

The Influence of Internal Audit Activities and Business Complexity on the Amount of Fees for External Auditors (Case Study of Manufacturing Companies on the IDX)

Arum Ardianingsih*, Hidayatul Affifah

Universitas Pekalongan, Indonesia

Info Articles

Abstract

Keywords:

The amount of fees for external auditors, internal audit activities

An audit is a supervision activity and evaluation of the effectiveness of internal control and the reasonableness of the financial statements. The purpose of the audit is to add the value to the company's operations and improve the reliability of financial reporting. Internal audit activities provide company business risk information to external auditors so as to reduce the scope of the audit and have an impact on the amount of fees for external auditors. Companies that are increasingly complex businesses owned also make the completion of the audit longer, as a result the amount of the fees for auditor services rises. This study wants to examine the effect of internal audit activity and business complexity on the amount of fees for external auditor services. The analysis technique uses classical assumption test, multiple linear regression and hypothesis testing. This study found that internal audit activity did not have a effect on the amount of auditor fees. While the complexity of the business has a positive effect on the amount of auditor fees.

*Address Correspondence:

E-mail : arumbundavina@gmail.com

INTRODUCTION

The contemporary business era has changed the business order to be borderless and increased business risk. Conflicts of interest between shareholders, company management, employees and parties within the company's circle itself have increased the risk of this business, so an independent party is needed to bridge this matter. External auditors are independent parties outside the company whose job is to check the fairness of the company's financial statements so as to minimize the occurrence of fraud. External auditors or independent auditors are needed by companies because many business decisions are based on independent auditor reports. The external auditor's duties and responsibilities are quite large, making the company provide compensation for audit services. In determining the amount of compensation for audit services, the auditor must pay attention to several things such as the responsibilities attached to the audit task, the complexity of the transaction or the complexity of the business division, the expertise and knowledge of the company being audited.

The amount of fees for auditor services has been determined through the bargaining power between the company as a client and the auditor as an examiner of the company's financial statements. The amount of auditor fees is sometimes too low or too high because there is no standard for auditor fees, so it is feared that it will have an impact on the quality of the audit results provided. In 2016, the Indonesian Institute of Certified Public Accountants (IAPI) issued Decree No. KEP.95/IAPI/II/2016 contains aspects that are taken into account in determining the fee for auditor services such as the size of the company, transaction complexity and business complexity, the competence of the auditor to enter into carrying out his audit duties. This IAPI decision letter provides a standard for the amount of auditor fees and ensures that the audit carried out has been running well. Empirical evidence shows that audit fees can be influenced by auditor concentration ratios, public accounting firm size, firm size and number of subsidiaries (Suharli and Nurlaelah, 2008).

An audit conducted by an external auditor usually considers a recommendation report as a result of an audit that has been carried out by an internal audit. The company's internal control is usually carried out by internal audit. The supervisory activities carried out by the internal auditors include monitoring the effectiveness of the company's internal control, projects or work programs, ensuring the achievement of company objectives as reflected in the company's financial statements. External auditors and internal auditors have responsibilities, goals, qualifications and duties in different activities, but both must coordinate with each other so that audit results can be of high quality and can be used for company business decision making. The internal audit activity assists the external auditor in identifying significant risks and the effectiveness of internal control which in turn has an impact on determining the amount of fees for external auditors' services. The research of Hapsari and Laksito (2013) found that the number of audit objects audited by the internal audit unit for 1 period had influenced the audit fees paid by the company. Rahayu (2017) found something different, namely internal audit, which was seen from the number of internal audit members in the company, did not affect the audit fee.

One of the internal audit activities is to supervise the complexity of business transactions and the complexity of the company's business. In general, companies listed on the Indonesia Stock Exchange (IDX) have many business divisions or subsidiaries. The complexity of the business seen from the number of subsidiaries has been able to make the scope of audits carried out by external auditors wider. The complexity of business transactions in each parent and subsidiary means that the external auditor's duties and responsibilities are getting bigger. So that the amount of external auditor fees charged by the company is getting bigger. Okta's research (2016) on business complexity which is calculated on a dummy basis where (1) means having a subsidiary, while (0) not having a subsidiary turns out to be considered in determining the audit fee. This study tries to proxy the complexity of the business by looking at the number of subsidiaries owned by the company. Because subsidiaries can reflect the complexity of business transactions, it increases the scope of the audit. So the possibility of an external auditor fee will increase. Meanwhile, according to Hay, et.al(2006) suggests that when the complexity of the client is higher, the audit becomes more challenging and requires a longer completion time so that it has an impact on the amount of remuneration for external auditors' services. These phenomena are a reference for researchers to propose problem formulations (1) Can internal audit activities affect the amount of remuneration for external auditors' services?. (2) Can the complexity of the business affect the amount of remuneration for external auditors? The purpose of this study is to provide empirical evidence that internal audit activities and business complexity in manufacturing companies on the IDX have an influence on the determination of the amount of remuneration for external auditors.

