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The Impact of Auditor Quality, Financial Stability, and Financial Target for Fraudulent Financial Statement

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Abstract. This study analyzes the influence of financial stability, financial targets and the role of the quality of auditors against fraud measures financial statements. This study using purposive sampling and use of the 21 companies that commit fraud recorded in the financial statements of the Financial Services Authority and 21 companies did not commit fraud which includes compass 100 in the Indonesia Stock Exchange using logistic regression analysis. The study found a positive effect of variable quality auditor against fraudulent financial reports, found a negative influence financial stability and financial variables against the target of fraudulent financial statements. Limitation of this study are limited variables and proxy variables used to measure financial targets, further research is recommended to add the variables that affect the occurrence of acts of fraud financial statements, and look for a proxy for a target financial variables.

Keywords: financial stability, financial statement fraud, financial targets, quality auditor

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Introduction

Violations that occurred in the capital market is an offense relating to the opening of issuers and public companies, securities trading and investment management. There are several large companies involved in infringement cases in the capital market including Enron scandal, WorldCom and Xerox that affect public confidence. The same violation was also conducted by PT KAI in its financial reporting present information that is not true is to raise profit in conditions of PT KAI is experiencing losses (Anshori, 2015). Violations often occur not only cheating the financial statements as prepared by PT KAI, based on information from the Financial Services Authority violations which occurred in the capital market consists of manipulation of accounting information, the delay in submission of the report, case related to financial statements, misapplication of accounting principles and the removal of a deliberate accounting information.

Violation of financial fraud can lead to lower the integrity of the financial information that may affect several parties including lenders, investors, employees, auditors, even competitors (Ansar, 2012). Reducing fraud in reporting financial information certainly takes the role of the auditor as a party that can ensure the fairness of the financial statements.

Research on the quality of previous audits have been conducted by Fernando et al. (2011) in his research found that audit quality attributes consisting of the auditor as a member of big 4 and auditor industry specialization negatively affect the cost of capital. Khurana et al. (2004) also found the quality of big 4 impact low cost of capital cost compared to non-big 4. Research conducted by Teoh et al. (1993), Balsam et al. (2003), and Dunn et al. (2004) also have shown that the results of the quality auditor higher yield better information so that the role of audit information shows that the audit will reduce risk through quality better information and a big 4 auditor will reduce capital costs by providing high quality audits with strong supervision than non-big 4 auditor (Fan & Wong, 2005).

Several previous studies have used factor analysis to detect fraud triangle financial statements including Ansar (2012) and Martantya (2013), whose results find two (2) of the fraud triangle factor is financial stability and financial targets significant effect on the financial statements fraud. This study will test empirically two of the fraud triangle factor is whether the factor of financial stability and financial targets cheating influential in the financial statements.

The study also aims to test and analyze whether the quality of the big 4 auditor can reduce the amount of financial statement fraud. Researchers also use variables financial stability and financial targets in determining whether a variable is more significant to the financial statements fraud measures.

Literature Review

Agency Theory

This theory was first coined by Jensen and Meckling (1976), which describes an agency relationship is a contract in which one or more people ordering others (agent) to perform a service on behalf of the principal. For companies who formed a limited liability company (LLC) registered in the capital markets frequently occurs separation between the management companies as the agent of the shareholders as the principle (Husnan & Pudjiastuti, 2011). The company's goal is to maximize shareholder wealth, but the fact that managers often do things that are contrary to these objectives. Agency theory indicates when the manager appointed by the shareholders then ideally they act to benefit the interests of shareholders (Sartono, 2001).

Financial Theory

Financial theory, in principle, explain how a person or a company behaves, this theory also studies the behavior of a person or company. Fraudulent financial reporting according to the American Institute of Certified Public Accountant (2011) is a deliberate act or omission on the material misstatements in the financial statements. Cheating reporting by Australian Auditing Standards (AAS) is a negligence or misstatements of certain amounts or disclosures in financial reporting to deceive users (Brenavi & McGrath, 2007). Cheating is also a deliberate deception aimed fabrication, lies and theft (Bologna & Lindquist, 1995).

Quality Auditor

Audit is an element or part that creates the efficiency in the capital markets, audits can also increase the credibility of financial information and creating corporate governance better. Reputation theory predicts a positive relationship between firm sizes with quality audit (Lennox, 2002), public accounting firm great to have incentives to avoid the things that can damage the reputation (De Angelo, 1981).

