexity of the company shows that the majority of the sample does not have a subsidiary, only about 4.8% of the sample has a subsidiary.

Table 1: Descriptive statistics of continuous variables

Variable	Mean	SD	Minimum	Maximum
Size	9,97	0,75	8,00	12,02
Prof	0,11	1,48	-11,57	7,41
Risk	0,38	0,30	0,00	1,00
ARL	101,85	119,26	0,00	554,00
Adfees	7,24	0,22	6,30	8,14

Table 2: Descriptive statistics of discontinuous variables

Variable		Frequency	Percentage	Accumulated Percentage
Aust	KAP Affiliation (0)	11	10,6	10,6
	Non Affiliation (1)	93	89,4	100,0
Inds	Industry (1)	40	38,5	38,5
	Non-Industry (0)	64	61,5	100,0
Comp	Has a subsidiary (1)	5	4,8	4,8
	Non Has a subsidiary (0)	99	95,2	100,0

Table 3 shows the Pearson Correlation test used to find multicollinearity problems in this study. It can be seen that the highest significant value is found in the risk variable for the company size variable, 0.425, and the industry variable for audit report lag variable, which is 0.221. Because all correlation coefficients between independent variables are less than 0.8, multicollinearity is not a severe problem in the interpretation of regression findings (Bryman and Cramer, 2005). Furthermore, the value of the Variance Inflation Factor (VIF) for all variables is shown in table 4. The VIF value for all variables is far below the critical value of multicollinearity, which is 10. Thus, multicollinearity is not a severe problem in the interpretation of regression results (Neter et al., 1983).

Table 3: Correlations between variable

Variable	Size	Prof	Risk	Aust	ARL	Inds	Comp	Adfees
Ukuran	1							
Prof	0,056	1						
Resiko	0,425**	0,075	1					
Aust	-0,296**	-0,085	-0,081	1				
ARL	-0,063	-0,169	0,021	0,161	1			
Inds	-0,011	0,124	0,070	-0,114	0,221*	1		
Comp	-0,061	0,005	-0,028	0,077	-0,030	0,007	1	
Adfees	0,487**	0,014	0,243*	-0,441**	-0,102	0,287**	-0,059	1

** . Correlation is significant at the 0.01 level (2-tailed).
* . Correlation is significant at the 0.05 level (2-tailed).
$R^2 = 0,412$
Adj. $R^2 = 0,369$
F= 9,622

The regression results are shown in Table 4. The F value in the first model is 9.622. This value indicates that model 1 is significant. The R2 value is 0.412, indicating that the independent variables simultaneously explain the dependent variable by 41.2%.

Hypothesis 1 states that firm size has a positive effect on audit fees. The findings support the first hypothesis in this study and provide evidence that firm size has a significant positive effect on audit fees. Companies with large total assets will require greater monitoring costs, in this case, the audit fee paid by the company will be greater as well. The results of the study are in line with research conducted (Anderson & Zeghal, 1994; Mike et al., 1997; Ashbaugh et al., 2003; Whisenant, et al., 2003; Naser & Nuseibh, 2008; Ellis & Booker, 2011; Hassan and Nase, 2013 ; Ulhaq & Leghari, 2015), that large companies tend to pay higher audit fees than smaller companies. Many reasons explain that large companies have high agency costs resulting from potential conflicts between management and stakeholders (Inchausti, 1997).

Hypothesis 2 states that the company's profitability has a positive effect on audit fees. The results state, the higher the level of profitability of the company, the higher the company will allocate available resources so that it can improve performance and reduce agency costs. The results of the study are not in line with research conducted by (Joshi & Albastaki, 2000), companies that will disclose more information about their company's activities in increasing auditor risk will cause an audit of the intensive audit of company revenues and expenses which will increase audit fees. Meanwhile, research conducted (Zukarnain & Shamsheer, 2008) states that external auditors are expected to conduct intensive tests of performance that will be used as a basis in the company's compensation system.

Hypothesis 3 states that firm risk positively influences audit fees. This states that the high level of risk a company takes in carrying out the audit will require a long time in conducting the audit so that it has an impact on audit fees. This research is also in line with research conducted by (Francis & Simon, 1987; Craswell & Francis, 1999), (Simunic, 1980; Francis & Stokes, 1986; Josh & Bastaki, 2000; Gonthier Besacier & Schatt, 2007), states increasingly the length of the audit period will further increase the risk to the company and impact on the audit fee.

Hypothesis 4 states that company complexity has a positive effect on audit fees. This states, the higher the level of complexity of the company in the examination, it will increase the audit fee. The results of this study are in line with research conducted by (Sandra & Patrick, 1996; Hoitash et al., 2007; Hackenbrack & Knechel, 1997), which states the complexity of the company can be seen from the company's indicators in the form of geography, company assets, while the results of research conducted (Rukmana et al 2017; Cristansy & Ardiati 2018) who also did not find a relationship between company complexity and audit fees.

Hypothesis 5 states that the type of industry has a positive effect on audit fees. This states, differences in companies that will be audited will have an impact on the disclosure of information. This research is in line with research conducted by (Firth, 1985; Anderson & Zeghal, 1994), stating that the type of industry requires sufficient time compared to other industries in conducting audits so that it influences audit fees. This can also be seen from the difference in the types of companies disclosed by (Klassen & Whybark, 1999). The financial statements prepared by manufacturing companies are more complete than the non-manufacturing financial statements, so companies ask for better audit quality, even manufacturing companies are more sensitive to the environment.

Hypothesis 6 states that KAP status has a positive effect on audit fees. This states, the status of the Public Accounting Firm in conducting an audit greatly affects the type of industry, audit quality, and audit fees. This research is in line with research conducted by, (Hay et al, 2006; De Angelo, 1981; Haniffa & Cooke, 2002; Glaum & Street, 2003), Public accounting firms that audit large companies are also higher than smaller companies and are usually better compared to public accounting firms

that audit small companies, so public accounting firms that audit small companies are considered to be still small.

Hypothesis 7 states that audit report lag has a positive effect on audit fees. This states the length of the audit completion at the company due to the level of risk in the financial statement check so that it can increase the audit fee. The results of the study are in line with research conducted by Nasser and Nuseibeh (2008), companies that have long audit report lag usually have problems in their financial statements. This occurs because it takes a long time and extra effort to resolve the company's financial statement problems, thereby increasing fees an audit. So the longer the audit time, the greater the audit fees set by the Public Accountant Office (Herwaty, 2011) while research conducted by (Hoffman and Nagy, 2017; Craswell and Francis, 1999) states that the level of risk to audit report lag does not affect audit fees.

Conclusion

Audit fees are important in the process of auditing a financial statement. Some of the factors that influence companies to incur audit fees for auditing services of a financial statement are company size, company profitability, company risk, complexity, industry type, and KAP status. This study uses a sample of 104 MSMEs in Indonesia. The results of this study indicate that company size and company risk have a significant relationship to audit fees, while company profitability, complexity, type of industry, and KAP status do not have a significant relationship.

Suggestions for the development of this research is to add other factors that can affect audit fees and add samples by being able to collaborate with P2PK to be able to retrieve data for more and know widely about audit fees paid by companies.

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