

ISBN: 978-602-60078-9-6

 ICAME 2017

# PROCEEDINGS

*THE 2nd*  
**INTERNATIONAL CONFERENCE**  
ON ACCOUNTING, MANAGEMENT AND ECONOMICS

**ICAME2017**

09-10, October 2017  
Makassar, Indonesia.



Faculty of Economics and Business  
Hasanuddin University

# Proceedings

The 2<sup>nd</sup> ICAME 2017

Makassar, 9 – 10 October 2017

ISBN : 978-602-60078-9-6

*Published by:*

Department of Management  
Faculty of Economics and Business  
Hasanuddin University

*Address:*

Gedung Fakultas Ekonomi dan Bisnis  
Kampus Unhas Tamalanrea  
Jl. P. Kemerdekaan KM. 10 Tamalanrea, Makassar 90245

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## ANALYSIS OF AUDITOR SWITCHING ON ASSOCIATION OF SOUTHEAST ASIAN NATIONS (ASEAN)

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**Abstract:** Objective of this research is to examine factors that affect auditor switching in ASEAN region. Auditee-related factors are audit opinion, management change, financial distress, company's size, ownership, audit committee, and independent commissioner. Auditor-related factor is auditor reputation. Country-related factor is financial deepening. Research samples are manufacturing companies in Indonesia, Malaysia, Singapore, Thailand and Philippines. Based on analysis of country fixed-effect regression; audit opinion, company's size, audit firm reputation, and financial deepening affect auditor switching. The results indicate the existence of opinion shopping in ASEAN. In the higher industry complexity, company is more likely to switch auditor. In terms of effect of auditor reputation, it indicates that company will switch auditor if auditor quality is low. Utilizing the financial deepening, it can be concluded that high public monitoring will affect company to switches auditor. This research shed a light to accountant profession, regulators and scholars about auditor switching practices by companies, and finally to draw up regulation and ethical framework. This research capture auditor switching between ASEAN countries as one region. The use of macro-economic factor could explain the phenomenon of auditor switching as well, especially in open market, such as ASEAN economic community.

**Field of Research:** Accounting

### 1. Introduction

Core objective of financial statement auditing is to assure weather financial statement reported by following accounting standards (Ikatan-Akuntan-Publik-Indonesia 2015; International-Auditing-and-Assurance-Standards-Board 2009). External auditor provides value added in financial reporting process by improving the reliability and credibility, and improve the quality of financial information. The role of auditor is prevention, detection and reporting (Hudaib & Cooke 2005). In order to maintain optimal service, external auditor should be independent, so he/she can provide objective opinion (Nasser et al. 2006).

Auditor faces many pressures in the audit process that can affect to auditor switching. It can be internal pressure in the form of self-interest threat (Hudaib & Cooke 2005). This pressure, potentially, reduces the independence of auditor because client can switch to another audit firm. Other pressures come from management. Management expects the best opinion in any actual conditions faced by the company. To oversee and ensure thus opinion, management may provide intimidation. The concrete act of intimidation is threat of auditor switching (Chow & Rice 1982).

Enron case is a picture why auditor switching is important. Accounting scandal of Enron happened because of ethics problem between management and auditor. Arthur Andersen act with no independence to let earnings manipulation and affect on auditor switching as well (Dunne et al. 2008). It is proved by increasing of audit risk on ex-client of Arthur Andersen, not only client in US but client around the world as well (Srinidhi et al. 2012; Kealey et al. 2007; Cahan & Zhang 2006). This case leads to formulation of business ethics standard; transparency of financial statement (Willits & Nicholls 2014) and audit rotation (Nagy 2005); which is Sarbanes Oxley Act (SOX). Some countries use audit rotation of SOX as well as regulation of mandatory switching; such as Indonesia, Singapore, Thailand, Laos have regulated 5 years of audit rotation; Cambodia have regulated 3 years of audit rotation (ASEAN-Federation-of-Accountant 2014). Audit rotation leads to auditor switching.

The focus of auditor switching is auditor independence. Auditor switching increases auditor independence (Junaidi et al. 2016; Elder et al. 2015). Increasing of auditor independence is important to provide high audit quality (Tepalagul & Lin 2015). It is proved by increasing of audit tenure (low auditor

switching) more likely to act not independently, because of strong personal relation between auditor and management, so objectivity of auditor will be lost (Junaidi et al. 2012).

Generally, there are two kinds of audit firm switching which are mandatory switching and voluntary switching (Hoyle 1978). Mandatory switching is audit firm switching in a specified period based on government regulation, while voluntary switching based on initiative of client (Lin et al. 2009). Audit tenure regulated to prevents deep relationship, loyalty and emotional with client, so that can threatens independence, competences in evaluating audit evidence (Nasser et al. 2006). Tenure regulation depends on condition of each country such as macroeconomics factor (financial deepening).

