

The Relationship between Auditor Partner Tenure, Auditor Industry Specialisation, Firm Complexity and Audit Fee

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This research aims to analyse the influence of audit partner tenure, auditor industry specialisation and company complexity to audit fees. This research uses the quantitative approach and secondary data to measure variables to be studied. This research data consists of financial reports and annual reports. The selection method of the sample is the purposive sampling method. The population in this research were non-financial companies listed on the Indonesia Stock Exchange (IDX) from 2015 until 2017 with 544 observations being used as samples. This research was investigated using multiple linear regression analysis with SPSS 23 software. The result of the t-test with $\alpha = 0.05$ indicates that auditor industry specialisation and company complexity has an impact on audit fees, while audit partner tenure has no impact on audit fees.

Key words: *Audit Fees, Audit Partner Tenure, Auditor Industry Specialisation, Company Complexity.*

Introduction

The number of public companies in Indonesia is increasing every year. These companies must provide financial reports in accordance with applicable accounting standards. Financial statement information is an important element for investors and business as a tool for decision making (Hasibuan et al, 2017). The audit committee also plays an important role in monitoring the company's finances in the reporting process. The audit committee meets regularly with the external auditors and internal financial managers to review the financial statements, audit processes, and internal controls of the company (Bukit et al, 2009). To be useful, financial statements must contain qualitative characteristics that are in accordance with accounting

standards (Abdilah et al, 2019). To ensure this, public accounting services are needed. Audit services generate audit opinions in accordance with the auditor findings. High audit quality requires high audit fees — audit fees are fees received by public accounting firms after carrying out audit services. The definition of audit fees is limited to costs paid to external auditors and does not include salaries paid to internal auditors (Simunic, 1980). The Indonesian Institute of Certified Public Accountants (IAPI) issues Management Regulation No. 2 of 2016 concerning the determination of the amount of the audit fee.

Guidelines are issued by IAPI as a guide to find out the amount of audit fees that must be issued to clients appropriately. In setting audit fees, Public Accountants must consider matters including client needs, statutory duties and responsibilities, independence, levels of expertise, responsibilities inherent to work performed by external auditors, the level of complexity of the work, the amount of time required by the auditor to complete the work, and the agreed fee basis. The service fee is related to the amount of time spent completing work, the value of the services provided to the client or to the relevant public accounting firm. In the event that service fees are not related to the amount of work time, members must submit an Engagement Letter that at least contains the objectives, scope of work and approach and methodology, and the basis for determining the amount of service fees (or estimation of the amount of service fees) as well as the manner and/or payment terms. In addition, based on IAPI rules, according to the audit pricing theory it says that the external audit fee is measured in quantity (Q) and price (P). Quantity is hours worked and price is the average level of billing hours worked. It is assumed that each portion of fixed costs is minimal relative to overall costs. The purpose of this theory is that audit costs are measured by the time taken by the auditor in completing the work. The longer the audit, the more expensive, and vice versa.

Audit tenure is the length of time of the client's audit engagement with the auditor. In Indonesia it is regulated that the Auditor can audit clients for a maximum of 3 years, in accordance with the rules of the Financial Services Authority (OJK) No. 13 / POJK.03 / 2017 concerning the Use of Public Accountant Services and Public Accounting Firms in Financial Services Activities, which states that those who carry out financial service activities are obliged to limit the use of audit services to the annual historical financial information from the same public accountant for a maximum of 3 (three) consecutive book years. According to Kealey (2007), the longer the auditor's working period, the more the auditor understands the company's condition, making it easier for the auditor to ensure accurate financial reporting.

Industry Specialisation Auditors are auditors who have experience auditing clients in the same industry. Andi (2018) argues that audit firms that have specialised industry teams are supported by a management database, work programs and specific training. Specialisation has an important role in auditing because it can increase efficiency and effectiveness in the audit process. Industry specialisation refers to the accumulation of specialised knowledge gained

from serving many clients in the same industry (Gul, Fung, & Jaggi, 2009). Public Accountant Firms that have industry specialisation certainly charge a higher audit fee.

Firm complexity is the complexity of transactions that exist in the company. The complexity can be due to the number of subsidiaries, the number of branches of the company, and transactions using foreign currencies owned by the company (Rukmana et al., 2017). When the company experiences significant growth and increase in its business operations, companies tend to expand their business by establishing subsidiaries. A subsidiary in business affairs is a company that is controlled by a higher company. The number of subsidiaries can increase the complexity – the auditor encounters more complication in conducting the audit process. The higher the level of firm complexity, the higher the audit fee because the auditor needs more time to audit.

