

THE INFLUENCE OF AUDIT RISK

ON AUDIT FEES IN INDONESIA

**(Empirical Evidence in Manufacturing Public Companies listed on
Indonesia Stock Exchange for Period 2015 - 2017)**



UNDERGRADUATE THESIS

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complete the Bachelor Program (S1) at the
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STATEMENT OF ORIGINALITY

I am Yusril Ihza Ainun Achda, state that the undergraduate thesis about: **THE INFLUENCE OF THE AUDIT RISK ON AUDIT FEES IN INDONESIA (Empirical Evidence In Manufacturing Public Companies Listed on Indonesia Stock Exchange for Period 2015 - 2017)** is the product of my own work, even though I may have received assistance from others on style, presentation and language expression. I hereby declare that the thesis is not obtained the whole or part of the someone else's works that I take by copying or imitating in the form of sentences or symbols that show ideas or opinions from others, which I acknowledge as my work, and / or there is no part or all of the writing that I copied, or I took from someone else's works without giving the original author recognition.

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ABSTRACT

The aim of this study is to examine the influence of the audit risk on the determination of audit fees. The independent variables that used in this research are inherent risk, control risk and detection risk while the dependent variable is audit fees. This research also used big 4 and firm size as control variable. The population in this study consists of all manufacturing firm in Indonesia Stock Exchange for the period 2015 - 2017. Sample determined with purposive sampling method. Total sample of this research is 132 companies. This study used multiple regression analysis for hypotheses testing. The results of this study indicate that not all attributes of audit risk such as inherent risk, control risk, and detection risk have a significant effect on the determination of audit fees in Indonesia.

Keywords: audit risk, inherent risk, control risk, detection risk, audit fees

ABSTRAK

Tujuan dari penelitian ini adalah untuk menguji pengaruh risiko audit terhadap penentuan biaya audit. Variabel independen yang digunakan dalam penelitian ini adalah risiko bawaan, risiko pengendalian, dan risiko deteksi. Sedangkan untuk variabel dependennya adalah biaya audit. Penelitian ini juga menggunakan big 4 dan ukuran perusahaan sebagai variabel kontrol. Populasi dalam penelitian ini terdiri dari semua perusahaan manufaktur yang terdaftar di Bursa Efek Indonesia pada periode 2015 – 2017. Sampel ditentukan dengan metode purposive sampling. Total sampel penelitian ini adalah 132 perusahaan. Penelitian ini menggunakan analisis regresi berganda untuk pengujian hipotesisnya. Hasil penelitian ini menunjukkan bahwa tidak semua atribut risiko audit seperti risiko bawaan, risiko pengendalian, dan risiko deteksi memiliki pengaruh signifikan terhadap penentuan biaya audit di Indonesia.

Kata kunci: risiko audit, risiko bawaan, risiko pengendalian, risiko deteksi, biaya audit

MOTTO AND TRIBUTE

Man Jadda Wajada

I present this undergraduate thesis to:

My beloved Father, Mother and Brother.

Keluarga Mahasiswa Akuntansi

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The author realizes that in the writing process of this thesis there are many mistakes and errors due to limited knowledge and experience. This undergraduate thesis is far from perfect, but it is expected that it will provide benefits and additional information for all parties in need. For this reason, constructive thoughtful suggestions and critics are welcomed.

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CHAPTER I

INTRODUCTION

The first chapter contains the introduction. This chapter describes the background of research on the influence of audit risk on the determination of audit fee in Indonesia. The background of this research will be explained further in sub-chapter 1.1. Furthermore, problem formulation, research objectives, and writing structure, each will be described in subchapters 1.2, 1.3 and 1.4.

1.1 Background Problem

The financial statements are arranged to afford relevant information respecting the financial position and all activities carried out by a reporting entity during the reporting period. An accounting cycle basically generate the financial statements which could be used as a tool for communication between financial data or the company's activities and some parties who have an interest in that data. Parties that have an interest to the financial position or development of a company are the shareholders, the management, the creditors, the investors and the government (Mulyadi, 2002: 1-4).