There are some factors that affect auditor switching; which are auditee-related factors, auditor-related factor, and country-related factors. Auditee-related factors lead to ownership, management change, audit opinion of financial statement, financial distress, company's size, audit committee, and independent commissioner. Auditor-related factor leads to audit firm reputation. Country-related factor is financial deepening as public monitoring by stock market.

Association of Southeast Asian Nations (ASEAN) economic community increasingly leads to the establishment at the end of 2015 (ASEAN-Federation-of-Accountant 2014). The ASEAN economic community will be a powerful, competitive regional economic force with an aggregated Gross Domestic Product (GDP) of 2.5 trillion USD, as year of 2014, representing the third largest economic cooperation following the North American Free Trade Agreement (NAFTA) and the European Union (EU) (Lee & Jeong 2016). ASEAN countries are working on improving integration through harmonization of regulations, reduction of trade barriers and the promotion of labor mobility between countries (ASEAN-Federation-of-Accountant 2014), including requirement of accounting and auditing.

Accounting and auditing profession is an essential component in the development of private sector, boost domestic investor confidence and the ability to attract foreign direct investment up. It is important to increase public sector in achieving sustainable management of public finance and promoting of governance, accountability and transparency (ASEAN-Federation-of-Accountant 2014). These explanations show that role of the auditor is very important for development of



ASEAN countries, including audit tenure, audit quality as well as auditor switching.

Generally, Indonesia and ASEAN region have a different cultural environment that influences different behaviors including in the context of business. Market discipline as the main economic models does not necessarily produce the same output with implementation in the western region. Behavior that is likely to be communal and close relation between persons affects business activities as well. Data between countries used in this study provide an opportunity to analyze the relationship of a country's financial characteristics related to auditor switching.

Aim of this study is to examine effect of ownership, audit opinion, management change, financial distress, company's size, audit committee, independent commissioner, audit firm reputation, and country's financial deepening on auditor switching. This study will capture the phenomenon of auditor switching from aspects of corporate governance implementation as well. The relationship between corporate governance and external audit is a central issue in agency relationship, especially in ASEAN region as the backbone of economic growth in the world.

This research will examine factors that affect auditor switching in five countries of ASEAN (Indonesia, Malaysia, Philippines, Singapore, and Thailand) as one region rather than by each country. Consideration of analysis of auditor switching in five countries of ASEAN as one region is establishment of open market in ASEAN leads to agency relationship as well as needs of auditor services across countries. This condition captures integration of stock exchange as well, includes of development of stock exchange parties *networking*, of five ASEAN countries (Indonesia, Malaysia, Singapore, Thailand, Philippines) (United States Agency for International Development 2013). It is important to analyze phenomenon of auditor switching across countries in ASEAN as one integrated business activities because of needs of high quality financial statement information across countries.

## 2. Literature Review

### 2.1. Agency Theory

Agency theory is defined as a contract between one or more parties (principal) that bind the other party (the agent) to carry out management of company based on interests of principal, including the delegation of decision-making authority to the agent (Jensen & Meckling 1976). Principal will provide incentives for agent and pay monitoring cost (Jensen & Meckling 1976).

Accounting has an important role in minimizing the agency cost as a result of a conflict of interest between principal and agent. The financial statements, as a result of the accounting process, which has been audited useful for reducing agency cost (Francis & Wilson 1988). This argument provides an explanation of financial auditing can reduce agency cost as well. Auditing is one of assurance service that aims to improve the quality of information produced by the management. The value given by the audit is expected to moderate the potential conflicts of interest.

### 2.2. Auditor Switching

Auditor switching is an audit firm switching by company. It can be caused by some factors which are both of client and auditor factors. First, client-related factors, which are financial distress, management failure, changes in ownership and initial public offering (IPO). Auditor switching can be carried out due to take over as well (Anderson et al. 1993). Based on Enron case, ex-clients of Arthur Anderson had to perform switching. They have higher skepticism in the process (Nagy

2005). Second, auditor-related factors, which are audit fees and audit quality. In the non-profit corporation context, consideration to switching auditor is affected by the operating structure, reputation management, and audit fees (Tate 2007).

Mandatory and voluntary auditor switching can be distinguished based on which party become concern from the issue. If auditor switching is done voluntarily, main concern is on client side. If the auditor switching is done mandatorily, main concern is on auditor side (Hudaib & Cooke 2005). When client switch its auditors, and there are no switching rules, there will be auditor resignation or dismissal by the client. Indonesia, Singapore, Thailand, Laos have regulation of auditor switching in every 5 years; Cambodia in every 3 years; Philippine, Malaysia, Vietnam have no particular auditor switching regulation (ASEAN-Federation-of-Accountant 2014). Auditor switching in this research refers to change of auditor after the end of audit. If current year auditor is same with next year auditor, then company does not switch auditor. If current year auditor is different with next year auditor, then company switches auditor.