Literature Review and Hypothesis Development

Audit Pricing Theory

The testing function performed by the auditor is an important part of the company's monitoring system and can be expected as an important element of the governance system. Audit pricing is a consequence of the auditor's assessment and testing of the client's control environment, as well as meeting client demands for better audit quality and leading to increased audit costs (Nasih et al, 2019). Auditors are required to be able to detect fraud in order to provide adequate guarantees that financial management is free from material misstatement (Sihombing, 2019). Simunic (1980) argues that external audit fees are measured by quantity (Q) and price (P), where quantity is hours worked and price is the average level of billing hours worked. It is assumed that each portion of fixed costs is minimal relative to overall costs. In a competitive market assumption, the audit fee submitted to the client will show an estimate of all costs required by the auditor in providing assurance services that the financial statements are in accordance with applicable accounting standards.

Audit fees are the unit price and quantity of audit services requested by the audit firm. The definition of audit fees is limited to costs paid to external auditors and does not include salaries paid to internal auditors (Simunic, 1980). Service fees that are too low or significantly lower than those imposed by the predecessor auditor/ accountant or submitted by other auditors/ accountants will raise doubts about the ability and competence of members in applying applicable technical and professional standards.

Auditors charge higher fees for higher quality audits. If experienced auditors make better decisions as suggested by experimental research, they can increase audit costs to better reflect their audit quality better. This difference in quality can result in higher audit fees being charged (Palmrose, 1986).

Auditor Partner Tenure

Auditor partner tenure is the length of the auditor's engagement with the client. (Simanora et al, 2019). Auditors who have long-term assignments will encourage the creation of knowledge and experience of the audited company so as to improve audit quality because they are considered to be more aware of the company's condition. Previous research reports that length of service can affect independence. Proponents of this issue argue that the longer the auditor retains their clients, the less the auditor can maintain their independence (Nasution, 2013). According to Kealey (2007), if the auditor subsequently views the length of the previous auditor's tenure with the client as a risk factor, then, costs must be adjusted. The higher the risk factor, the higher the audit fee. Another perspective from auditor rotation is that auditor rotation can increase initial costs through auditor changes (Widyaningsih et al, 2019).

Industry Specialisation Auditor

The term Industry Specialisation Auditor means that the auditor has experience in auditing clients in the same industry. Auditors' expertise in the industry is an important factor in reducing risk and improving audit quality (Cenker and Nagy, 2008). Auditors who have industry specialisation certainly set the audit fee to be higher for high audit quality. Chen (2001) conducted a study that found that industry specialist auditors charge higher audit fees. Auditor expertise in an industry is an important factor in reducing litigation risk and increasing auditor retention and audit quality (Cenker and Nagy, 2008).

Firm Complexity

The complexity of the company is related to the complexity of transactions in the company. The complexity can come from transactions that use foreign currencies, the number of subsidiaries and branches, the number of segments, as well as the existence of business operations abroad (Rukmana et al, 2017). The development of the company can be seen from the number of subsidiaries. More and more subsidiaries increase the complexity of audits conducted by auditors, so that it will increase audit fees because auditors will need more time in auditing financial statements. Mohammadi (2018) argues that there is a relationship between the number of subsidiaries and audit fees, whereas in contrast, the research conducted by Suharli (2008) found that there is no positive influence of subsidiaries on independent audit fees.

Previous Research

Kealey (2011) conducted a study of the effect of audit partner tenure on audit fees that occurred in the ex-Andersen case. The conclusion of the study is that the fees paid are influenced by the previous auditor. Previous auditors are considered to have risk factors, so the fees paid must be

adjusted to the risk of the previous auditor. The high risk borne by the auditor will subsequently have an impact on the high audit fee.

Kikha (2015) examines determinants of audit fee evidence from Jordan. Kikha argues that audit partner tenure is not related to audit fees, this is because of the *auditor's* tenure, audit risk and audit fees. The researcher also points out that there is a negative relationship between financial risk and audit fees. Also, there is no relationship between audit tenure and audit fees. Chen (2001) conducted a study of how audit fees are influenced by auditor industry specialisation. The results of his study prove that specialist auditors in unregulated industries charge higher audit fees compared to specialist auditors in regulated industries.

Cahan et al (2011) conducted a study of how industry specialisation affects two variables, namely audit fees and discretionary accruals. In his research he found that specialist auditors who audit clients in small amounts because they have product differentiation, offer high audit quality, thus charging higher fees. According to Immanuel and Yuyetta (2014), the more subsidiaries owned, the greater the audit fee paid to the auditor. This is because the auditor needs more time to complete his task, so it will affect the amount of audit fees paid by the company.

