CHAPTER I

INTRODUCTION

A. Research Background

Capital market especially Indonesia capital market has been experiencing a rapid growth compared to the growth of other fields of financial services. The growth itself is also encouraged by the increased number of people taking on the role as investors that choose to actually invest their money to the instruments offered by the capital market as well as stock. Financial Services Authority/Otoritas Jasa Keuangan (OJK) recorded average daily stock volume from 2016 to 2017 increased almost 65% with the increased in transaction frequency up to above 80% (OJK, 2017). However, in making decisions investors will likely to consider many aspects, especially the financial performance of a company. Therefore financial reports are needed for investors as well as other external parties as the main sources of information in decision making. This is in line with the purposes stated in the definition of financial statements presented by the International Accounting Standards Board (IASB) in the Framework for the Preparation and Presentation of Financial Statement which states that by preparing the financial statements, the right economic decision-making can be made.

In accordance with that main purpose, the financial statements must meet several characteristics to ensure its quality. According to the Statement of Financial Accounting Concept (SFAC), number 8 chapter 3 qualitative

characteristics that is needed to meet a good financial statement include relevancy and faithful representation as the main and fundamental characteristics. The financial statement also should be supported by other characteristics including comparability, verifiability, timeliness, and understandability. To guarantee the fulfillment of those characteristics and a financial statement can be declared free of material misstatement requires an independent professional service that can ensure that the information contained can be used in decision making. These services are provided by independent auditors and/or public accounting professions.

The annual financial statements of companies that have registered in the Indonesia Stock Exchange (IDX) must be reported to the Capital Market and Financial Institution Supervisory Agency/Badan Pengawas Pasar Modal and Lembaga Keuangan (BAPEPAM and LK) or which have now been transferred to OJK. As stipulated and arranged in X.K.2 through BAPEPAM and LK decree number KEP-346 / BL / 2011, an audited financial statement of an audited company shall be reported no later than 3 months or as of 90 days from the date of the annual financial statements to BAPEPAM and LK. In addition, BAPEPAM and LK decree X.K.6 number KEP-431 / BL / 2012 states that each issuer that has been going public and listed on Indonesia Stock Exchange must also submit the annual report for a maximum of 4 months or 120 days from the year the book ends. Therefore, every listed company must submit an audited financial statement and annual report within the specific time period.

The time difference from the date of annual financial reporting to the time of reporting of the audited result occurs because in the completion of the audit process an auditor requires some time. This is because an auditor also has procedures to do before giving his opinion. Ashton et al. (1987) use the term audit delay to describe this in which they define audit delay as the length of time that occurs from a company's fiscal year-end to the date of the auditor's report.

The need for relevant financial information requires financial statements to be presented on time or should pay attention to aspects of timeliness of the information provided. In Islam, it has also been explained through the Surah Al-Asr in the holy book Al - Qur'an, that people who do not use their time well and do good things will lose:

وَٱلۡعَصۡرِ (١) إِنَّ ٱلۡإِنسَٰنَ لَفِي خُسۡرٍ (٢) إِلَّا ٱلَّذِينَ ءَامَنُواْ وَعَمِلُواْ ٱلصَّٰلِحَٰتِ وَتَوَاصَوۡاْ بِٱلۡحَقِّ وَتَوَاصَوۡاْ بِٱلصَّبۡرِ (٣)

Translation: *"By time, (1) Indeed, mankind is in loss, (2) Except for those who have believed and done righteous deeds and advised each other to truth and advised each other to patience."*

In fact, there are still many things that hamper and slow down the presentation of financial statements by the auditor. In 2017, it is reported that there were 70 companies that are late in reporting their financial statement until May 2017. Some of the companies also have not reported their 2016 audited financial report (IDX, 2017). The longer the time needed to publish audited financial statements will further reduce the relevance of

such financial statements to external users such as investors. In the middle of intense competition in the intercompany capital market, delays will have a negative impact not only for the investor but also for the company. Investors will lose confidence in the company's performance with the assumption that the length of time it takes to audit the company is because the company has serious problems. Loss of confidence from the investors will also affect the company's performance on the IDX, the loss of investor’s interest in investing will affect the company's stock price.

There are some factors that influence the audit delay that happened. In a study conducted by Aditya and Anisykurlillah (2014) audit delay is influenced by profit as well as audit opinion. Fahrezza (2016) in his study has found that audit opinion and auditor quality influence the audit delay. Dao and Pham (2014) has found that a short audit tenure affects the length of time that the auditor needs until the time of issuing an audit opinion.

Furthermore, Habib and Bhuiyan (2011) studied the influence of auditor industry specialization on audit delay. In their research auditors with industry specializations can complete their audit processes more quickly and impact on shorter audit delay. While Rahadianto (2012) in his study found that the auditor industry specialization has no effect in reducing the audit delay. On the other side, a study done by Primantara and Rasmini (2015) is in line with Habib and Bhuiyan's study that the industry specialization of auditors significantly influences the audit delay and it influences the audit delay in negative direction.

Another study of audit delay is done by analyzing the characteristics of corporate governance and their effect on audit delay. Corporate governance is a system conducted with the purpose of ensuring and overseeing the running governance system of a company and is expected to reduce the control risk as one of the audit risks that may reduce the auditor's time in conducting the substantive tests that result in shorter audit delay. According to Asian Corporate Governance Association through their survey, it shows that Indonesia's score on corporate governance watch market scores in 2016 has been decreasing compared to 2014 from 39 to 36 (ACGA, 2016). The decrease of the score may also be assumed to be related to the delay in audited financial reporting around the year of 2016 to 2017 as declared by the IDX.