### 2.3. Hypotheses

Generally, businesses started from family businesses and still being a basic of business development. The consequence is owners have big interventions to company's activities. Agency theory stated that the bigger interventions of the owners (or shareholders in public companies), the bigger performance of company (Jensen & Meckling 1976). However, even legally there is separation between owners and management, but practically both parties can affect each other. Intervention of owners can happen in auditor selection as well (Lodge 2008). Observation of capital market practitioners shows that shareholders switching affect auditor switching (Lodge 2008).

Institutional shareholders spend more time to do research related to company and its industry, compared to individual shareholders spend less time to monitoring related to company (Man & Wong 2013). Institutional shareholders give more direct monitoring, as one of corporate governance mechanisms, in disciplining of manager (Talley 2009). Supervision of institutional shareholders can reduce agency problems, including decision of auditor switching. Institutional shareholders determine increasing demand of audit quality (Chan et al. 2007).

Managerial ownership is one of mechanisms to reduce agency problem. Managerial ownership makes interest of manager (agent) and shareholders (principal) can be aligned. Manager will do direct monitoring on internal performance of company. Interest alignment stimulates manager to make decision aligned with shareholders' interest, including auditor switching decision making.

Foreign ownership is one of corporate governance mechanisms as well that can reduce agency problem. Foreign shareholders from countries with good corporate governance implementation will implement good corporate governance implementation as well in countries with developed corporate governance (Klapper et al. 2006). Foreign shareholders will implement better oversight than local shareholders as well, because foreign shareholders will face risk of reputation and legal if it does not implement good corporate governance (Klapper et al. 2006). One of good corporate governance implementation is selection of auditor.

- H1a: Institutional ownership affect auditor switching
- H1b: Managerial ownership affect auditor switching
- H1c: Foreign ownership affect auditor switching

Management change affects auditor switching, to absorb new ideas in order to improve the company's expansion policy under new management (Hudaib & Cooke 2005).



Management change of company may change policy in accounting, finance, and auditor selection. Company will seek auditor that aligned with accounting policy and reporting. If this expectation is not met, company will replace its auditor. Company that change CEO and having distress may receive qualified opinion, and affect to switch auditor. Intimidation and close relationship giving high probability of auditor switching as well, caused by worse qualified opinion (Hudaib & Cooke 2005).

#### H2: Management change affect auditor switching

Auditor switching is driven by the opinion given by the auditor (Chow & Rice 1982). Company expects to get unmodified or unqualified opinion. Dissatisfaction with another opinion received, beside unmodified or unqualified opinion, will stimulate company to switch auditor. Qualified opinion explains that companies have weak corporate governance. This explanation is in line with research related to qualified opinion with implementation of corporate governance (Lin & Liu 2009). Companies which have weak corporate governance and get qualified opinion tends to switch auditor (Lin & Liu 2009).

#### H3: Audit opinion affect auditor switching

Company tends to switch auditor in financial distress condition (Hudaib & Cooke 2005). It shows company that received going concern opinion and still survive tends to get another auditor firm compared to company that did not received going concern opinion. Auditor with distress client will have shorter tenure than non-distress client. Financial distress gives tension to relationship between auditor and management as well. This tension caused by differences related to methods of accounting, dissatisfaction with the audit opinion, or dissatisfaction with performance of auditor (Schwartz & Menon 1985). Hudaib & Cooke (2005) found company that change CEO and having distress may received qualified opinion, and affect to switch auditor.

#### H4: Financial distress affect auditor switching

Big company shows more complex business and it usually is company group consists of some linear or not linear companies (Anderson et al. 1993; Firth 1999). Big company have big gap between management and owner, because of large number of agents in company group (Willenborg 1999). In order to aligns auditing processes every company, company group will switches auditor to reduce audit complexity and fees (Anderson et al. 1993; Firth 1999), and big gap between owner and many agents (Willenborg 1999). The bigger company is, the higher auditor switching.

#### H5: Size affect auditor switching

Audit committee have important role in minimizing the agency cost as well. Audit committee is one of committees made by board of commissioners. Audit committee have responsibility to ensure high quality of financial reporting, by fraud prevention, financial reporting monitoring, regulation compliance review, risk measurement and monitoring, code of conduct compliance review, and interaction with external auditor (Deloitte 2015). To fulfill this responsibility, audit committee will assesses and recommends external auditor. Audit committee assesses and recommends external auditor based on auditor independence, audit fee, and results of communication with auditor (Deloitte 2015).

