

Moderating Role of Political Connection Between Audit Evidence and Audit Quality

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Oktri Supyati Jaisyul Usrah, *Nurkholifah Burhanuddin, Grace T. Pontoh, Mediaty

Master of Accounting, Economic and Business Faculty,
Universitas Hasanuddin, Indonesia

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ABSTRACT

This study aims to provide empirical evidence of the influence of the role of political connections as a moderator between audit evidence and audit quality at the Makassar Public Accountant Office. This study uses a quantitative approach and data collection using a questionnaire through a google form at Public Accountant Office in Makassar. The results showed that audit evidence had a significant positive effect on audit quality. The results of this study also show that the moderating variable of political connections cannot significantly weaken the effect of audit evidence on audit quality. This study provides evidence that public accountants at the Public Accountant Office in Makassar feel that audit evidence is an essential factor in the excellent quality of an audit assignment. Implementing a two-tier system can also reduce the degradative effect of political connections on audit quality and reduce agency conflicts in companies.

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ABSTRAK

Penelitian ini bertujuan untuk memberikan bukti empiris pengaruh peran koneksi politik sebagai moderator antara bukti audit dan kualitas audit pada Kantor Akuntan Publik Makassar. Penelitian ini menggunakan pendekatan kuantitatif dan pengumpulan data menggunakan kuesioner melalui google form pada Kantor Akuntan Publik Makassar. Hasil penelitian menunjukkan bahwa bukti audit berpengaruh positif signifikan terhadap kualitas audit. Hasil penelitian ini juga menunjukkan bahwa variabel moderasi koneksi politik tidak dapat secara signifikan memperlemah pengaruh bukti audit terhadap kualitas audit. Penelitian ini memberikan bukti bahwa akuntan publik pada Kantor Akuntan Publik di Makassar merasa bahwa bukti audit merupakan faktor penting dalam kualitas yang sangat baik dari suatu penugasan audit. Menerapkan sistem dua tingkat juga dapat mengurangi efek degradatif dari koneksi politik pada kualitas audit dan mengurangi konflik keagenan di perusahaan.

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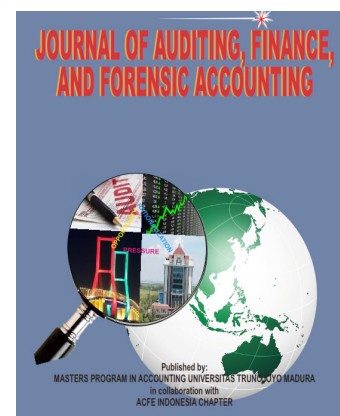
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Keyword:

Political Connection, Audit Evidence, Audit Quality.

1. INTRODUCTION

The Garuda Indonesia airline, which in 2017 experienced a loss, 2018 recorded a phenomenal net profit (Nugroho, 2020; Utami & Kartikasari, 2020), leading to suspicions of manipulating the financial statements of this company. This suspicion was further strengthened by the refusal to sign the financial statements by two Garuda Indonesia commissioners, namely Chairul Tanjung and



Dony Askaria (Bwarleling, 2020; Utami & Kartikasari, 2020). This case eventually culminated in a revision of Garuda Indonesia's financial statements (Christian et al., 2021). Based on a statement issued by the Ministry of Finance, it is known that there were three omissions by Public Accountants in auditing the financial statements in the Garuda case. First, receivables income has been recognised even though, in nominal terms, the company has not received it. It is considered a violation of Auditing Standard 315. Second, the public accountant has not fully obtained audit evidence that is deemed sufficient to recognise the accounting treatment following the substance of the transaction agreement. It leads to a violation of Auditing Standard 500. Third, the public accountant cannot consider the facts after the date of the financial statements as the basis for accounting treatment deemed to violate Auditing Standard 560.

Financial reports provide various kinds of information related to the description of the company's performance. This report is made as a form of internal party accountability to the company's owner. Not only that but financial statements can also be used by other interested parties such as the public, investors, creditors and so on. In agency theory, there is the term agency conflict. This agency conflict can occur when the management (agent) acts according to their interests and forfeits the interests of shareholders (principals) (Jensen, 1976). Therefore, in preparing financial statements, this agency conflict can occur. For example, the management always strives to present good financial reports so that the principal considers their performance reasonable. Therefore, financial statements are prone to manipulation. Meanwhile, the financial reports that external parties want are actual financial reports so that external parties can conduct performance assessments under existing conditions.

