

The Effect of Audit Quality Attributes on the Cost of Equity Capital (Empirical Study on Manufacturing Companies Listed In Indonesia Stock Exchange Year 2014-2016)

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Abstract: This research aims to examine and analyze the effect of audit quality attributes on the cost of equity capital. The audit quality attributes is measure by the size of the public accounting firm, the industry specialty auditor and audit tenure. Meanwhile, the cost of equity capital is measure by using the PE Ratio. The population in this study is all manufacturing companies listed on Indonesia Stock Exchange on 2014-2016. Sampling technique using purposive sampling method obtained by samples 237 companies during the year observation. The result showed that the variable size of the public accounting firm and the industry specialization of the auditor negatively affect the cost of equity capital. Meanwhile, audit tenure does not affect the cost of equity capital. Based on the determination coefficient test (R^2) obtained the coefficient of determination with adjusted R^2 of 0,527. These result show that 52,7% of variables cost of equity capital can be explained by the size of the public accounting firm, the industry specialization of auditors and audit tenure. While, the rest of 47, 3% is explained by other factors outside the model in this research.

Keywords: [audit quality attributes ; cost of equity capital]

1. INTRODUCTION

The separation of ownership and control of the company caused the asymmetry of information between company managers and investors (Hajiha & Sobhani, 2012). Currently, the transparency and the quality of financial information is the basis of economic decision-making of investors, creditors, and other users. Auditing reduces the information asymmetry that exists between managers and stakeholders of the company by allowing outside parties to verify the validity of the financial statements (Hajiha & Sobhani, 2012).

According (Khurana & Raman, 2004) Audit is a requirement for users of financial statements. The role of the monitoring of audits designed to improve information about the company. This will reduce the asymmetry of information

between the company and investors. The greater the risk of information encountered by investors, the greater the value the quality of audits. Audit information reduces the risk faced by investors because it allows them to verify the validity of the financial statements. Any warranty on the quality audit will lower the cost of equity capital.

Specialization industry Auditors as differential, this strategy gives Auditors a competitive advantage. Thus, the specification of the industry was able to give a better auditor quality. An auditor independence will be lost if there is a very close relationship between the Auditors with clients because it will influence the opinions and attitudes of the auditors themselves.

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because it will influence the opinions and attitudes of the auditors themselves. One of the most influential is auditing a long tenure.

Auditing a long tenure would give rise to a sense of emotional kinship between the public accounting or with the client as a result, the quality of the audit work the auditor competence and will decrease.

The cost of equity capital is the return expected by investors as they invested money in the company. In other words, the cost of capital earned from trade between risk and return. This is an important fact that must be considered by the manager that the risk information is reported to affect the rate of return investors. The risk of information depending on the level of classified information and the accuracy of the information reported.

(Hajiha & Sobhani, 2012) stated that research conducted (Khurana & Raman, 2004), Hope et al (2008), Ahmed et al (2008), Stoke et al (2009) provide evidence of a direct relationship between the different dimensions of quality audits are related positively with a cost of equity capital.

According to (Jensen & Meckling, 1976) in (Setiawan & Daljono, 2014) Agency theory is the relationship that occurs in a contract between a party with other parties. In the contract, there are two parties namely the owner (the principal) and an agent is give a party authorized by the owner to take a decision in accordance with the interests of the principal. Agency theory assumes that all individuals Act in their own interests. Shareholders acting as principals assumed are interested only in the financial result increased or their investment in the company. While the agents assumed to receive gratification in the form of financial compensation and

the terms that accompany such a relationship.

(DeAngelo, 1981) indicated that big Auditors ten to deliver high-quality audit services on certain clients rather than small Auditors because of dependence in economic matters the auditor on the client can be ignored for Auditors and Auditors have great larger losses (losses will lose its reputation) in case of failure of the audit, the Auditors compared to small.

Balsam and Krishnan (2003) in (Desiliani & Meiranto, 2015) says that the auditor specialists tend to invest more in the recruitment and training of staff, information technology and audit technology more sophisticated than the non-Auditors specialist. Industrial specialist Auditors also tend to have an incentive to keep their reputation and avoid damage to reputation. This shows that the specialist auditor industry providing quality higher than the audit the auditor of non-specialist. As a result, they tend to be not in the intervention by representatives of management.

After several years of auditor audit services to clients that will generate a close sense of family then can impact the decline in the quality of financial reporting. Audit the audit resulted in the tenure of high quality, so that should reduce the risk of information and produce a cost of equity capital is lower.