The more effective audit committee, they will recommend auditor switching to board of commissioner to increase financial reporting quality. Audit committee with high competency of financial and accounting tends to switch auditor (Andersen Audit Firm) with another high quality auditor (Chen & Zhou 2007). They will recommend auditor

switching to board of commissioner to increase financial reporting quality. It is consistent with responsibility of audit committee to assess and prevent auditor independence by auditor switching.

#### H6: Audit committee affect auditor switching

Board of commissioners can be used as a measure of the implementation of corporate governance (Talley 2009). As shareholders' representatives, board of commissioners have significant role in monitoring internal management, including of financial reporting. Effectiveness of commissioners depends on independent commissioner composition. Independent commissioners are personnel of board of commissioners who does not have significant relationship with company (including subsidiary, affiliate, and associate company), shareholders; they are not audit firm staff that do auditing process in the company as well (Man & Wong 2013). Independent commissioner will give recommendation to annual general meeting of shareholders related to selection of auditor based on public interest. In order to prevent auditor independence, independent commissioner recommends auditor switching (Lee et al. 2004).

#### H7: Independent commissioner affect auditor switching

Auditor reputation can affect auditor switching. If small audit firm, with small clients, loss one of significant client, then large audit firm considered more able to maintain the independence of the auditor rather than small audit firm. Larger audit firm is usually considered to be able to maintain independence better than smaller audit firm because they usually provide a range of services to clients in large numbers, thereby reducing their dependence on specific clients. In addition, larger audit firm is generally considered as a provider of higher audit quality and enjoy a high reputation in the business environment, so it will attempt to its image (Nasser et al. 2006). The company will seek high credibility audit firm to enhance the credibility of financial statements. Investors tend to believe accounting data generated from a reputable auditor. Company will not switch audit firm if it already have high reputation and quality.

#### H8: Auditor reputation affect auditor switching

The penetration of financial instruments indicates the level of public awareness of any existing financial instruments. Mechanism for financial instruments is strongly influenced by the available information, including financial information. The deeper penetration of financial instruments, the more sensitive position of public companies information will be.

De Gregorio (1999) shows that financial deepening would increase economic growth. Economic growth can run faster for more effective if allocation of funds goes to potential sector. Company will respond to this phenomenon by making optimal policy so that the performance of the company will obtain an optimal response from the market. One of policy must be made by the company is to determined audit firm.

This explanation is in line with policy of privatization that monitoring of market will be able to improve companies' performance (Megginson et al. 1994). Companies can improve efficiency because of market pressures supervisions by public/investors/creditors. Public supervisions will stimulate company to make best policies for stakeholders. External parties tend to affect policy formulation of the company (Megginson et al. 1994).

Economic growth of countries is affected by financial sector. Financial deepening as the picture supervisions of the public will encourage companies to make the best policy for the



various parties related to companies business, including auditor switching policy. Existence of well public supervisions will make high audit quality demand, so company will switch auditor with more qualified auditor.

H9: Financial deepening affect auditor switching

### 3. Methodology

#### 3.1. Source of Data

This research is a quantitative research based on secondary data collected from various available sources and databases (OSIRIS, Thomson Reuters, Beuro Van Dijk) in year 2012-2014. Consideration of research period between 2012-2014 is integration of stock exchange, includes of development of stock exchange parties *networking*, of five ASEAN countries (Indonesia, Malaysia, Singapore, Thailand, Philippines) have just been established in 2012 (United States Agency for International Development 2013).

#### 3.2. Research Sample

Research sample is manufacture companies listed in stock exchange in ASEAN region. There are five ASEAN countries used in this research.

Table 1. Sample

Companies in Each Country			Total
Indonesia	Manufacture Companies listed 2012-2014	93	83
	Incomplete Data	(10)	
Malaysia	Manufacture Companies listed 2012-2014	211	211
Philippine	Manufacture Companies listed 2012-2014	20	20
Singapore	Manufacture Companies listed 2012-2014	120	120
Thailand	Manufacture Companies listed 2012-2014	71	68
	Using Local Language	(5)	
Number of Companies			500
Number of Observations			1.000

#### 3.3 Variables and Operational Definitions

Dependent variable is auditor switching. Auditor switching, as dummy variable (1 if switch auditor, 0 otherwise), is voluntary audit firm switch (Chow & Rice 1982). Voluntary switching can be seen by audit firm switching before the time of audit rotation is end. Auditor switching, as ratio variable (1/4 if auditor switching direction from big four to non big four, 2/4 if big four to non big four, 3/4 if big four to big four, 4/4 if non big four to big four), is downward or upward direction audit firm switching seen by size of audit firm. Auditor switching is seen by switching in one year ahead after the end of audit of current year financial statement. If current year auditor is same with next year auditor, then company does not switch auditor. If current year auditor is different with next year auditor, then company switches auditor.