The Effect of Audit Partner Tenure on Audit Fees

The relationship between Audit Partner Tenure and Audit Fee is rarely examined. Audit Partner Tenure is the length of time a public accountant has been providing audit services to its clients (Fanny, 2007). The auditor in the study is defined as a public accountant who signs the audited financial statements. A public accountant who has a long-standing engagement has the advantage that the auditor better knows the company's condition so that it does not require an excessive time. However, the longer the tenure of the auditor, the less independent they are deemed to be. The latest Financial Services Authority (OJK) regulation 2017 limits public accountants to audit for a maximum of 3 consecutive years. This regulation is expected to increase the level of independence. According to Kealey (2007), a high audit fee is influenced by the risk of the previous auditor. The higher the audit risk, the higher the audit fee. This is following the Audit pricing theory. According to Simunic (1980), high risk requires long working hours, so it requires more time, which can increase audit fees. It is inversely proportional to the regulation issued by the Financial Services Authority that the maximum tenure for public accounting is three years in a row, so it is considered that audit partner tenure is not affected by audit fees due to these limitations.

H1: Audit Partner Tenure affects Audit Fee

The Effect of Industry Specialisation Auditors on Audit Fee

Industry Specialisation Auditing is the auditor's special expertise in certain industries. This expertise creates its own value to increase audit fees. This study explains that the more specialised auditors are considered to have better business knowledge so that the audit effort expended will be lower, along with a lower audit fee. This is in contrast to some other previous studies seen from the supply-side theory of audit fees, which show that audit firms view audit quality as the main factor determining audit fees. The higher quality audit requires more effort and higher fees. In accordance with Arens et al. (2011), specialist auditors are auditors who have deep industry-related knowledge and have a lot of experience in the industry. They are expected to provide high assurance audit services.

H₂: Audit Industry Specialisation Affects Audit Fee

The Effect of Firm Complexity on Audit Fee

Some audit assignments are considered as complex and difficult, while others consider them as easy (Jiambalvo and Pratt, 1982 in Arifuddin, 2014). The complexity of the task in this study is defined as a complex task, consisting of many parts that are varied and interrelated to each other. In carrying out its complex functions, the auditor as a member of the audit team requires skills, abilities, and a high level of patience. An increasingly complex audit task will have an impact on higher audit fees. Companies that are developing well generate a significant increase in business operations, with many subsidiaries having a higher level of complexity due to the large number of transactions that must be audited. The number of transactions that need to be audited requires a longer audit time, according to the audit pricing theory – which is the length of working hours can increase audit fees – so that more transactions require a longer time and will increase the audit fee. Chandra (2015) states that complexity has a positive effect on audit fees. This means that the complexity of companies that will be audited will increase audit fees that must be paid by companies. This can be understood because the auditor requires more time and effort to complete the audit of the financial statements: thus the audit fee is higher.

H₃: Firm complexity affects audit fees

Methodology

This research uses quantitative methods that are causal associative. The definition of quantitative methods that are causal associative, according to Sugiyono (2013), is a study that aims to look for the influence and relationship between two or more variables consisting of independent variables (X) and dependent variables (Y). This study aims to examine the effect of independent variables, namely: audit tenure, auditor industry specialisation, and company

complexity on the dependent variable, namely audit fees. This data was obtained from all companies engaged in the non-financial industry sector that included an audit fee for the current year, and the previous year which was listed on the Indonesia Stock Exchange (IDX). The period of annual financial statements issued by the company is 31 December 2015-2017. The criteria used for sampling are as follows:

1. The company is listed on the Indonesia Stock Exchange and is not included in the financial industry category.
2. Non-Financial companies that were listed in the 2015-2017 period
3. Companies that disclose the amount of audit fees paid to external auditors.
4. Companies that disclose information and data related to the variables needed in this study.

This study uses several control variables: the control variable is a variable that is controlled or made constant so that the influence of the independent variable on the dependent variable is not influenced by external factors or other factors not examined (Anshori & Iswati, 2009). The control variables used are Return On Assets (ROA) and Company Size.

In this study, auditor tenure is calculated from the number of consecutive years of the auditor-client relationship, starting from one (if the current year is the first year of involvement with the current auditor). Industry Specialisation auditors are measured by a dummy variable, given a score of 1 if the percentage is more than 10% and a score of 0 if less than 10%. The complexity of the company is measured by the number of subsidiaries.