METHODS

The research conducted is a type of causal research or cause and effect. This study identifies a

causal relationship between variable x and variable y or how variable x affects variable y (Sugiyono, 2013). There are 2 independent variables (X) in this study, namely internal audit activity (X1) measured from the frequency of supervision carried out by internal audit so as to provide added value for company operations. Meanwhile, the X2 variable is the complexity of the business as measured by the number of subsidiaries. The dependent variable (Y) in this study is measured by the logarithm of the external auditor's fee. The object of research is a manufacturing company listed on the Indonesia Stock Exchange (IDX). The sample criteria are (1) manufacturing companies that are listed consecutively during 2016-2018, (2) companies that issue annual reports and have been audited by external auditors, (3) financial statements include the amount of fees for external auditors, internal audit activities and has subsidiaries. The data analysis technique used classical assumption test, multiple linear regression analysis and hypothesis testing.

RESULTS AND DISCUSSION

This research was conducted on the audited annual reports of manufacturing companies listed on the Indonesia Stock Exchange (IDX). The observation period in this study was 2016-2018. The research sample amounted to 51 consisting of 17 manufacturing companies during the 2016-2018 period, presented in the table as follows:

Table 1. Company Sample List

Code	Company Name
ADES	PT. Akasha Wira International Tbk
AKPI	PT. Argha Karya Prima Industry Tbk
ALMI	PT. Alumindo Light Metal Industry Tbk
AMFG	PT. Asahimas Flat Glass Tbk
DVLA	PT. Darya-Varia Laboratoria Tbk
ICBP	PT. Indofood CBP Sukses Makmur Tbk
IMPC	PT. Impack Pratama Industri Tbk
INDF	PT. Indofood Sukses Makmur Tbk
KDSI	PT. Kedawung Setia Industrial Tbk
KLBF	PT. Kalbe Farma Tbk
LMSH	PT. Lionmesh Prima Tbk
MBTO	PT. Martina Berto Tbk
MLBI	PT. Multi Bintang Indonesia Tbk
SMSM	PT. Selamat Sempurna Tbk
TCID	PT. Mandom Indonesia Tbk
UNVR	PT. Unilever Indonesia Tbk
WSBP	PT. Waskita Beton Precast Tbk

Classical assumption test results

The classical assumption test in this study consisted of normality test, multicollinearity test, heteroscedasticity test and autocorrelation test. The normality test shows a significance value of 0.145 and the value of kolmogorow-smirnov is 0.151 so that the data is said to be normally distributed. The result of the tolerance value for the internal audit activity variable is 1,977 with a VIF value of 1,023 while the business complexity variable is 1,975 with a VIF value of 1,021. This means that there is no multicollinearity. The results of the heteroscedasticity test using the glejser test show a significance value for the internal audit activity variable of 0.592 and business complexity of 0.057 so there is no heteroscedasticity because the sig value is above 0.005. Autocorrelation test using durbin watson obtained a value of 2,391 so that there is no autocorrelation.

The Influence of Internal Audit Activities on the External Auditor Fees

Based on the regression test, the results obtained a significance value of 0.856 with a coefficient of -0.004. So that the internal audit activity does not have a negative effect on the amount of fees for external auditors' services. Internal audit activities owned by publicly listed companies have met the requirements set by the stock exchange to carry out internal supervision. Because the internal audit activity is related to the supervision of the company's operations, supervision of the effectiveness of the company's internal control, significant business risks that need to be watched out for so that the company's goals can be achieved. Internal audit activities are also related to oversight of company policies and rules, company work programs and good governance systems. When internal audit activity increases, external auditors can use information from internal audit related to significant risks in the company. This will reduce the

need for the scope of the audit to be carried out by the external auditor, thereby reducing the amount of the auditor's fee. This study supports the research conducted by Dita (2017) and Rahayu (2017) about the internal audit function having no effect on the determination of audit fees.

The effect of business complexity on the amount of external auditor fees.

The results of the regression test obtained a significant value of 0.000 with a coefficient of 0.071. This means that companies that have a high business complexity will make the amount of compensation for external auditor services high as well. The bigger the company, the more likely it is that there are more and more subsidiaries that are scattered. Because the complexity of the business refers to the complexity of the transactions that occur between the parent and the subsidiary. The complexity of this relationship makes the duties and responsibilities of the audit scope of the auditor increase. As a result, the amount of service fees set also increased. This research is in line with Okta's (2016) research which states that the number of subsidiaries owned has an effect on the determination of the audit fee.

CONCLUSION

Internal audit activities do not have a negative effect on the amount of fees for external auditors' services. Companies with better internal audit controls will reduce monitoring of external auditors, reduce the scope of audits carried out and will not increase audit fees given by companies to external auditors. Business complexity has a positive influence on the amount of remuneration for external auditors. The more complex the client company, the auditor will face a high significant risk, the scope of the audit and audit responsibilities are getting bigger, so that the amount of remuneration for external auditor services will also increase.

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