Independent variables are share ownership, management change, audit opinion, financial distress, company's size, audit committee, independent commissioner and financial deepening. Ownership is shareholders with significant intervention with minimum 5 percent share ownership (Hudaib & Cooke 2005; Lodge 2008), measured by percentage of institutional, managerial, foreign ownership. Institutional ownership calculated by number of share owned by institution divided by number of outstanding share with cut-off point 5 percent or more, while below 5 percent ownership includes in zero ownership. Managerial ownership calculated by number of share owned by management divided by number of outstanding share with cut-off point 5 percent or more, while below 5 percent ownership includes in zero ownership. Foreign ownership calculated by number of share owned by foreigner divided by number of outstanding share with cut-off point 5 percent or more, while below 5 percent ownership includes in zero ownership. Management change is CEO change caused by general meeting of shareholders or own-decision (Hudaib & Cooke 2005; Schwartz & Menon

1985), measured as dummy variable (1 if change CEO, 0 otherwise). Audit opinion is opinion provides by auditor in audit report, measured as dummy variable (1 if unqualified opinion, 0 if qualified opinion). Financial distress is a condition where companies face finance difficulties (Hudaib & Cooke 2005), measured by Altman Z-Score ( $Z = 1.2 [\text{Working Capital to Total Assets}] + 1.4 [\text{Retained Earnings to Total Assets}] + 3.3 [\text{Earnings Before Interest and Tax to Total Assets}] + 0.6 [\text{Market Value of Equity to Book Value of Liabilities}] + 0.999 [\text{Sales to Total Assets}]$ ). Size of company is measured by logarithm of total assets. Effectiveness of audit committee is calculated by number of audit committee member whose held competency in accounting, finance, and auditing divided by total number of all audit committee member (Lee et al. 2004). Independent commissioner is measured by proportion of number of independent member of board of commissioner divided by total member of board of commissioner (Lee et al. 2004). Audit firm reputation is size of audit firm, measured as dummy variable (1 if affiliate with big four, 0 otherwise). Country's financial deepening is public access to financial instrument or literacy (Di Giovanni 2005), measured by percentage of market capitalization to gross domestic products.

Control variables are number of meeting of commissioner, profitability and leverage. Regarding to auditor recommendation, board of commissioner is the party that will give auditor recommendation based on audit committee evaluation to shareholders in annual general meeting of shareholders. Effectiveness of board of commissioner will be seen by number of board meeting. Number of board of commissioner meeting is measured by number of meeting that have been done in a year (Lee et al. 2004). The more effective board of commissioner, the more likely company will switches auditor (Lee et al. 2004). Profitability and leverage are related to financial distress that shows financial health of company (Landsman et al. 2009). Profitability is measured by return on assets (ROA), which is net income divided by total assets. The higher ROA, the less likely company will switches auditor (Landsman et al. 2009). Leverage is measured by debt to assets ratio (DAR), which is total debt divided by total assets. The higher DAR, the more likely company will switches auditor (Landsman et al. 2009).

#### 3.4 Regression Model

$$ASW_{i,t+1} = \beta_0 + \beta_1 IOT + \beta_2 MOI + \beta_3 FOI + \beta_4 MCI + \beta_5 AOI + \beta_6 FDI + \beta_7 SIZEI + \beta_8 ACI + \beta_9 ICI + \beta_{10} BIGI + \beta_{11} FDPt + \beta_{12} MEETt + \beta_{13} ROAt + \beta_{14} DART + \sum \text{Country-effect} + e$$

Where:

ASW <sub>t+1</sub>	: Auditor Switching (ratio) period t+1
IOT	: Institutional Ownership period t
MOI	: Managerial Ownership period t
FOI	: Foreign Ownership period t
MCI	: Management Change period t
AOI	: Audit Opinion period t
FDI	: Financial Distress period t
SIZEI	: Size of Company period t
ACI	: Audit Committee period t
ICI	: Independent Commissioner period t
BIGI	: Size of Audit Firm period t
FDPt	: Country-Financial Deepening period t
MEETt	: Number of Board of Commissioner meeting period t
ROAt	: Return on Assets period t
DART	: Debt to Assets Ratio period t

Hypotheses test will be run by country fixed-effect panel regression test.