Quality audits as a measure to locate and report on violations in the accounting system of its clients. Quality audits can be seen from the audit firm, large audit firms will seek to present a greater audit quality compared to small audit firms (De Angelo, 1981). Large audit firms better capture the signal against fraud occurring and express the result in their audit opinion (Lennox, 2002).

This research on audit quality tested only on companies that are audited by the accounting firm Deloitte among the big 4 auditor, PWC, Ernst & Young, and KPMG. Research conducted by Choi and Lee (2014) found that big 4 auditor reduce capital costs by providing high quality audits so that investors trust the financial information audited by big 4 auditor of the non-big 4 auditor. The results of the same study also found in the study Knechel and Causholli (2014) and Randal, and Fernando et al. (2011) that high quality auditors will reduce the cost of capital and a reduction in the cost of debt.

Hypothesis Development

Impact of Auditor Quality and Financial Report Fraud

Auditing with qualified services will increase the users' trust in financial statements, and can serve as a basis for decision making. The quality of the auditor is an assessment of the likelihood of the auditor finding violations in the company's audited accounting system. The quality of the auditor's work is not easily assessed directly, so the measure that can be used to see the capabilities of the auditor's quality is to use a Accounting Firm industry proxy that may reveal whether the audited client has cheated the financial statements and reported them. Large audit firms will seek to present better audit quality compared to smaller audit firms.

Large audit firms will seek to present better audit quality compared to smaller audit firms. Firms that are audited by big 4 public accounting firm tend to gain more trust from investors, not only that big 4's public accounting firm is judged to be higher capturing signals of fraud and disclosing the results and will transparently report in their audit opinion reports (Guedhami et al. 2014). The results of Bloomfield & Shackman's (2013) study found a positive correlation of auditor quality toward restatement of corporate financial statements, where the results showed that with the existence of Big 4 auditors providing good quality auditors able to provide good results on the restatement of audited financial statements. The results of Palmrose (1988) study that found big 8 auditors have higher audit quality than non-big 8 auditors in detecting fraud and submitting their opinion in the auditor independence report.

H1: The quality of auditors positively affects financial reporting fraud

Impact of Financial Stability and Financial Report Fraud

Financial Stability is a condition that describes the financial condition of a company at a safe point. Conditions that illustrate the risk of a company's stability may manipulate earnings when financial stability or profitability is threatened by economic conditions. In order to make financial statements looks good, management will manipulate for growth looks stable (Skousen, 2008). Unstable corporate conditions will certainly provide a large enough opportunity for companies to commit fraud to the presentation of financial statements.

Assets are a reflection of the wealth of a company that can be used as a benchmark by investors. Large companies certainly have a lot of assets and have a good image in the eyes of creditors and investors. Conversely, if the asset growth rate is smaller or even negative, it indicates that the company's financial condition is unstable and is considered unable to operate properly.

Management often gets pressure to show that the company is able to manage the assets well so that the resulting profits are also many and will eventually increase the bonus received and will generate a high return also for investors. Management utilizes financial statements as a tool to cover up the conditions of poor financial stability by committing fraud. According to researcher Martantya (2013) financial stability effect on fraudulent acts of financial statements.

H2: Financial stability negatively affects fraudulent financial statements

The Influence of Financial Target and Financial Report Fraud

The agency theory basically explains the relationship between shareholders and management. Shareholders have a goal to get a high return on their investment, while management has an interest to get a big bonus as a result of its work. Management is a party contracted by the principal, of course management will provide maximum results in meeting the interests of principals or shareholders.

ROA is often used in assessing manager performance, in deciding bonuses, and wage increases (Skousen, 2008). Management will be likely to manipulate, for example by manipulating profits to be deemed capable of achieving predetermined financial targets. The high preceding ROA of the previous year showed a high profitability of the company and made the profit targets to be earned in the following year. The comparison of earnings in the previous period can be used to see if in the current year the profit generated has reached the established financial target or not.

Targets to be achieved are usually related to the target profitability, with the target will certainly put pressure for management to work hard to achieve. Companies with low profitability tend to record excessive income or record the burden too low. Research conducted by Ansar (2012) found a significant relationship between financial targets against fraudulent financial statements. Different results were found in the study of Skousen et al. (2008) there is no effect of profitability on fraudulent financial statements. Different research conducted by Fimanaya & Syafruddin (2014) whose research results found a negative effect of profitability on fraudulent financial statements.

