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Determinants of audit delay: evidence from manufacturing sector of Indonesia

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Abstract

This paper is focused on the determinants of audit delay. The purpose of this paper is to examine the relationship between profitability, solvency, audit opinion and audit delay in manufacturing sector of companies listed on the Indonesian stock exchange. The paper uses 53 Indonesia companies over the period 2011-2014. The Multiple linear regression analysis is provided to test hypothesis. Cluster analysis is also provided for clustering long audit delay. All companies fulfill the requirement to publish the audit report in four months after the year end. Companies in cluster one have audit delay in one or two months after year end and cluster two has audit delay in three months after year end. The difference between cluster one and cluster two is given by the profitability factor. This study concludes that profitability has impact on audit delay, while solvability and audit opinion do not have impact on the audit delay. This research has three implications, (1) profitability is important to be considered when publishing the audit report (2) companies tend to publish their audit report on time to convince the investor, because a long audit delay can affect the decision of the company's stakeholder especially the investor (3) leverage for firm in cluster 2 (more audit delay) higher than leverage in cluster 1 (less audit delay).

Keywords*: Audit Delay, Audit Opinion, Leverage, Profitability*

JEL Classification*: M,40,M41,M42,*

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Introduction

The financial statement is a structured presentation of financial position and performance of an entity. The objective of the financial statement is to provide information regarding the financial position, financial performance and cash flow of an entity which the majority of the financial statement's users will benefit from when making an economic decision. The financial statement also exhibits the managerial accountability towards the utilization of resources which ~~is~~ are entrusted to them.

The financial statement must be able to provide relevant information. One of the obstacles in actualizing relevant financial statement is timeliness. If a financial statement is not presented timely then that financial statement is losing its information value since the financial statement is unavailable when the users need it for decision making.

The investor and manager also recognize the importance of a timeliness in financial reporting since a timely reporting of a company's financial statement can affect the value of that financial statement. It means that the timeliness of a published financial statement will lead to a rise or fall in stock price.

There are many interested parties in the financial statement such as management, shareholder, investor and government; also, in stock market, the main user of financial statement is the investor. One of the methods used by the investor to monitor the performance of go public companies is through the published financial statement.

Audit delay, which is the number of days from fiscal year end to audit report date, has been studied through previous studies. Leventis and Weetman (2004) stated three aspects that link to timeliness financial report were proprietary cost, information cost saving and relative good news and bad news. This research focus on using relative good news and bad news by using audit opinion, profitability and leverage. Ansah (2000) concluded that company size and profitability are significant factors of timely reporting In Zimbabwe. Similarly to Ansah (2000), Apadore and Noor (2013) also stated that profitability significantly associated with audit report lag. Ayemere and Elijah (2015), Al-Ghanem and Hegazy (2011), Mouna and Anis (2013) find that leverage has no significant impact on audit delay. Unlike Laventis and Weetman (2004), Vuko and Cular (2014) find that audit opinion is an insignificant determinant audit delay in Croatia.

The results above indicate that there is no agreement between researchers; therefore, it motivates researcher to reexamine the influence of solvability, profitability and audit opinion. The purpose of this paper is to examine the relationship between solvability, profitability, audit opinion and audit delay of 53 Indonesian manufacturing companies listed on the Indonesian Stock Exchange over the period 2011-2014.

This study might be the first that explore difference factors that affect firms in respect of publishing their report in first or second month from the year end (cluster 1) and in third month from year end (cluster 2). This paper adds literature in terms of analyzing the determinants of audit delay. This research also offer understanding about determinants of audit delay in the Indonesians context.

I. Theoretical Framework

The qualitative characteristic is an attribute that makes the information inside financial statement useful for financial statement's user. There are four basic characteristics of financial statement, which are: (1) easily understood; (2) relevant; (3) reliable and (4) comparable. The company's financial statement becomes the main source of information for the investor; thus, it should have several basic elements, which must be fulfilled in order to make the financial statement reasonable and easily understood by most people. To be able to present a financial statement, which should be in accordance with regulation/standard imposed, the external auditor should understand and know the rules in preparing audited financial statement that is disclosed.

