The Effect of Auditor Switching, Audit Report Lag, and Financial Distress on Financial Statement Fraud

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Abstract. This study examines the effect of auditor switching, audit report lag, and financial distress on financial statement fraud. This study uses a sample of banking companies listed on the Indonesia Stock Exchange during the 2018-2020 period, as many as 43 companies. Data collection techniques using the purposive sampling method and analysis using the logistic regression method. The results showed that Audit report lag and financial distress positively affect financial statement fraud, while auditor switching does not affect financial statement fraud.

Keywords: Audit Report Lag, Auditor Switching, Financial Distress, Financial Statement Fraud.

1 Introduction

Financial reports become a reference for internal and external parties to evaluate the company's performance. The general purpose of financial statements is to provide information about an enterprise's equity, economic, and financial position and to demonstrate management's responsibility for using the resources entrusted to it. The existence of a company performance review motivates management to carry out company operations optimally with the aim of informing stakeholders that the company's health is getting worse. However, regulatory efforts sometimes produce financial statements that need to reflect the actual situation. Inappropriate financial statement information makes financial reporting irrelevant for related parties as a basis for economic decisions. In the financial statements, the existence of misstatements due to errors or fraud can cause the trust of stakeholders in the company's management to be lost. Therefore, companies must be able to detect and minimize fraud in preparing financial statements.

The 12th Global Fraud Survey by Ernst & Young, 2011 revealed that fraud remains one of the most problematic issues for businesses or companies worldwide [1]. One form of fraud that can affect the long-term success of a business is fraudulent financial statements. This is because the annual financial report provides information to help make useful decisions for key owners of financial statements, such as stakeholders, management, directors, and employees.

Cases of fraudulent financial statements continue to occur in Indonesia, especially in large and state-owned companies. The case in, Garuda Indonesia managed to rec-

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ord a profit of US $ 809 thousand or equivalent to Rp. 11 billion in the 2018 financial statements, inversely proportional to the loss experienced in 2017 of US $ 216.58 million. Tanjung and Dony Oskaria consider that the financial statements are not by PSAK. [2].

Another case occurred in PT Asuransi Jiwasraya (Persero), which could not pay the insurance policy (default). The investigation results by the Supreme Audit Agency (BPK) found that the problem had been going on for a long time. Since 2006, Jiwasraya has still recorded a profit, but the profit is false due to accounting engineering (window dressing) even though the company's financial condition was experiencing a loss. In 2018, Jiwasraya posted a loss of 15.3 trillion. The loss occurred because Jiwasraya sold its JS Saving Plan product with a very high cost of funds above the interest on deposits and bonds made since 2015 [3].

Auditor switching is the change of auditors and Accounting Firms (KAP) who conduct audits in a company. Auditor switching is considered one factor that affects the delay in audit reports because new auditors take a long time to understand the characteristics and business systems of the client. This can take up the auditor's time and cause delays in presenting the audited annual financial statements [4]. Widharma and Susilowati's research shows that auditor switching has no effect on audit report delays, and auditor turnover does not directly affect fraud in annual financial statements. In contrast, Achmad's research shows that auditor switching positively and significantly affects fraudulent financial statements [5].

Audit Report Lag is also one of the factors that can cause accounting fraud because the longer the audit report, the more errors or missing data. The auditor's financial information errors found during the audit hampered the auditor's performance. The investigation results by Widharma, and Susilowati show that Audit Report Lag affects fraud in financial statements.

Financial distress is associated with a company's condition when cash flows fall below the expected level. Companies in financial distress or financial difficulties find that the company's management cannot manage the company's financial stability, causing a loss of trust in the company by investors and other stakeholders. This can trigger fraudulent financial statements because management tends to hide the true status of the company to provide sufficient information to interested parties [6]. Widharma and Susilowati's research shows that financial distress impacts fraud in financial statements.