## 4. Findings and Discussions

### 4.1 Results

Table 2. Descriptive Statistics

	N	Minimum	Maximum	Mean	Standard Deviation
ASW (ratio)	1,000	0.00	1.00	0.0530	0.17951
IO	1,000	0.00	0.99	0.4580	0.28982
MO	1,000	0.00	0.85	0.1267	0.17730
FO	1,000	0.00	0.99	0.1604	0.24199
FD	1,000	-38.03	319.06	4.6630	13.31809
SIZE	1,000	6.61	16.46	9.2707	1.66603
AC	1,000	0.00	1.00	0.5345	0.24453
IC	1,000	0.00	0.98	0.4429	0.12611
FDP	1,000	0.38	2.46	1.3908	0.57394
MEET	1,000	0.00	42.00	5.2740	3.36426
ROA	1,000	-5.48	46.82	0.0878	1.51524
DAR	1,000	0.01	21.65	0.4256	0.73300
Switch Auditor	93				
Not Switch Auditor	907				

Source: Statistical Output

Table 2 shows that mean of auditor switching in ASEAN period 2012-2013 and 2013-2014 is 0.053. Number of observations that switches auditor is 93 observations. Number of observations that not switches auditor is 907 observations.

Table 3. Fixed-Effect Regression Test

	Coefficient	Significance	Notes	Sign
Constant	-0.114249			
IO	0.016592	0.9207	Have no effect	
MO	-0.022717	0.4598	Have no effect	
FO	-0.045888	0.1682	Have no effect	
MC	0.008981	0.7970	Have no effect	
AO	-0.050442	0.0102	Have significant effect (level 5 percent)	-
FD	-0.000408	0.4214	Have no effect	
SIZE	0.018910	0.0536	Have significant effect (level 10 percent)	*
AC	-0.005772	0.4758	Have no effect	
IC	-0.021717	0.5610	Have no effect	
BIG	-0.052717	0.0001	Have significant effect (level 1 percent)	-
FDP	0.057365	0.0000	Have significant effect (level 1 percent)	+
MEET	-0.001431	0.2642		
ROA	0.000731	0.9837		
DAR	0.027899	0.0004		
Adjusted R-squared = 0.0595				
Significance (F-statistic) = 0.000				

Source: Statistical Output

### 4.2 Robustness Test

Robustness test to testing weather result of country-fixed effect panel regression is consistent if tested by other analytical tools. Robustness test will be applied by country-fixed effect logistic regression, with auditor switching (dummy) variable as dependent variable. Another alternative test is common effect regression test without country effect factors consideration. Comparison between common effect, logistic, and country fixed effect regression is as followed:

Table 4. Robustness Test

Variable	Coefficient			Notes
	Country Fixed-Effect Multiple Regression	Country Fixed-Effect Logistic Regression	Common-Effect Multiple Regression	
Constant	-0.106109	-4.256145	-0.114249	Consistent
IO	0.002898	0.413671	0.016592	Consistent
MO	-0.030903	-1.302751	-0.022717	Consistent
FO	-0.036725	-0.504098	-0.045888***	
MC	0.004805	0.203629	0.008981	Consistent
AO	-0.053726**	-1.130800*	-0.050442**	Consistent
FD	-0.000370	-0.052897***	-0.000408	
SIZE	0.017230***	0.172709	0.018910*	Consistent
AC	-0.017123	0.238668	-0.005772	Consistent
IC	-0.028690	-0.831793	-0.021717	Consistent
BIG	-0.046678*	-0.658319*	-0.052717*	Consistent
FDP	0.085830*	1.912841*	0.057365*	Consistent
MEET	-0.001938	-0.012962	-0.001431	Consistent
ROA	7.92E-05	0.123977	0.000731	Consistent
DAR	0.028003*	0.087530	0.027899*	
Adjusted-R <sup>2</sup>	0.0595		0.0457	
McFadden-R <sup>2</sup>		0.1172		
Sig. of F-Statistic	0.000*	0.000*	0.000*	

\*Significant in 1 percent

\*\*Significant in 5 percent

\*\*\*Significant in 10 percent

Source: Statistical Output

Source: Statistical Output

Based on comparison between country fixed-effect multiple regression and logistic regression tests, all results are consistent; except for variables financial distress and leverage are not consistent. It indicates that financial distress and leverage are more sensitive if auditor switching seen by direction of auditor switching or without considering of switching direction.

Based on comparison between common effect and country fixed effect regression test, all results are consistent; except for variable foreign ownership. It indicates that effect of foreign ownership on auditor switching is more sensitive to country factors. Each country have different policy of investment from outside the country. Even open market and integration have been established between countries in ASEAN, there are still unilateral liberalization initiatives in some countries (Yean & Das 2015), such as Thailand allows free movement of capital in and out of the country, while Indonesia have are required to apply for permission from the Central Bank of Indonesia for the repatriation and inflows of funds (Niblock et al. 2014).