H3: Financial targets negatively affect fraudulent financial statements

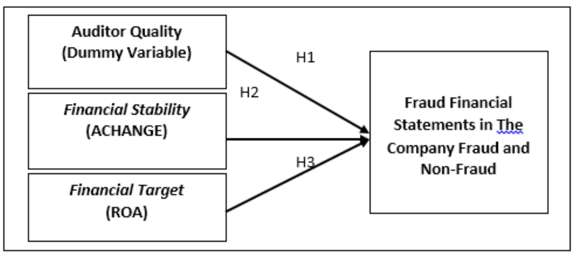

Fig. 1 Research Model

Research Methods

This study uses some research variables, namely ACHANGE, return on assets (ROA), and a big 4 auditor. The object of this research is the company's annual financial report issued by non-financial companies listed on the stock exchange. This data was obtained from the official website of the stock exchange (www.idx.co.id). The population in this study is a non-financial companies listed on the Financial Services Authority (FSA) has made fraudulent financial reports from 2010 to 2014. The sample used as the object of this research is purposive sampling. The criteria for determining the sample in this study are non-financial companies are exposed to financial statement presentation case; the company publishes financial statements and audit reports in 2010-2014; fraud samples taken from the report the FSA and non-fraud samples taken from website idx.co.id. In this study was not performed classical assumption, so just test the hypothesis by using binary logistic regression analysis.

Results and Discussion

Descriptive Analysis

This shows that in 2010-2014 non-financial companies listed on the Indonesia Stock Exchange as much as 44% have defrauded the financial statements. In Table 1 shows that the average value is 0.121008 financial stability which showed that about 12.1% rate affects the stability of the company's financial statements onset of action fraud. In table 1 shows that the financial targets have an average of 0.032728.

Table 1
Results Average Variable

	N	Min	Max	Mean	Std. Dev.
Fraud	181	0	1	0.44	0.498
Financial Stability	181	-0.610251	0.994755	0.121008	0.217257
Financial Target	181	-1.126.349	0.887050	0.032728	0.151310
Quality Auditor	181	0	1	0.34	0.474
Valid N (List wise)	181				

This reflects that each unit of asset able to generate a profit of 0.032728 percent. The maximum value of the target financial variables is 0.887050 and the minimum value of -1.126349 which shows that in 2010-2014 there were companies that commit fraud financial statements at a loss.

Hypothesis Testing

Testing the influence of the independent variable on the partial variables can be seen from the output variable in the equation.

Table 2
Test Results of Binary Logistic

	B	Sig	α
Quality Auditor	0.956	0.010	0.05
Financial Stability	-1.957	0.018	0.05
Financial Target	-5.100	0.013	0.05
Constant	-0.482	0.164	0.05

This shows that when a company's financial statements audited by a big 4 accounting firm, the higher the chances of cheating actions found on the company. Financial stability against fraudulent financial statements to show the value of coefficient of -1.957 with a significance of 0.018, so it was found that the Financial Stability negative effect on the financial statements fraud. This shows that when the condition of the assets of a company are in stable point then the likelihood of financial statement fraud measures less.

Target financial results of testing against fraud financial report shows the value of coefficient of -5.100 with a significance of 0.013, so it was found that the negative effect on the Target Financial fraud financial statements. ROA is low due to low profit generated. This resulted in management must work harder in order to improve the financial condition which is not healthy. One of the indicators for assessing the performance of a company is to see profitability generated, when profitability is generated not in accordance with the targets set then there is an opportunity for management to manipulate earnings and make it as small as possible manipulations known to the auditor.

Conclusion

This study aimed to see if the financial stability and financial variables affecting a company's target of an act of fraud financial statements, and how the role of the quality of auditors in finding such action. The results of this study indicate that the role of the quality auditor positive effect on financial statement fraud measures. This means that the higher the quality of auditors, the greater the chances of finding that a company has to rig the financial statements. For variable financial stability and financial targets are found equally have a negative impact on the financial statements fraud measures. Financial stability is a condition of financial stability, when the financial situation is unstable is certainly more likely for companies to commit fraud in the presentation of financial statement information to make it look stable. Financial targets are financial targets that use the previous year's earnings as a reference for the target company in the next month. Financial or profit targets are achieved not in accordance with the desired target gives great opportunities for companies to conduct financial statements fraud measures in case of errors in the presentation of financial statements.

Limitation of the study are limited variable and proxy variables to measure the target financial variables. Future studies are expected to increase the number of research period, seek a proxy for a target financial variables, and add the variables that allow fraud financial statements other than the variable has been used in this study.

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