This research is a joint study of Widharma Susilowati), and the research of Dzaki & Suryani [7]. Research conducted by Widharma and Susilowati discusses Auditor Switching, Financial Distress, and Financial Statement Fraud Practices with Audit Report Lag as an Intervening Variable. The results showed that the auditor switching variable did not affect financial statement fraud, the auditor switching and financial distress variables did not affect auditor report lag, and the financial distress and audit report lag variables affected financial statement fraud. Research conducted by Dzaki and Suryani discusses The Effect of Corporate Governance, Company Size, and Financial Performance on Fraudulent Financial Statements. The results showed that the financial performance variable had a positive effect on fraudulent financial statements, while the company size and corporate governance variables, as proxied by the board of commissioners and audit committee, had no effect on fraudulent financial statements.

Researchers combine several independent variables that exist in previous studies. The independent variables the authors examine are Auditor Switching, Audit Report Lag, and Financial Distress. The difference with previous research lies in the object and year of research, where the object in this study is a banking company listed on the Indonesia Stock Exchange for the 2018-2020 period.

2 Literature Review

2.1 Auditor Switching

According to Widharma and Susilowati, auditor switching is the change of auditors and Public Accounting Firms (KAP) that conduct audits on a company. The government issued rules regarding auditor rotation to maintain auditor independence.

To tighten the supervision of public accountants who conduct audits of companies providing financial services, the Financial Services Authority (OJK) issued Financial Services Authority Regulation Number 13/POJK.03/2017 [8] concerning the Use of Public Accountants and Public Accounting Firms in Financial Services Activities. The regulation stipulates that financial service institutions must use a public accountant and a public accounting firm (KAP) registered with the OJK. Financial service institutions must also limit the use of audit services from public accountants for a maximum of 3 (three) consecutive financial years. In contrast, restrictions on using services from KAP depend on the Audit Committee's evaluation results.

2.2 Audit Report Lag

Audit report lag is the period for completing the annual financial statement audit, from the closing date of the company's books to the date stated in the independent auditor's report [9]. Timeliness of the issuance of audited financial statements is very important, especially for publicly listed companies whose main funding source is investors. Delays in the publication of financial statements will be very detrimental to investors because they can increase information asymmetry and insider trading and create rumors that can influence market decisions. Therefore, the Financial Services Authority (OJK) has set a maximum time limit for submitting financial reports for go-public companies, which is by March 30 for the submission of the annual financial report and April 30 for the submission of the annual report. Audit report lag is also considered to affect financial statement fraud because the longer the audit report, the more errors or lack of data will occur. Errors in the auditor's financial data found during the audit of these financial statements will hinder the auditor's performance.

2.3 Financial Distress

In general, the term "financial distress" is often used negatively to describe the financial health of a company facing liquidity shortages and failing to meet its financial obligations [10]. Financial distress is the stage of declining financial conditions that occur before bankruptcy or liquidation.

2.4 Financial Statement Fraud

Fraud is any illegal act characterized by fraud, concealment, or breach of trust [12]. This action does not rely on threats of violence or physical force. Financial statement fraud is a fraud scheme in which an employee intentionally misrepresents or omits material information in a company's financial statements, for example, recording fictitious revenues, understating reported expenses, or artificially inflating reported assets (artificially inflating reported assets). This scheme is the least common scheme when compared to the other two schemes, but it is this scheme that causes the most losses.

3 Conceptual Framework and Hypotheses Formulation

H1: Auditor switching has a positive effect on financial statement fraud
SAS No. 99 states that companies that perform auditor switching voluntarily can be an indication of fraud. In line with agency theory, a management request for a change of auditor could indicate fraudulent financial statements. This is because the auditors previously knew the company's characteristics and conditions well, so they could better detect the possibility of fraudulent financial statements committed by management. Before the indications of fraud are revealed, the company will voluntarily change auditors. The new auditors need to learn the condition of the company better when compared to the previous auditors. The research results by Widharma, and Susilowati show that auditor switching has no direct effect on financial statement fraud. In contrast, research conducted by Achmad shows that auditor switching has a significant positive effect on financial statement fraud.