Agency theory explains the relationship between agent (management of certain business) and principal (business owner). Within the agency relationship, there is a contract in which one person or more (principal) govern other people (agent) to perform a service on a behalf of principal and authorize the agent to make the best decision for the principal (Jensen and Meckling, 1976). The principal can also limit the divergence of interest by providing decent level of incentive to the agent and willing to pay monitoring cost to prevent hazard from agent. The agency theory also contributes as a basic pillar to the accounting role in providing information and it is usually associated with the stewardship role of accounting; thus, it provides accounting with the value of feedback in addition to predictive value.

Researchers found audit delay determinants are profitability, solvability and audit opinion (Leventis and Weetman, 2004; Al-Ajmi, 2008). Profitability is the company's ability to generate profit at the certain level of sales, asset and capital share. Profitability is often used as the measurement of management performance and the efficiency of working capital usage so it can generate profit for the company. Profitability can be good sign for investor (Leventis and Weetman, 2004)

Solvability is the company's abiliy to pay short term and long term debt. Solvability can be seen based on debt to asset ratio as well as debt to equity ratio. A high debt to asset ratio portrays that the company is experiencing financial difficulties; thus, indicating that the company has high risk. Carslaw and Kaplan (1991) first used debt proportion on audit delay study. The result of the study stated that debt to asset ratio proportion might indicate the company's financial health. A higher debt to asset ratio can cause an increase in company's failure that makes the auditor pay more attention to the company's financial report because there is a possibility for the financial statement not to be reliable; thus, the auditor needs longer audit process.

Audit opinion is an opinion given by an auditor to his/her clients -in respect of the audited financial statement to determine whether the financial report is qualified or not. An unqualified audit opinion can affect the audit delay (Turel, 2010).

II. Hypotheses Development

The influence of profitability on audit delay

There are two reasons why companies tend to experience longer audit delay. First, when the profitability is low, the company wants to delay the bad news; thus, company will ask auditor to reschedule the audit assignment. Second, the auditor will be more cautious in the auditing process when he/she believes that the profitability of the company is low, fact which might be due to company's financial failure or management fraud. Therefore, manager's role is very important in terms of the level of company's profitability because the information asymmetry arises when the manager knows better the internal information and company's future prospect, compared to shareholder and other stakeholders.

When there is an increase in profitability the financial report will be published sooner than in the case of a decrease in profitability. The manager wishes to satisfy the investor with good news about profitability (Leventis and Weetman, 2014). The sign of income is also a determinant of timely reporting (Ansah , Leventis, 2006). Based on the explanation above, it can be hypothesized:

H1: There is negative relationship between profitability and audit Delay

The influence of solvability on audit delay

Solvability is the company's ability to pay all its debts, either the long-term or short-term debt. The solvability of a company is measured by comparing the value of debt to the value of assets.

A high level of debt to equity ratio reflects the company's higher financial risk. This risk indicates the possibility that the company cannot repay its debt obligation in the form of principal and interest. A high-risk company indicates that the company is facing financial difficulties. The financial difficulties will affect company's condition in the public eye. Moreover, the management tends to delay the submission of financial statement that contains bad news.

This indicates that the larger the debt to asset ratio, then the longer is the time span required for finishing the audit of the annual financial statement. Based on the explanation above, it was shown that solvability had significant influence on the audit delay.

H2: There is positive relationship between solvability and audit delay

The influence of auditor opinion on audit delay

Companies which were given qualified audit opinion tend to have a longer audit delay since the auditor requires more time and effort to find out the audit procedure when confirming the audit qualification. The provision of a qualified audit opinion involves negotiation with the client, consultation with more senior audit partners or technical staff and elaboration of the scope of audit.