The shareholders are individuals, companies, or organizations, that own shares of a for-profit entity. The individuals own a certain amount of shares, which they each purchased at a definite price. The shareholders want to obtain reliable information from

management regarding the funds they have invested. On the other hand, the management has an interest in presenting financial statements as a tool for responding to the funds that come from outside parties. The existence of two different interests between management and external parties of this company caused the presence of the external auditor (Mulyadi, 2002).

In perspective of the external auditor, auditing is an objective test of the financial statements of an entity or other organization with the aim of determining whether the financial statements are presented fairly, within all material matters, financial position and results of company's operations (Mulyadi, 2002). Publicly listed entities are mandatory to hand over their audited financial statements annually. The obligation to submit audited financial statements has been regulated by Financial Services Authority (OJK) through regulation No. 29 / POJK 04 / 2016 and the Indonesia Stock Exchange through regulation No. 306 / BEJ / 07-2004 which regulates about the obligation of publicly listed companies to submit interim and annual financial statements to the capital market.

The main benefit for auditees of purchasing audit service is liability avoidance (Simunic, 1980). The external auditor has a function to audit the financial statements issued by the Indonesian Public Accountant Institute (IAPI) to issue PP No. 2 of 2016 concerning the Determination of Audit Fee Policy. The letter explains that there are guidelines for Members of the Indonesian Institute of Certified Public Accountants as public accountants in determining a reasonable amount of compensation for the

professional services they provide. The amount of audit fees are given to an auditor will vary because it is seen from the level of audit risk, the complexity of audit services, what competencies are needed, and consideration of non-audit services (Mulyadi, 2002). Furthermore, the audit efforts took in auditing are related to audit costs and the compensation for risk-taking is a risk premium.

In Indonesia, the determination of audit fees is still a long discussion, because many factors influence it. It was explained that in establishing a reasonable service fee should appropriate with the dignity of the auditor's profession. The amount should suitable with the demands of the applicable professional standards of public accountants. Service fees that are too low or significantly lower than those imposed by auditors or other accountants will raise doubts about the ability and competency of members in establishing applicable technical standards and professional standards. Many factors influence the amount of the audit fees, such as the size of the client, the location of the audit firm, the number of subsidiaries, audit services, company size, audit risk and the size of the audit firm (Tina Hartati Saputri et al, 2017).

Audit risk is one of the important factors which drive the amount of audit fees. Audit fees are driven primarily by two natures of risk (Calderon et al, 2012). Firstly, a risk raised based on historical factors which is the expected risk. For example, when the auditor assesses a risk, they also consider some frauds that happened in previous year. Secondly, a risk showed up during the current period which is the realized risk. As example, when auditor assesses a risk, they used current year's financial statements

as benchmark. Practically, auditors rely heavily on past audit results in audit planning for the current period. According to the audit risk model, there are three types of audit risk such as control risk, inherent risk, and detection risk. Control risk and inherent risk usually come from the client or internal factor. Risk-based auditing comes mostly from models that believe inherent risk and control risk are different concepts. Inherent risk arises from attributes of the audit environment that are completely independent of attributes that determine the level of control risk (Gregory Shailer et al 1998). Otherwise, the detection risk comes from auditor or external factor. For example, when a material misstatement in an account balance or transaction stream fail to be detected by auditor's procedures.