This interest difference causes the company owner to be advised to use the services of a third party to examine the reports presented by management. The third-party in question is a public accountant. The purpose of using a public accountant is to assess whether the statement made by management is fair or not. In carrying out the audit process, the auditor must provide a valid and reliable opinion. Therefore, the collection of audit evidence becomes something important. However, audit evidence can be used to express an auditor's opinion.

Mulyadi (2014), states that audit evidence can be used as the basis for disclosure. Therefore, there is a possibility that an auditor will become a target for corrupt actors or officials to cover up their fraud. Of course, this could happen. Therefore, as a public accounting profession that is highly trusted by the public because it is recognised as an independent auditor in supporting its professionalism as a public accountant in carrying out its audit duties. The auditor must be guided by the audit standards set by the Indonesian Institute of Certified Public Accountants (IICPA) to provide good audit quality for clients. This research is necessary because the outside agent (in this case, the director) has a political

background so that it can directly influence the government (Agrawal & Knoeber, 2001).

In the case of Garuda Indonesia, the opinion issued by a public accountant gave a misleading signal about the company's financial condition. It is possible because the audit committee is not active and independent (Abbott & Parker, 2000; Abdel-Khalik, 2002), and the intervention of the board of directors (Alfraih, 2017) has strong political connections. The existence of political connections is indicated by company executives or the largest shareholder (holding 10% of the total shares and having voting rights) who have close political relations (Faccio, 2006). Political connection is a variable that is often linked to several other variables such as effective tax rates (Adhikari et al., 2006), earnings quality (Al-Dhamari & Ku Ismail, 2015; Chaney et al., 2011; Cho & Song, 2017; Harymawan & Nowland, 2016; Hashmi et al., 2018; Narayanaswamy, 2013), tax avoidance (Butje & Tjondro, 2014; Lestari & Putri, 2017), tax aggressiveness (Kim & Zhang, 2016), auditor choice (Cheng et al., 2015; Guedhami et al., 2014; Habib et al., 2017; He et al., 2015; Liu et al., 2017), earnings management (Chi et al., 2016), funding (Cho & Song, 2017; Claessens et al., 2008), firm value (Fisman, 2001), loan contract fees and terms (Houston et al., 2014), audit fees (Wahab et al., 2011), agency cost (Khan et al., 2016) and audit quality (Armadiyanti & Iswati, 2019).

Referring to Armadiyanti & Iswati (2019), research the current study tries to develop political connections as a moderating variable by using the concept of agency. The results showed that audit evidence had a positive and significant effect on audit quality, while political connections did not significantly moderate the effect of audit evidence on audit quality. The findings of this study provide two contributions. First, audit evidence is still crucial for public accountants in Makassar to provide satisfactory audit services. Second, the lack of evidence for the moderating effect of political connections shows that public accountants at Public Accountant Office in Makassar perceive that applying a two-tier system can mitigate the adverse effects of political connections in Indonesia.

2. LITERATURE REVIEW AND HYPHOTESIS DEVELOPMENT

Agency theory according to Jensen (1976), is a relationship between the agent (in this case, management) and the principal (in this case, the business owner). Meanwhile, according to Mursalim (2005), agency theory is part of game theory, a contractual model between two or more parties. Pebriana & Sukartha (2012), state that the primary purpose of agency theory is to explain how the principal and agent can design a contract whose goal is to minimise costs due to asymmetric information and conditions of uncertainty. Meanwhile, for external parties, in this case, the auditor, agency theory can help an auditor understand the problems between the agent and the principal. The auditor's presence is expected to bridge the agent and the principal as a form of the agent's accountability to the principal. In this case, they provide an opinion on the fairness of the financial report prepared by the agent.