### 4.3 Ownership and Auditor Switching

Institutional ownership have significance value 0.9207 (insignificant). Managerial ownership have significance value 0.4598 (insignificant). Foreign ownership have significance value 0.1682 (insignificant). Institutional, managerial, and foreign ownership have no effect on auditor switching. This results is not in line with Lodge (2008) that stated ownership structure will affects auditor switching, as well as with Chan et al. (2007) and Klapper et al. (2006) that stated institutional and foreign ownership have high demand of audit quality. In ownership structure, there is problem called entrenchment effect. Entrenchment is the act of controlling shareholder protected by their control right to perform abuse of power (Fan & Wong 2002). The higher ownership (institutional / managerial / foreign ownership) does not always followed by good performance, including financial reporting performance because of abuse of control right to meet self-interests instead of public interests.

Abuse of control right includes in auditor switching as well. High control right may ignore demand of high audit quality, so it does not affect auditor switching. Credibility of accounting information will be decreased when controlling shareholders are protected by their control right (Fan & Wong 2002). Decision making of auditor switching based on self-interest, not based on needs of high financial reporting and auditing quality.



#### 4.4 Management Change and Auditor Switching

Management change have significance value 0.7970 (insignificant). Management change have no effect on auditor switching. This result is not in line with Chow and Rice (1982) that stated management change will affects auditor switching. This result indicates that change on management is not always followed by company policy in using auditor services (Damayanti & Sudarma 2008). Although change on management followed by change on management policy, only a few cases followed by change on financial management policy (Burton & Roberts 1967). It shows that accounting policy and reporting by predecessor audit firm can be adjusted to new management policy by renegotiation between both of these parties (Damayanti & Sudarma 2008).

Management change is done because of restatement and violation of financial statement as well (Niehaus & Roth 1999). Problem of financial statement caused by poor management performance in maintains relationship between company and auditor (Menon & Williams 2008). If management change followed by auditor switching, then there will be high uncertainty in financial reporting, thus increasing the cost of capital (Menon & Williams 2008). Management is the party who will take the responsibility on financial statement problem. Concern of solving problem is management change instead of auditor switching. This explanation shows that change on management is not always followed by auditor switching.

#### 4.5 Audit Opinion and Auditor Switching

Audit opinion have significance value 0.0102 (significant in 5 percent) with negative coefficient sign. This result is in line with the opinion shopping concept. Auditor switching is driven by the opinion given by the auditor (Chow & Rice 1982). Company expects to get unmodified or unqualified opinion. Dissatisfaction with another opinion received, beside unmodified or unqualified opinion, will stimulate company to switch auditor. Qualified opinion explains that companies have weak corporate governance. This explanation is in line with research related to qualified opinion and implementation of corporate governance (Lin & Liu 2009). Companies which have weak corporate governance and get qualified opinion tends to switch auditor (Lin & Liu 2009).

#### 4.6 Financial Distress and Auditor Switching

Financial distress have significance value 0.4214 (insignificant). This result is not in line with Hudaib and Cooke (2005) that stated distressed company tends to switch auditor. Correlation between financial distress and auditor switching related to audit quality and audit fee. These factors make financial distress do not affect auditor switching. Knechel and Vanstraelen (2007) compare companies between financial distress and save condition and show that auditor independence does not decrease but does not increase as well in bankruptcy prediction. Decreasing of audit quality came from auditor's decision that did not provide going concern opinion to distress company or provide going concern opinion to company that still able to operate well.

Although there is problem of audit quality related to bankruptcy prediction, company refuse to switch to higher quality auditor because of increasing of audit fee. For example, a distress company audited by low quality auditor (e.g. non big four) will refuse to switch to high quality auditor (e.g. big four). Big four auditor fee will increase in future (Elliott et al. 2013). Decreasing of audit fee only in the first year after auditor switching (Ghosh & Lustgarten 2006). Auditor tends to give audit fee discount for profitable companies, while lost companies do not get fee discount (Walker & Canstrella

2000). Increasing of audit quality that followed by increasing of audit fee make a distress company does not always switch auditor.

#### 4.7 Size and Auditor Switching

Size have significance value 0.0536 (significant in 10 percent) with positive sign. Size have positive effect on auditor switching. This result is in line with results of Anderson et al. (1993) and Willenborg (1999). Size of companies shows how large companies (Hogan & Roger 2009; Hudaib & Cooke 2005), industry domination and business complexity (Anderson et al. 1993; Firth 1999). Large companies shows more complex business and could be companies group consist of few subsidiary with linear and nonlinear business (Anderson et al. 1993; Firth 1999). Large companies have large gap between management and owner as well, because there are many agents in companies group (Willenborg 1999). Larger company tends to switch auditor in order to decreases audit fee and complexity with same auditor within companies in one group (Anderson et al. 1993; Firth 1999). Willenborg (1999) also stated that large company should switch to big 4 auditor because of business complexity and larger gap between management and owner. High quality auditor more capable to do audit processing in big number of business as well as decreasing of large information asymmetric because of large gap.