This research aims to (1) prove that relationship between the size of public accountant firm against the cost of equity capital. (2) Prove that there is a relationship between audit industry specialities against the cost of equity capital. (3) Prove that there is relationship audit tenure against the cost of equity capital.

2. THEORITICAL FRAMEWORK

The theoritical framework of this research is illustrated as follows:

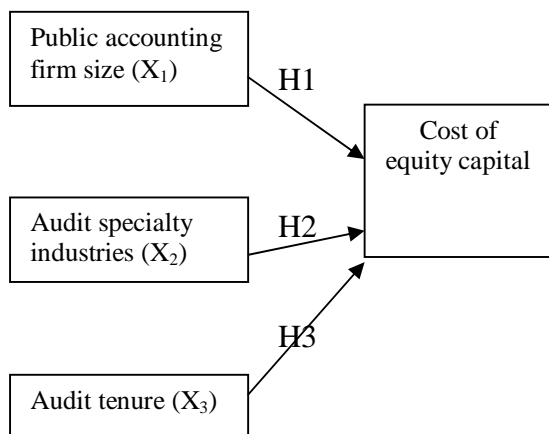


Figure 1. Theoretical Framework

3. RESEARCH METHODS

Research method using the method of content analysis, data type used is the quantitative data. The source data used are secondary data. The data collection method used is the documentation. Data analysis technique used was multiple linier regression analysis. The population in this study was all company listed on Indonesia stock exchange year 2014-2016 by using the purposed sampling.

Data Analysis Technique

Data analysis techniques used in this research are as follows:

- a. Descriptive statistics on do to get an overview of the variables within a research
- b. A classic Assumption Test
 - 1) Test of Normality was done to know that normally distributed data to regression
 - 2) Autocorrelation test was conduct to find out the residual in a single observation.
 - 3) Multicollinearity test aims to find out there or whether the

same relationship between free variables used.

- 4) The heteroskedasticity test aims to analyze, the occurrence of inequalities between the residual.
- c. Multiple linear regression analysis is the technique through a coefficient parameter to know the magnitude of the influence of variables is independent of the dependent variable. The regression model in this research:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e$$

Information:

Y	: The cost of equity capital
X1	: Size of public accounting firm
X2	: Auditor Industry Specialities
X3	: Audit Tenure
α	: constant
$\beta_1 - \beta_3$: Regression coefficient
e	: error

- d. The F-test is done to see the impact of influence between independent variables to dependent variables simultaneously
- e. T-test was conduct to know the influence of partially dependent variable against the independent variable.
- f. Determination of coefficient of test done to measure the proportion of the variation in the free variables in explains zero regression.

4. RESEARCH RESULT

Result of Data Collection

The object of this research is a company listed on Indonesia Stock Exchange in 2014-2016. This research using method of purposive sampling so at 237 companies was outstanding research into the sample. The cost of equity capital measured with PE Ratio.

$$\text{PE Ratio} = \frac{\text{Price Per Shares}}{\text{Earning Per Shares}}$$

Figure 2. PE Ratio

Classical Assumption Test Result

The Descriptive Statistics Analysis

The result of the analysis of descriptive the public accounting firm size, Audit specialty industries, Audit tenure and the cost of equity capital is serving the following:

Table 1 Summary Of Descriptive Statistic

	N	Min	Max	Mean	Std Dev
UKAP	237	0	1	0,37	0,483 21
SPES	237	0	1	0,44	0,498 78
Tenure	237	1	3	2,63	0,698 01
BME	237	- 835,7 1	933,3 3	30,62 37	119,0 2110

Source of Data Processed 2017

The average size of a public accountant at the manufacturing companies listed on the Indonesia stock exchange (IDX) in 2014-2016 of 0.37 standard deviation of 0.48321 to or greater than the average value, thus indicating that research data of the size of the public accountant. The average value of specialization industrial auditors at manufacturing companies listed on the Indonesia stock exchange (IDX) in 2014-2016 of 0,44 with standard deviation of 0.49878 to or greater than the average value, thus indicating that research data of specialization industry Auditors varies. The average of value audit tenure at manufacturing companies listed on the

Indonesia stock exchange (IDX) in 2014-2016 of 2.63 with a standard deviation of 0.69801 or smaller than the average value, thus indicating that the research data audit of tenure does not varies. The average of value of the equity cost of capital in the manufacturing companies listed on the Indonesia stock exchange (IDX) in 2014-2016 of 30.6237 with a standard deviation of 119.02110 to or greater than the average value, thus indicating that the data the study of the equity cost of capital varies.