Mulyadi (2014), states that audit evidence is information that supports the audit process and the information presented in the financial statements, which the auditor can use as a basis for expressing his opinion. Meanwhile, based on the theory put forward by Bennett, G. B. H & Stefaniak (2015), it is stated that audit evidence must receive the auditor's attention from the audit planning stage to the end of the audit process. Pintasari, (2016) claims that audit evidence can help auditors to be able to produce audit results that are free from deviations and comply with the established audit standards. The more reliable the evidence collected by the auditor, the quality of the audit results will increase. Based on the description above, the authors formulate the following hypothesis:

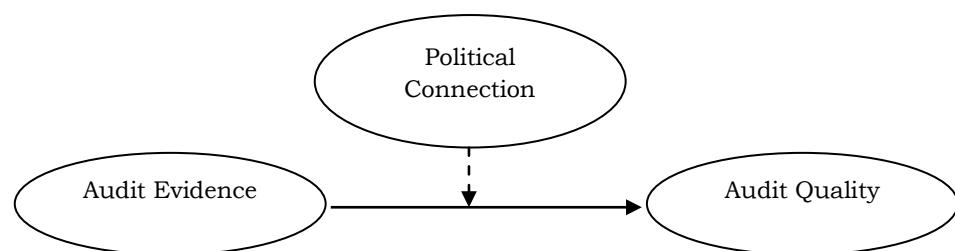
H₁ : Audit evidence has a positive effect on audit quality at the Makassar Public Accounting Office.

Referring to agency theory, according to Rodriguez et al. (2007), companies with political connections are closely related to the emergence of agency conflicts. They tend to minimise the disclosure of crucial information. This statement is also supported by (Al-Dhamari & Ku Ismail, 2015; Chung et al., 2005). They claim that companies with strong political connections tend to have poor earnings due to agency conflicts. It means that it is less likely to obtain audit evidence. The research conducted by Cheng et al. (2015) and Habib et al. (2017), stated that the company's political connections negatively influence auditor selection decisions.

Companies with political connections will tend to choose less qualified auditors (not auditors who are in the top 10) to cover up the company's earnings management behavior (Armadiyanti & Iswati, 2019). It is in line with Khan et al. (2016), which state that boards of directors who have strong political connections can take various advantages due to their proximity to the government. The implication is that they can cover fraud even though the auditor has audit evidence. Based on the description above, the authors formulate the following hypothesis:

H₂: Political connection weakens the influence of audit evidence on audit quality at Makassar Public Accounting Office.

Figure 1 exhibits that the collection of audit evidence (X₁) and the effect on audit quality (Y) is moderated by political connections (X_M).



**Figure 1
Research Conceptual Framework**

3. RESEARCH METHOD

This study uses a quantitative approach using three variables: audit evidence as an independent variable, audit quality as the dependent variable, and political connections as a moderating variable. Audit evidence (X_1) is all information used by the auditor to be used as a basis or reference for the assessment by comparing the suitability of the information with predetermined criteria. Audit quality (Y) is the ability of the auditor to find and report a violation of the accounting system to produce satisfactory and valuable audit reports for its users. Political connection (X_M) is a connection between the government or certain parties with independent auditors for specific purposes.

The measurement of these three variables uses a Likert scale with a score of 1-5. This research was conducted at the Makassar Public Accounting Office. Meanwhile, the study will be carried out for two months, from October to November 2021. According to Sugiyono (2017), the population is a generalisation area consisting of objects or subjects with specific qualities and characteristics determined by the researcher to be studied and then concluded. The population in this study were all auditors who worked at the Makassar Public Accounting Office. In this study, a sample of 32 auditors came from several Makassar Public Accounting Offices and had met the established criteria.

The samples in this study came from various public accounting offices in Makassar, namely Rusman Thoeng Public Accounting Office, Yuniswar & Partners Public Accounting Office, Ellya Noorlisyati Public Accounting Office, Anwar & Partners Public Accounting Office, Drs. Thomas, Blasius, Widartoyo & Partners Public Accounting Office, Ardaniah Abbas Public Accounting Office, S. Mannan, Ardiansyah & Partners Public Accounting Office, and Manaswati Public Accounting Office. The sampling technique in this research is using purposive sampling. According to Sugiyono (2017), purposive sampling is a method of determining respondents to be sampled on specific criteria to get samples that match the specified criteria. The sample criteria in this study are auditors at the Makassar City Public Accountant Office who have at least one year of experience as an auditor. The data analysis techniques used in this research are descriptive analysis, simple regression analysis, and moderated regression analysis.