H2: Auditor report lag has a positive effect on financial statement fraud
Audit report lag is the period for completing the annual financial statement audit, from the closing date of the company's books to the date stated in the independent auditor's report. The longer it takes to complete the audit report will affect the quality of the audit and ultimately can affect the occurrence of financial statement fraud because the longer the audit report, the more errors and data deficiencies will occur. In line with agency theory, audit report lag can be used by management to cover the shortcomings of its performance. The results of research conducted by Widharma and Susilowati show that audit report lag affects financial statement fraud. Other research conducted by Suryanto [13] also proves that audit report lag affects fraudulent financial statements or financial statement fraud.

H3: Financial distress has a positive effect on financial statement fraud
Financial distress describes a company's financial health faced with a liquidity shortage failing to meet its financial obligations [14]. Companies experiencing financial distress indicate that management cannot manage the company's financial stability, which can cause a loss of investor and stakeholder confidence in management performance. Based on agency theory, management tends to cover up the actual condition of the company to provide sufficient information to stakeholders. The existence of this conflict of interest can trigger fraudulent financial statements. The research results by Widharma and Susilowati show that financial distress affects financial statement fraud. Meanwhile, research conducted by Safiq and Seles [15] showed dif-

ferent results. Namely, financial distress did not have a significant effect on financial statement fraud.

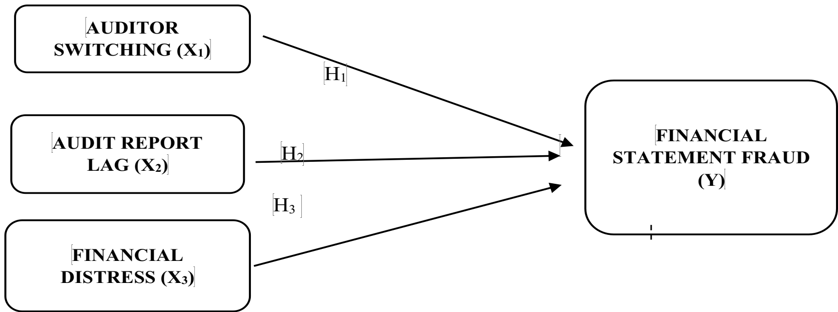

Fig. 1. Framework.

4 Research Methodology

4.1 Research Design

This type of research is quantitative research by testing the hypothesis. This study uses quantitative data from secondary sources, namely the financial statements of banking companies that have gone public and are listed on the Indonesia Stock Exchange (IDX) from 2018 to 2020.

4.2 Method of Collecting Data

Sampling in this study was carried out using the purposive sampling method, namely by applying certain criteria to take the sample. The sample selection criteria are as follows:

1. Banking companies listed on the Indonesia Stock Exchange (IDX) for 2018 – 2020.
2. Banking companies that publish consecutive financial reports during 2018 – 2020.
3. Banking companies that have complete and clear data regarding the required variables.

4.3 Data Collection Instruments

The researcher used one dependent variable and three independent variables in this study. The following is the definition of each variable:

Financial statement fraud

Financial statement fraud in this study was measured by a dummy variable using the Beneish Model.

Auditor Switching

Auditor switching is a change in the Public Accounting Firm (KAP) carried out by the company either on their own volition or because of government regulations [16]
This study measures auditor switching using a dummy variable.'

Audit report lag

Auditor report lag in this study was measured using a ratio scale, namely by counting the number of days from the closing date of the last book to the independent audit report.

Financial Distress

Financial distress in this study was measured using a ratio scale and calculated using the Bankometer or S-Score formula [17].

4.4 Population & Sample Size

The data for this study were obtained from www.idx.co.id. Sampling in this study was carried out using the purposive sampling method. A total of 46 banking companies are listed on the IDX. Based on the established criteria, 43 companies met and were used as research samples.