Table 2 Frequency and Percentage of Dependent Variable

	Variable	Frequency	Percentage
UKAP	Big 4	87	36.7%
	Non Big 4	150	63.3%
	Sum	237	100 %
SPES	Specialty	105	44.3 %
	Audit	132	55.7 %
	Non Specialty	237	100 %
Tenure	Audit less	57	24.1 %
	3 years	180	75.9 %
	Audit with 3 years	237	100 %

Source of Data Processed 2017

Classic Assumption Test

A classic assumption test result that include a test of normality, multicollinearity, heteroskedastic, and autocorrelation are presented in the table bellowed:

Table 3 Summary of Normality Test

Variable	N	Kolmogo rov- Smirnov Z	Sig.	Descri ption
Undstandar dized	2 3	0,630	0,05	Norma 1
Residual	7			

Source of Data Processed 2017

From table 3 it is known that the Kolmogorov-Smirnov test showed 0,05 significance. So the regression model has a normal distribution. So in inclusion, normally distributed data and can move on to next test. The next test is the multicollinearity table shown bellow:

Table 4 Summary of Multicollinearity

Variable	Tolerance	Variance Inflation Factor (VIP)	Description
UKAP	0,806	1,240	No Problem Multicollinearity
SPES	0,925	1,181	No Problem Multicollinearity
Tenure	0,867	1,154	No Problem Multicollinearity

Source Data Of Processed 2017

Based on the above table, the value of tolerance all variables are above 0,1 and the value VIF is less than 10 so that it can be concluded there is no Multicollinearity between the variables.

Table 5 Summary of Heteroskedastic

Variable	Sig	Std	Description
UKAP	0,521	0,05	No Problem Heteroskedastic
SPES	0,443	0,05	No Problem Heteroskedastic
Tenure	0,322	0,05	No Problem Heteroskedastic
BME	0,203	0,05	No Problem Heteroskedastic

Source of Data Processed 2017

Based on the table note that the results of the heteroskedastic on the value Sig Tailed is greater than 0,05 so it can

be said that there are no problem heteroskedasticity.

Autocorrelation test the result can be seen in the table bellowed:

Table 6 Summary of Autocorrelation

DW	Du	dL	4-dU	4-dL	Description
2,000	1,763	1,813	2,237	2,187	No Problem Autocorrelation

Sourced of Data Processed 2017

From table 6 above known values of dL is 1,763 and dU is 1,813 and value of 4-dU is 2,187 and 4-dL is 2,237. From the calculation of the value of DW=2,000 between dU=1,763 and 4-dU=2,237, so that it can be concluded there is no autocorrelation.

Table 7 Summary of F Test

F count	Sig.	F table	Description
7,453	0,000	2,640	Accepted

Sourced of Data Processed 2017

Based on the above table, the value of F is count 7,453. The value of F tables retrieved from table statistic F test with sig 0,05 with df 1 (number variables-1) = (4-1)= 3 df2 obtained from (n-k-1) = 237-4-1 = 232 (n is the number of data and k is the number of independent variables). The result obtained for F count was 7,453 > F table value 2,640, then accepted the H1 and Ho are rejected.

Table 8 Summary of t Test UKAP

Variable	t	Sig	Stand ar	Description
(Constant)	-9,250	0,00	0,05	
UKAP	-2,027	0,01	0,05	Accepted

Sourced of Data Processed 2017

Based on a test of t, the t value obtained of -2.027 indicates that the size of the public accountant has a negative direction and obtained the value of Standart < 0.05 (0.01 < 0.05) then the Ha received. It can conclude that the size of the public accountant significantly negative effect on the equity cost of capital.

Table 9 Summary of t Test SPES

Variable	t	Sig	Standart	Description
(Constant)	-2,237	0,00	0,05	
SPES	-1,972	0,03	0,05	Accepted

Source of Data Processed 2017

Based on a test of t, the t value obtained of -1,972 indicates that the audit industries specialty has a negative direction and obtained the value of Standart < 0.05 (0.03 < 0.05) then the Ha received. It can conclude that the audit specialty industries significantly negative effect on the equity cost of capital.

Table 10 Summary of t Test Audit Tenure

Variable	T	Sig	Standart	Description
(Constant)	-2,783	0,00	0,05	
Tenure	1,723	0,21	0,05	Rejected

Sourced of Data Processed 2017

Based on a test of t, the t value obtained from 1.723 audits showed that tenure has a positive direction and obtained the value of sig of > 0.05 (0.212 > 0.05) then Ha was rejected. It can be conclude that the audit of tenure does not affect significantly towards the cost of equity capital.