Audit Fee variable is measured by Natural Logarithm of Audit Fee. This study uses multiple linear regression to find the correlation between independent variables with the dependent variable. To investigate the effect of auditor tenure, auditor industry specialisation and company complexity on audit fees, the equation model is carried out as follows:

$$AFEE = \alpha + \beta_1 PTENURE + \beta_2 SPEC + \beta_3 TNR + \beta_4 KMP + \beta_5 ROA + \beta_6 SIZE + \varepsilon$$

Description:

AFEE = Audit Fee

α = Constant

$\beta_1 \beta_2 \beta_3 \beta_4 \beta_5$ = Regression Coefficient

PTENURE = Audit Partner Tenure

SPEC = Auditor Industry Specialisation

KMP = Firm Complexity

ROA = ROA

SIZE = SIZE

ε = Error

Result and Discussion

| Independent Variable | Regression Model | | | |
|----------------------|--------------------|---------|-------|--|
| | Coefficient | T-value | Sig | Conclusion |
| (constant) | 8.693 | 10.754 | 0.000 | |
| P-TENURE | -0.007 | -0.116 | 0.907 | H ₀ accepted atau H ₁ rejected |
| SPECDUM | 0.313 | 3.704 | 0.047 | H ₀ rejected atau H ₁ accepted |
| KMP | 0.011 | 4.197 | 0.000 | H ₀ rejected atau H ₁ accepted |
| ROA | 1.671 | 4.496 | 0.000 | |
| SIZE | 0.396 | 13.863 | 0.000 | |
| R square | 0.452 | | | |
| F statistic | 85.382 | | | |
| F Sig | 0.000 ^b | | | |

Multiple Linear Regression

Regression coefficients of the study showed positive results. These results indicate a direct change between the independent variable and the dependent variable. Based on the regression results, it can be concluded that the auditor industry specialisation has a positive effect on audit fees. Significance value of 0,000 that is smaller than 0.01 so it can be concluded that the auditor industry specialisation has a positive effect on audit fees. Based on the regression results it is concluded that the complexity of the company has a positive effect on audit fees. Significance value of 0,000 is smaller than 0.01 so it can be concluded that the complexity of the company has a positive effect on audit fees. Significance value of 0,000 which is smaller than 0.01, it is concluded that Return on Assets (ROA) has a positive effect on audit fees. Significance value of 0,000 is smaller than 0.01, so it can be concluded that company size (SIZE) has an effect on audit fees.

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate | Durbin-Watson |
|-------|-------------------|----------|-------------------|----------------------------|---------------|
| 1 | .676 ^a | .458 | .452 | .8902838 | 1.856 |

The coefficient of determination (R²) shows how the independent variable explains the dependent variable. In table 4.7, the R² value of 0.452 shows that Audit Partner Tenure, Auditor Industry Specialisation, Company Complexity, Return On Assets (ROA) and Company Size (SIZE) is able to explain variations in earnings quality by 0.452 or 45.2%, while the remaining 0.548 or 54.8% are explained by other variables outside of the independent variables including foreign ownership structure, auditor changes, and voluntary disclosure.

Based on the Durbin-Watson test presented in Table 4.6, the regression for equation 1 shows the value of 1.856 which means the Durbin-Watson value is still in the autocorrelation free range because it is between -2 to +2.

Discussion

The Effect of Audit Partner Tenure on Audit Fee

The result of this research shows that Audit Partner Tenure does not affect Audit Fee. Audit Partner Tenure is the length of the auditor engagement. Audit Partner Tenure does not specify that the auditor better understands the company's condition so that it cannot cause the audit fee to be expensive when the tenure is longer and become cheaper when the tenure is shorter. Another reason is because public accountants are limited by a maximum 3-year engagement period in accordance with regulations issued by the Financial Services Authority (2017).

The Effect of Auditor Industry Specialisation on Audit Fee

Auditor Industry Specialisation has a positive effect on audit fees. Specialisation can be called expertise: the more specialised, the more expensive the audit fee will be because greater expertise will produce more accurate, timely and quality audit results. Previous research by Cahan (2011) found results where specialist auditors would charge a higher audit fee. Specialist auditors only audit a number of companies in one sector to make their specialisation a product differentiation, thereby offering a higher audit fee.

The Effect of Firm Complexity on Audit Fee

Based on the results of this study it can be seen that firm complexity has a positive effect on audit fees. High levels of complexity will require a longer time to audit and the higher the risk, the more expensive audit fees. This is consistent with previous research by Immanuel and Yuyetta (2014) which states that company complexity positively influences audit fees. According to Immanuel and Yuyetta (2014), the more subsidiaries owned, the greater the audit fee paid to the auditor. This is because the auditor needs more time to complete the audit process so that it will affect the amount of audit fees paid by the company.

Conclusion

This study shows that Auditor Industry Specialisation and the complexity of the company affect audit fee. Industry specialisation auditor means that the auditor has expertise in auditing certain industries so that it will have an impact on service costs. The complexity of the company also



affects the increase in audit fees because the more subsidiaries they have, the greater the audit fee paid to the auditor.

Unlike with Industry Specialisation Auditor and firm complexity, Audit Partner Tenure has no effect on audit fees. The audit tenure does not specify that the auditor better understands the firm's condition so that it cannot influence the audit fee to be expensive or become cheaper. For further research, another researcher could consider other variables such as audit changes, foreign ownership structure, and voluntary disclosure.

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