4.5 Data Analysis Plan

The Software Statistical Package for Social Science (SPSS) will be used to collect, tabulate, and analyze the data. The data will be transferred to SPSS software for further analysis, such as (1) performing descriptive, (2) mainstay analysis, (3) logistics regression testing, and (4) hypothesis testing [18].

5 Results and Discussion

5.1 Effect of Auditor Switching on Fraud Financial Statements

The test results show that auditor switching does not positively affect financial statement fraud. These results prove that the company does not show fraud despite changing auditors. The Financial Services Authority (OJK) has regulated auditor switching in regulation Number 13/POJK.03/2017, which explains that parties conducting financial service activities must limit audit services from the same AP for a maximum of 3 (three) years. This study's results align with compliance theory, where the entity that performs auditor switching is a form of compliance with the applicable rules.

Table 1. T-test results of logistics regression model.

Variable	B	SE.	Wald	df	Sig. 2-tailed	Sig. 1-tailed	Conclusion
Constant	-2,292	0,734	9,579	1	0,002	0,0010	
Auditor Switching	0,354	0,371	0,912	1	0,340	0,1705	H1 rejected
Audit Report Lag	0,013	0,006	4,329	1	0,040	0,0200	H2 accepted
Financial Distress	0,005	0,003	3,756	1	0,063	0,0315	H3 accepted
Dependent Variable: Financial Statement Fraud							

Source: Data processed using SPSS 21

This study's results align with research conducted by Widharma and Susilowati, which proves that auditor switching does not affect financial statement fraud. However, contrary to research by Achmad, auditor switching has a significant positive effect on financial statement fraud.

5.2 Effect of Audit Report Lag on Fraud Financial Statements

The test results show that audit report lag positively affects financial statement fraud. These results indicate that during the examination of financial statements if the time required for the auditor is getting longer, it is likely that there will be many errors or a lack of data needed by the auditor. Errors or lack of data can hinder the auditor's performance in completing the company's appraisal report.

This study's results align with research conducted by Widharma and Susilowati, which proves that audit report lag affects financial statement fraud. Other research conducted by Suryanto also proves that audit report lag affects financial statement fraud.

5.3 Effect of Financial Distress on Financial Statement Fraud

The test results show that financial distress positively affects financial statement fraud. There are great demands in presenting financial statements with good conditions, putting pressure on the company's management. The pressure on the management of this company will encourage them to commit fraudulent financial statements so that the users of financial statements believe that the company's condition is in good condition.

This study's results align with research conducted by Widharma and Susilowati, which proves that financial distress affects financial statement fraud. However, this contradicts the research conducted by Safiq and Seles, which shows that financial distress does not have a significant effect on financial statement fraud.

6 Conclusion, Implications, and Suggestion

6.1 Conclusion

Based on the results of data analysis and discussion that has been carried out, it can be concluded that:

1. Auditor switching is proven not to affect financial statement fraud.
2. Audit report lag has been proven to affect financial statement fraud positively.
3. Financial distress is proven to affect financial statement fraud positively.

6.2 Implications

This research has implications for several parties, including:

1. For Regulators: This research is expected to provide an overview and reference in detecting companies that commit fraudulent financial statements.

2. For Companies: It is hoped that this research can provide input for companies to be able to identify early the factors that can cause financial report fraud so that companies can prevent fraud committed by company management and company employees.
3. For Investors: This research can help investors in making investment decisions so that they can assess which companies are indicated to be committing fraudulent financial statements so that investors are not wrong in making a decision. Investors should consider the influence of audit report lag and financial distress variables, as well as several other variables that are considered capable of influencing a company's decision to commit financial statement fraud.

6.3 Suggestions

Based on the conclusions from the research results as described above, the suggestions that can be given are as follows:

1. Further researchers are advised to use several other variables that can influence the company's decision to commit financial statement fraud.
2. Further researchers are also expected to be able to expand the object of research so that it is not limited to banking companies listed on the IDX, as well as increase the research period for more complex results.

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