4. RESULTS AND DISCUSSION

The results of hypothesis testing were carried out using a regression test with the SPSS version 21. The results of hypothesis testing can be seen in tables 1 and 2 below.

$$Y = 19,744 + 0,400X_1 + e$$

The regression equation can be interpreted in several ways as follows. It can be stated that Audit Evidence (X_1) has a significant positive effect on audit quality. It can be seen in the unstandardized beta coefficient of the audit evidence variable (X_1), which has a

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positive value of 0.400. With a significance level of $0.002 < 0.05$. Meanwhile, the adjusted r square value of 0.252 or 25.2% can be interpreted as the magnitude of the effect of the audit evidence variable (X_1) on audit quality (Y). While the remaining 74.8% were influenced or explained by other variables that were not included in this study. Thus H1, which is audit evidence that has a positive effect on audit quality at the Makassar Public Accounting Office is accepted.

$$Y = 19,806 + 0,391X_1 + 1,429X_M + (-0,017)X_1X_M + e$$

From the regression equation, it can be seen that the adjusted r square value is 0.247 or 24.7%. Thus, there was a decrease in the value of adjusted r square, which was initially worth 0.252 or 25.2% for the relationship between the influence of audit evidence and audit quality, to 0.247 or 24.7% with the presence of a moderating variable of political connections. It means that the moderating variable of political connections can weaken the relationship between audit evidence and audit quality, although it is not significant. Thus, H2, namely political connections, weakens audit evidence's effect on audit quality at the Public Accounting Office in Makassar City is rejected because the interaction between audit evidence and political connections does not significantly affect audit quality.

Table 1
Hypothesis Test Results 1

Model	Unstandardized	Standardized	T	Sig.
	Coefficients	Coefficients		
	B	Beta		
(Constant)	19,744			0,002
Audit Evidence (X_1)	0,400	0,526	3,385	0,002
Adjusted R Square		0,252		

Source: Primary Data Processed, 2021

Table 2
Hypothesis Test Results 2

Model	Unstandardized	Standardized	t	Sig.
	Coefficients	Coefficients		
	B	Beta		
(Constant)	19,806		2,984	0,006
Audit Evidence (X_1)	0,391	0,514	2,874	0,008
Political Connection (X_M)	1,429	0,499	0,203	0,840
Mod. X_1X_M	-0,017	0,293	-0,119	0,906
F Test		4,385		
Sig. F		0,12		
Adjusted R Square		0,247		

Source: Primary Data Processed, 2021

Effect of Audit Evidence on Audit Quality

The results of hypothesis testing show that audit evidence has a significant positive effect on audit quality. So, it can be interpreted that the results of this study indicate that audit evidence is the basis of reference for public accountants in Makassar to provide satisfactory financial statement auditing services. It means that the more reliable the audit evidence obtained by the auditor, the better the quality of the audit will be. The findings of this study are in line with agency theory which states that public accountants provide assurance services to mediate agency conflicts between agents and principals.

To carry out an audit process, one of the essential things needed by the auditor is audit evidence to provide good audit quality. In this study, some auditors rely more on audit evidence obtained from external parties because several auditors believe that external parties will provide more reliable audit evidence. Some auditors say that evidence obtained from internal parties will be more reliable because internal parties have improved performance. Audit evidence obtained directly by the auditor through physical examination, observation, and calculations will be more valid and trustworthy than audit evidence that the auditor cannot obtain directly. In an individual audit, the auditor believes that the audit cannot be relied upon if it provides such information. The auditor also proves that the audit must be objective to represent the account or transaction to be examined by the auditor. Of course, as an auditor, work as planned and if the audit evidence collected exceeds the limit, it is very vulnerable to doubts about changing the audit evidence.