Based on the explanation above, the auditor opinion has a significant influence on the audit delay. A company that was given an unqualified audit opinion has the tendency of wanting to expose its financial statement faster to the public because the auditor stated that the financial statement was presented reasonably and all material elements, financial position, revenue, changes in equity and cash flow of the entity were in accordance with the generally accepted accounting principles in Indonesia. A company that gets another audit opinion besides the unqualified audit opinion, tends to hold its financial statement before its release to the public.

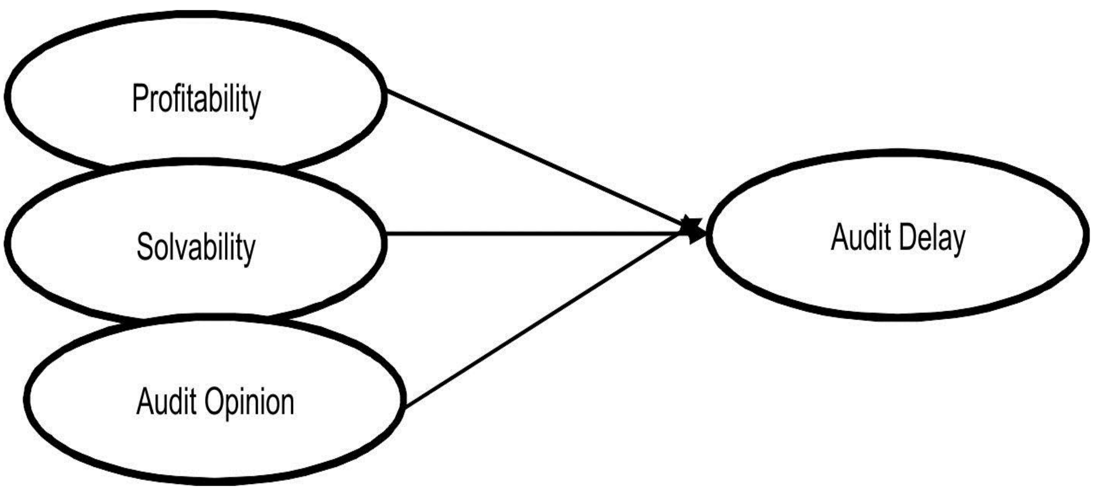
H3: There is positive relationship between audit opinion and audit delay

Research Framework

Referring to literature review and previous studies, hypotheses that will be developed in this study are the implementation of profitability, solvability and auditor opinion. Based on those literature review and previous studies, this study tries to reveal new factors that determine timeliness of the financial statement, which are profitability, solvability and auditor opinion, determinants that become references in improving the result of the study on audit delay.

If depicted in a scheme, the outline of partial and combined hypotheses tested in this study is conducted in the following format:

Figure 1. Research Framework



The framework of research includes; profitability, solvability, auditor opinion as independent variables and the audit delay as a dependent variable.

3. METHODOLOGY

Data

This study analyses 53 companies that published their financial reports from 2011-2014, so the total data of 212.

Variable

The variables used in this study are audit delay, profitability, solvability and auditor opinion. The operational definition of the variables used in this study is as it follows:

Table 1. Operational definitions of variables		
Variables	**Definition**	**Measurement**
A. Independent		
1. Profitability	Company ability to get profit	$\text{ROA} = \frac{\text{net income/loss}}{\text{Total Asset}} \times 100\%$
2. Solvability (Saka and Jarboui, 2016; Mauna and Anis, 2013)	Company's ability to pay all its debts, either long-term debt or short-term debt. The solvability of a company can be measured by comparing debt to assets	$\text{Debt to Asset (DAR)} = \frac{\text{Total Debt}}{\text{Total Asset}} \times 100\%$
3. Audit Opinion DeFond and Lennox (2011), Gunny and Zhang (2013)	Opinion that was given by public accountant	The data are dummy if 0 equals to qualified audit opinion, in this case adverse audit opinion and disclaimer of audit opinion; also, if 1 equals to unqualified audit opinion, in this case unqualified audit opinion with explanatory language)
B. Dependent		
Audit delay	Audit completion's length of time measured from the date of closing of financial year until the date on which the audit report is signed (Iskandar and Trisnawati, 2010)	Audit delay = Audit Report Date – Financial Statement Date