Prior research by Calderon et al (2012) shows the influence between prior year control and audit fees in the current period. The findings are consistent with the audit risk model and suggest that audit effort and/or premiums are adjusted for risk. Feng Shiyi and Dr. S.S. Jeyaraj (2017) also conducted research on the relationship of audit risk with audit fees. It was found that control risk and inherent risk had a significant positive effect on audit fees while detection risk did not have a significant effect. However, in the sub-sample of financial companies, it was found that auditors did not consider corporate governance to determine the audit fees. Due to, in the 2007 or the period before the 2008 crisis the majority of financial companies in the sample did not have good corporate governance. In other study conducted by Chiraz Ben Ali et al (2012) it was found that inherent risk that proxied by family firm ownership did not

have a significant influence on audit fees. One possible explanation is the existence of two opposite effects between the decrease in type 1 agency conflict for family-controlled firms and the increase of type II agency conflict, which both influence the magnitude of audit fees. Type 1 is the agency problem that arises between the principal as the owner of companies and agents as the manager who is the executor the company's operations. While the issue of agency type II is the agency problem that occurs between controlling shareholders and minority shareholders.

Based on the previous explanation and the elaboration of previous research that there are still inconsistencies in the results of research regarding the above factors. Thus, the researcher takes the title "**The Influence of the Audit Risk on Audit Fees in Indonesia (Empirical Evidence in Manufacturing Public Companies listed on Indonesia Stock Exchange for Period 2015-2017)**".

1.2 Problem Statement

The appointment of the external auditor aims to monitor the performance of management, know the policies applied in the entity, and improve the quality of the entity's financial statements. Therefore, the audit fee is an integral part when it comes to audit services provided by external auditors.

Based on the research background described above, the research problems can be stated as follows:

1. Does the control risk have an influence on audit fees in Indonesia?
2. Does the inherent risk have an influence on audit fees in Indonesia?
3. Does the detection risk have an influence on audit fees in Indonesia?

1.3 Research Objectives and Purposes

The purpose of this research is to focus on how audit fees are influenced by examining the effect of audit risk in Indonesia.

1. To analyze the influence of control risk on the determination of audit fee in Indonesia.
2. To analyze the influence of inherent risk on the determination of audit fee in Indonesia.
3. To analyze the influence of detection risk on the determination of audit fee in Indonesia.

This research is expected to be useful especially for writers and readers in general both theoretically and practically. Results of this research is expected to have the following benefits:

1. Empirical benefits :

- a. This research provides information in the form of views or suggestions to regulators in developing rules regarding audit risk that are considered in determining the audit fees in Indonesia.
- b. This research is expected to be a reference and provide conceptual contributions to similar researchers as well as further research in order to develop knowledge for the development and progress of the world of education.
- c. This research is assumed to contribute ideas for further research, especially those relating to the influence of the audit risk on the audit fees.

2. Practical benefits

a. Audit Firm

This research is assumed to provide useful information for the audit firm, such as providing an overview to the audit firm on the determination of audit fees needed to take notice the influence of the audit risk (control risk, inherent risk, and detection risk).

b. Company

The results of this research can provide an alternative for the company as a material deliberation in making decisions about the amount of audit fees paid to the auditor later in order to improve the quality of the company's financial reporting.

1.4 Writing Structure

To obtain a complete picture of this thesis, the writing structure will be divided into five chapters, with the following details:

Chapter I contains the introduction which is the basis of a study. The introduction consists of background problems, problem formulation, research objectives, research benefits and structure of writing. This introduction helps in understanding research in general.

Chapter II of the study contains a review of the research library. In this chapter will be elaborated on the basis of research theory that is used as a basis for research reference, previous research related to research, research frameworks and hypotheses.

Chapter III contains research methods. This chapter will describe the type of research, the determination of samples, types, and sources of data, methods of data collection, research variables to be taken and operational definitions of the variables used in research, methods of analysis and hypothesis testing. The research method covers all aspects of the details of the data and how to analyze it.

Chapter IV contains the description of the object of research, data analysis, and interpretation of results. Description of the object of research explaining the sample research and the process of determining the sample of the study population. The data analysis contains an explanation of the results of the analysis. Interpretation of the

results contains a further explanation of whether the results support or reject the hypothesis that has been formulated.

Chapter V contains conclusions, research limitations as well as research suggestions. This conclusion is a brief presentation of what is obtained from the discussion. Limitations of the study describe the weaknesses and flaws found after analysis and interpretation of results. Suggestions contain future policy implications and research suggestions.