The findings of Bennett, G. B. H & Stefaniak (2015), show that audit evidence should receive the auditor's attention from the audit planning stage to the end of the audit process. Considering that the opinion issued by the auditor must be accountable and verifiable, audit evidence has implications for audit quality. In addition Pintasari (2016), also states that audit evidence can help auditors to be able to produce audit results that are free from deviations and comply with the established auditing standards. The more reliable the evidence collected by the auditor, the quality of the audit results will increase.

The Effect of Audit Evidence on Audit Quality By Moderating Political Connection

Based on statistical results, it was found that the presence of a moderating variable political connection could not significantly weaken the relationship between audit evidence and audit quality. The political connection shown in this study is a connection between the auditor and government officials who are also part or shareholders of a company. So when the company is audited, it is hoped that this government official will choose an auditor who has political connections with him. The findings of this study are consistent with the statements of Al-Dhamari & Ku Ismail (2015); Chung et al., (2005); and Rodriguez et al., (2007), which state that

referring to the concept of agency theory, companies with political connections will tend to limit information disclosure and present low-quality earnings as a result of agency conflict.

Companies in Indonesia adhere to a two-tier system on their boards of directors. So regardless of whether there is a political connection, the supervisory board will still appoint a good quality public accountant from the Big 4 or an industry specialist public accountant to produce good audit quality. This statement is supported by the research results of Guedhami et al. (2014) and Narayanaswamy (2013), who found that companies will continue to appoint quality public accountants to get good audit quality as well. Cheng et al. (2015), stated that companies with political connections tend to choose unqualified auditors (non-top ten auditors) to cover their earnings management behavior. Habib et al. (2017), also stated that politically connected companies in Indonesia tend to appoint auditors who are of poor quality/not from the Big 4. The results of this study refute both statements above.

There are several reasons why political connections cannot weaken the effect of audit evidence on audit quality—first the implementation of a two-tier system on the board of directors of companies in Indonesia. With the performance of this system, there is more control over the behavior or decisions made by company executives compared to using a one-tier system (Rajablu, 2016). It is possible because duties are separated between the executive and the supervisory board (Jouber, 2021). The implication is that there is oversight of options exercised by the executive in a two-tier system, and the supervisory board can monitor and provide independent advice to management (Bezemer et al., 2014). Pham & Tran (2019), stated that implementing the two-tier system encourages companies to disclose more information than the one-tier system, for example, CSR information. Second, with more and more information being released to the public, companies get greater scrutiny. Consequently, the company will improve transparency, GCG, financial report quality, and audit quality to reduce agency conflicts and criticism from the crowd Armadiyanti & Iswati (2019).

5. CONCLUSIONS AND SUGGESTIONS

Based on data analysis, hypothesis testing, and discussion of the research results that have been described previously, the conclusion in this study is that audit evidence has a significant effect on audit quality. It means that the more reliable the audit evidence obtained by the auditor, the better the quality of the audit will be. This study also reveals evidence regarding political connections that cannot moderate or weaken the relationship between audit evidence and audit quality significantly. This study provides evidence that political connections as a moderating variable cannot produce a tendency to minimise the disclosure

of crucial information. It means that it is possible to obtain audit evidence that will undoubtedly impact the quality of the resulting audit.

This study has limitations on the data collection process. The study should have used a sample of internal government auditors. Still, due to the busyness of the internal government auditors, time constraints required this research to be completed to fulfil the final project, the researchers decided to carry out research at the Makassar Public Accountant Office. Therefore, future researchers are expected to carry out a similar research model but use an internal sample of government auditors and expand the distribution of questionnaires so that the number of samples obtained is much larger than this study so that research results can be generalised. If possible, the research can be expanded by adding additional samples and independent variables that have not been studied that are moderated by the political connection variable.

This research contributes both theoretically and practically. Theoretically, this study can partially support the application of agency theory, especially on the effect of audit evidence on audit quality, but fails to support the effect of the interaction between audit evidence and political connections on audit quality at the Makassar Public Accounting Office. Practically, this study's findings support that implementing a two-tier system can reduce the adverse effects of political connections and agency conflicts, especially in developing countries. To enhance the prevention mechanism of political connection, companies have to implement better good corporate governance practices.

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***Coressponding Authors:**

Author can be contacted on E-mail: ifahnurkholifah1@gmail.com