Previous study by Wardhani and Raharja (2013) tried to examine the effect of size, independence, number of meetings, and competence of audit committee members, as well as the size of board and independent commissioners as corporate governance characteristics that influencing audit delay. The study was succeeded in identifying that the size, independence, and competence of audit committee members significantly influenced the audit delay and the characteristics of corporate governance influenced audit delay in positive direction. While board size has a positive influence on audit delay. Lastly, audit committee meeting and independent commissioners are proven to have no effect on audit delay.

Kuslihaniati and Hermanto (2016) stated that the independent board of commissioners and board of commissioners meetings has no significant effect on audit delay. This is in line with the research of Wardhani and Raharja (2013) in which the independent board of commissioners have no effect on audit delay. In addition, the independent board of directors and board of directors meetings also proved to have no significant influence on audit delay. While audit committee meetings have proven to have a negative influence and it significantly influence the audit delay which is different from previous research from Wardhani and Raharja (2013).

Kusumah and Manurung (2017) also analyzed the influence of corporate governance using the company size, independent audit committee and the number of meeting the committee have conducted as their independent variables. Other independent variables they use are the size of board and the independent commissioners. The result of this study is different from the study conducted by Wardhani and Raharja (2013) as well as Kuslihaniati and Hermanto (2016) where independent commissioners have no effect on audit delay. In Kusumah and Manurung (2017) research, the independent commissioners influenced the audit delay in a positive direction. The study also shows that the size of commissioners, the number of audit committee meetings, and the company size influenced the audit delay with a negative direction. In line with the research by Kuslihaniati and Hermanto (2016) where the number of audit committee meetings also

influenced the audit delay. As for the independent audit committee, the research showed that it has no effect on the audit delay.

The Indonesian capital market consists of various types of companies which are then listed as issuers in the Indonesia Stock Exchange. The growing number of companies enrolled in IDX is also driven by the growth of Indonesian economy. World Economic Forum reported that Indonesia's rank rose from 41 to 36 from the list of countries with the most competitive economy in the World Market in the past one year (The Global Competitiveness Report, 2017-2018).

It is undeniable that each type of company has an average time span in its financial reporting including audited financial statements. In most cases, a non-financial company takes longer time than a financial company in its financial reporting. The group of non-financial companies on the Indonesia Stock Exchange (IDX) itself is dominated by manufacturing companies. Manufacturing companies are considered to have assets that are more difficult to evaluate and to be valued compared to other non-financial companies. Therefore, this type of company is requires more time in reporting its financial statements as explained by Marhayaacob and Ahmad (2012) in Aditya and Anisykurlillah (2014). In addition, manufacturing companies experience significant operational variation that will take longer time to be audited. Finally, manufacturing companies have a wide scope and are considered capable of representing the condition of companies listed on the Indonesia Stock Exchange.

Based on the descriptions of previous studies, this study intends to examine the effect of corporate governance mechanisms and the influence of auditors with industry specialization on audit delay. This research is a replication of Alfraih research in 2016. The difference of this research with the first previous research lies in the object of research which uses the Indonesian listed manufacturing companies in the Indonesia Stock Exchange (IDX). Second, the year period used also differs from the length of period which is from 2015-2017. Third, this research eliminates the variables of joint auditor and government ownership because these variables are considered less appropriate with existing conditions in Indonesia. Fourth, this research will add audit committee variables as other characteristics of corporate governance as well as the addition of auditor industry specialization as new independent variable.

Based on the above description, the author conducts a research under the title **"The Effect of Corporate Governance Mechanisms and Audit Industry Specialization on Audit Delay in Manufacturing Companies listed on Indonesia Stock Exchange year 2015-2017"**.

B. Research Scope

In order for this research to provide an understanding in accordance with the objectives of the research, there are restrictions on the scope of the research. The restrictions include:

1. Corporate governance mechanisms used in this research are the board commissioner size, independent commissioners, role duality, institutional ownership, and the audit committee.
2. In addition to the existing aspects of corporate governance, auditor industry specialization is added as independent variables.
3. Companies to be studied are manufacturing companies listed on the Indonesia Stock Exchange (IDX) in 2015-2017.
4. The data used for this research come from secondary data which are annual financial reports and independent auditor reports.

C. Research Questions

The formulation of the proposed problem based on the above background description are as follows:

1. Does the size of board commissioner have a positive influence on audit delay in Indonesian manufacturing companies?
2. Does the independent commissioners have a negative influence on audit delay in Indonesian manufacturing companies?
3. Does the role duality have a positive influence on audit delay in Indonesian manufacturing companies?
4. Does the institutional ownership have a negative influence on audit delay in Indonesian manufacturing companies?
5. Does the audit committee have a negative influence on audit delay in Indonesian manufacturing companies?

6. Does the auditor industry specialization have a negative influence on audit delay in Indonesian manufacturing companies?

D. Research Objectives

Based on the formulation of the above problems, this research is conducted with the purpose of:

1. Testing and finding empirical evidence of the positive influence of board commissioner size on audit delay.
2. Testing and finding empirical evidence of the negative influence of independent commissioners on audit delay.
3. Testing and finding empirical evidence of the positive influence of role duality on audit delay.
4. Testing and finding empirical evidence of the negative influence of institutional ownership on audit delay.
5. Testing and finding empirical evidence of the negative influence of audit committee on audit delay.
6. Testing and finding empirical evidence of the negative influence of auditor industry specialization on audit delay.

E. Research Contribution

1. Theoretical Benefits

Theoretical benefits and contribution expected through this research are to provide additional information necessary for auditors in the audit environment. This research also can be used to increase science and audit knowledge about the delay.

2. Practical Benefits

This research is expected to increase knowledge, give a new insight, and a deeper understanding for auditors and accounting practitioners about the relationship of corporate governance mechanism associated with audit delay.