The result of multiple linear regression analysis using SPSS can be seen the table bellowed:

Table 11. Summary of Multiple linear Regression

Variable	B	Sig
(Constant)	-2,237	0,00
UKAP	-0,363	0,01
SPES	-0,135	0,03
Tenure	1,174	0,21

Sourced of Data Processed 2017

Based on the result of regression analysis obtained by the following equation :

$$Y = -2.237 - 0.363 X_1 - 0.135 X_2 + 1.174 X_3$$

Determination of coefficient of test results can be seen in the table bellowed:

Table 12 Summary of Adjusted R Square

R	R Square	Adjusted R Square	Std. Error of the Estimate	Description
0,760	0,577	0,527	0,88573	Influential 52,7 %

Source of Data Processed 2017

From the table above it can be seen the value of R is 0,760. This means that the correlation between the size of public accounting firm, audit industry specialist and audit tenure against the cost of equity capital and that value 0,527 approaching 1 means going on the dependent variables against the correlation between independent variables. While the value of R² obtained was 0,527 or 52,7 % this means that the percentage of the contribution to the influence of variable size of public accounting firm, audit industry specialities and audit tenure against the cost of equity capital 52,7 %, while the rest is the influence of the other variables that are not included in this research.

Discussion

- a. The effect of size public accounting firm on the cost of equity capital

The size of the public accountant significantly negative effect on the equity cost of capital. The results of this research are consistent with research conducted by (Fernando, Abdel-Meguid, & Elder, 2010), (Desiliani & Meiranto, 2015), (Setiawan & Daljono, 2014). This is because the Big 4 only selecting the best services in the audit. The best service it will give rise to investor confidence. Trust given this will reduce the cost of equity capital. The public accounting firm of the Big 4 is a public accounting firm of a good quality, so it is assume that owned auditor has the ability and attitude of independence. As a result, they tend to be not in the intervention by representatives of management.

- b. The effect of auditor's industry specialization on the equity cost of capital.

The auditor's industry specialization significantly negative effect on the equity cost of capital. The results of this study are in line with research (Hajiha & Sobhani, 2012), (Fernando, Abdel-Meguid, & Elder, 2010), (Herusetya, 2012). According to Balsam & Krishnan (2003) in (Hajiha & Sobhani, 2012) States that the auditor specialists tend to invest more staff training and recruitment services, information technology, and technology audit cutting edge than the Auditors of non-specialists. An auditor who is a specialist in the industry also tends to have an incentive to protect their reputation capital and avoid damage to reputation.

- c. The effect of audit tenure on the cost of equity capital

The audit tenure no effect on the equity cost of capital. The results of this study are in line with (Suparno & Kiswara, 2013), (Desiliani & Meiranto, 2015), (Arta & Sari, 2013). According (Desiliani & Meiranto, 2015) stating that there is an indication of a positive relationship between audit tenure with equity cost of capital. Based on the results of the audit of research, tenure can enlarge equity cost of capital. The old Alliance auditor 's assessment can lead to a growing bias against the potential risk of the company can valuated investors increased more than expected rate of return increased.

Conclusion

The results of testing hypotheses 1 and 2 which States the size of the public accountant to the equity cost of capital, and industrial specialties auditor effect on equity capital costs supported by empirical evidence with a level of significance of 5%.

The results of this study indicate that (1) size accountant public firm Big 4 prioritizes the best services in the audit. The best service it will give rise to investor confidence. Trust given this will reduce the cost of equity capital. (2) Specialty industry Auditors usually have a lot of clients engaged in the same field will have a lot of experience and understanding of the special audit risks in the industry that can reduce the cost of equity capital. (3) The Audit of tenure has no effect on the equity cost of capital. This is in line with research (Suparno & Kiswara, 2013), (Desiliani & Meiranto, 2015) and (Arta & Sari, 2013) there is an indication of a positive relationship between audit tenure with equity cost of capital. The old Alliance auditor 's

assessment can lead to a growing bias against the potential risk of the company so can valuated investors increased more than expected the rate of return increased.

The company is expect to further realize the importance of the quality of an audit in the future so that conflicts between ownership and control that may cause the information asymmetry and the problems that increase the cost of capital requested by an investor can be overcome. The company can fix these conflicts by publishing credible financial statements.

Suggestions that further research is needed to develop the next can do is research sampling not only from the manufacturing company but also other industries such as LQ45, real estate, banking or telecommunications and increased research into the period of 5 years, so that subsequent research results better.

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