Based on above discussion, we test the following model:

$$\textit{Audit Delay} = a_0 + \beta_1 \textit{Profitability} + \beta_2 \textit{Solvability} + \beta_3 \textit{Audit Opinion} + \varepsilon$$

FINDINGS

Descriptive Statistics

In this study, the data for whom we know the description are profitability, solvability and audit opinion, data on the audit delay of the manufacturing companies listed in Indonesia Stock Exchange in the period of 2011-2014. The result of the descriptive statistics is shown as it follows:

Table no. 2. Descriptive Statistics			
Variable	**Minimum**	**Maximum**	**Mean**
Profitability	-34.59	40.38	7.57
Solvability	3.72	255.42	47.17
Audit Opinion	0	1	0.9
Audit Delay	33	137	75.75

Table no. 2 shows that for the 53 manufacturing companies or 212 firms during the four years of reporting, which were listed on Indonesia Stock Exchange for the period 2011-2014, the mean value for profitability is 4.42, the maximum value for profitability is 40.38 and the minimum value for profitability is -18.58. Moreover, the mean value for solvability is 0.47 while the maximum and minimum value for solvability are 2.55 and 0.03. The mean value for audit opinion is 0.9; the maximum value for audit opinion is 1 while the minimum value for audit opinion is 0.00. The mean value for audit delay is 75.75, which is still under maximum period of four months after end year of financial report (Financial Services Authority (FSA) regulation No. 29/POJK.04/2016 related to the Annual Report for the Issuer or Public Company amended Decision of the Chairman of Bapepam-LK No. Kep-431/BL/2012 on 1 August 2012, concerning Submission of Issuer or Public Company Annual Report). The maximum value for audit delay is 137 and the minimum value for audit delay is 33.

This study divides the firms in two clusters in terms of the audit delay, mening that 13 firms published the audit report in first or two months from the year end (cluster 1) and 40 firms published it in three month from year end (cluster 2).

Table 3. Audit Delay Cluster

	Cluster	
	1	2
Audit Delay	60.40	81.97
Profitability (mean)	11.45	6.04
Solvability (mean)	34.83	53.44
Audit Opinion (mean)	0.88	0.92
Firms	15	38
Firms per Years	60	152

Correlation

To explore the direction and strength of the relationship between the independent variables we undertook the Pearson correlation coefficient matrix. The matrix was presented in Table 4. It can be seen that the correlation coefficient between two independent variables is less than the critical value of 0.80 (Bryman and Cramer, 2011), suggesting that multicollinearity is not a problem.

Table 4. Correlation Among All Variables Used in The Study

Variable	Audit Delay	Profitability	Solvability	Audit Opinion
Audit Delay	1			
Profitability	-0.166*	1		
Solvability	0.195**	-0.198**	1	
Audit Opinion	0.102	0.082	-0.26	1

*Notes: *,** The correlations are significant at the 0.05 and 0.01 levels, respectively (two-tailed)*

To assess the normality, probability plot of the residual method was employed and no serious deviations were found from the diagonal line, the residual from the model seem to have a normal distribution. **Table no. 5** shows that no case in the data set has Cook's distance value higher than 1 (Stevens, 2012), which indicates that no outliers have been found.

As the assumptions of normality, absence of outliers and lack of multicollinearity among the independent variables are met, multivariate test was performed. **Table no. 5** presents multivariate test using OLS regression models.

Table 5. Results of Regression analysis

Variables	B	T	Sig
Profitability	-0.341	-3.225	0.001*
Solvability	0.040	1.443	0.151
Audit opinion	6.115	1.822	0.070**

*Note: *'**Significant at 5% and 10%*

According to Table no. 5, profitability is significant at 0.05 level and audit opinion is significant at 0.10 level. The most significant variable that impacts audit delay is profitability.

The multivariate tests for clusters 1 and 2 are presented in Tables no. 6 and no. 7.

Table no. 6. Results of Regression analysis of Cluster 1

Variables	B	T	Sig
Profitability	-0.366	-1.767	0.083**
Solvability	0.016	0.287	0.775
Audit opinion	1.981	0.434	0.666

*Note: **Significant at 10%*

Table no. 7. Results of Regression analysis of Cluster 2

Variables	B	T	Sig
Profitability	-0.107	-1.187	0.237
Solvability	-0.003	-0.114	0.910
Audit opinion	4.163	1.308	0.193

According to Table no. 6, profitability significantly affects audit delay at 0.10 for cluster 1. According to Table no. 7 profitability, solvability and audit opinion do not affect audit delay for cluster 2.

4. Discussion

a. The influence of profitability on audit delay

The partial test indicates that there is negative relationship influence between profitability and audit delay on firm. Negative relationship means that auditor need more time to do the audit. On the company side, company tend to postpone the bad news about negative profitability.

According to the data analysis, there's different impact of profit on audit delay for firms in cluster one and cluster two. In cluster 1, the negative profit has significant impact on audit delay. It means that the auditor considers the profit when doing the audit on average two months. Otherwise, in cluster 2, negative profit doesn't have significant impact on audit delay. It means that the firms and auditor tend to fulfill the dateline to publish their audit report when the audit process lasts more than two months. The earnings reported after the extended audit process may still suffer deficiencies and create scepticism among investors about earning quality.

b. The influence of solvability on audit delay

The result of the study found out that solvability had no relationship with the audit delay. Although solvability has no relationship with audit delay, from the cluster analysis we find out that the firms in cluster 2 had a higher level of debt than the firms in cluster 1. A high level of debt to equity ratio indicates the company's high financial risk.

A high level of risk shows there is the possibility that the company cannot repay its debt, either the principal or interest. The company's high risk indicates that the company is experiencing financial difficulty. The financial difficulty will influence company's condition in the eyes of public. The management tends to delay the submission of a financial statement that contains bad news.

c. The influence of audit opinion on audit delay

The result of the study found out that audit opinion had no impact on audit delay. Relate with Carson et al (2013) that going concern audit opinion can be presence of a longer audit report lag or on the other hand going concern problems lead to delay in issuing audit opinions. The direction of causality is unclear.

Almost all firms have constantly audit delay every year. Chan et al (2016) find that long audit reporting lags are more likely to have the receipt of non-standard audit opinion in subsequent periods and the firms with extremely long audit reporting lags tend to have more restatements in the subsequent year. Consistency in publishing the audit report becomes an important factor in preventing the investor scepticism.

5. Implication to Research and Practice

The findings indicate that the sample firms have the audit delay under the maximum period, four months after year end. The possible reason is that the firms avoid the delay in publishing the audited financial statements because they want to convince the investors about the position of the company. The findings also indicate that solvability is considered an important factor for the auditor and company in finishing audit.

Conclusion

One aspect of the financial reporting quality is the timeliness. This study provides empirical evidence of the determinant factors of a long audit delay. Findings show that the mean delay of sample is 75.75 days, which is below the maximum period of four months after year end). Profitability is the determinant factor that affects the audit delay. Solvability and audit opinion do not significantly affect the audit delay. This research divides the companies in two clusters. The average audit delay in cluster 1 is of two months and the average audit delay in cluster 2 is more than two months. Profitability has negative relationship with audit delay in clusters 1 and 2, but it only has significant relationship with audit delay in cluster 1. The companies in cluster 2 have higher leverage than the companies in cluster 1.

Future Research

The sample size is relatively small so, the next researcher needs to consider adding the sample size. To enhance the explanatory factors, the next study may consider other factors such as the corporate governance mechanism related to the audit delay. It's also interesting to explore the implications of a long audit delay on the company performance.

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