#### 4.8 Audit Committee and Auditor Switching

Audit committee have significance value 0.4758 (insignificant). Audit committee have no effect on auditor switching. There are two reasons why audit committee do not affect auditor switching. First one, the more effective audit committee, they will recommend auditor switching to board of commissioner to increase financial reporting quality. Second one, the more effective audit committee, they will recommend board of commissioner to keep company's auditor. These differences make effectiveness of audit committee do not affect auditor switching significantly.

Chen & Zhou (2007) found that audit committee with high competences of financial and accounting tends to switch auditor (Andersen Audit Firm) with another high quality auditor. It shows that the higher competences of financial and accounting of audit committee, the more demand of high quality auditor. They will recommend auditor switching to board of commissioner to increase financial reporting quality.

On the other side, audit committee with high financial and accounting competences tends to keep company's auditor. The more effective audit committee, the less hidden audit risk (Lee et al. 2004). Audit committee concerns about legal responsibility and reputation, so that instead of switches to new auditor, they prefer to support current auditor to accomplishing their assurance duties (Lee et al. 2004).

In addition, audit committee have no effect on auditor switching because audit committee have no direct effect on decision making of auditor switching. Main role of audit committee is making assessment and recommend external auditor. Audit committee assess and recommend external auditor based on auditor independence, audit fee, and results of communication with auditor (Deloitte 2015). Audit committee recommendation can be used or can be not used in decision making by management or general meeting of shareholders.

#### 4.9 Independent Commissioner and Auditor Switching

Independent commissioner have significance value 0.5610 (insignificant). Independent commissioner have no effect on auditor switching. Similar to audit committee explanation,



there are two reasons why independent commissioner do not affect auditor switching. First one, the bigger composition of independent commissioner, independent commissioner will recommend auditor switching to general meeting of shareholders to increase financial reporting quality. Second one, the bigger composition of independent commissioner, independent commissioner will recommend to general meeting of shareholders to keep company's auditor. These differences make effectiveness of independent commissioner do not affect auditor switching significantly.

Chen & Zhou (2007) found that the bigger composition of independent with tends to switch auditor (Andersen Audit Firm) with another high quality auditor. It shows that the more effective independent commissioner, the more demand of high quality auditor. They will recommend auditor switching to general meeting of shareholders to increase financial reporting quality.

On the other side, big composition of independent tends to keep company's auditor. The more effective independent commissioner, the less hidden audit risk (Lee et al. 2004). Independent commissioner concerns about legal responsibility and reputation, so that instead of switches to new auditor, they prefer to support current auditor to accomplishing their assurance duties (Lee et al. 2004).

In addition, independent commissioner have no effect on auditor switching because they have no direct effect in decision making of auditor switching. Board of commissioner, includes of independent commissioner, give external auditor recommendation to general meeting of shareholders, based on audit committee assessment and recommendation of audit committee. Independent commissioner recommendation can be used or can be not used in decision making by general meeting of shareholders.

#### 4.10 Auditor Reputation and Auditor Switching

Auditor reputation have significance value 0.0001 (significant in 1 percent) with negative coefficient sign. Auditor reputation have negative significant effect on auditor switching. It is consistent with Nasser et al. (2006) that stated company with high auditor reputation is less likely to switches auditor. Large audit firm (affiliated with big 4) is more independent compared with the small audit firm (affiliated with non-big 4). When large audit firm lost one of the clients, it is not so influential on its revenue. If small audit firm, with small clients, loss one of significant client, then large audit firm considered more able to maintain the independence of the auditor rather than small audit firm. Larger audit firm is usually considered to be able to maintain independence better than smaller audit firm because they usually provide a range of services to clients in large numbers, thereby reducing their dependence on specific clients. In addition, larger audit firm is generally considered as a provider of higher audit quality and enjoy a high reputation in the business environment, so it will attempt to its image (Nasser et al. 2006). The company will seek high credibility audit firm to enhance the credibility of financial statements. Investors tend to believe accounting data generated from a reputable auditor. Company will not switch audit firm if it already have high reputation and quality.

#### 4.11 Financial Deepening and Auditor Switching

Financial deepening have significance value 0.0000 (significant in 1 percent) with positive coefficient sign. Economic growth of countries is affected by financial sector. Financial sector mediates all parties that have interest in business process. In dynamics of the relationship of various stakeholders in the business, there is a phenomenon of information asymmetry. Asymmetry of information risen up with high transactional

and informational costs. The phenomenon of information asymmetry can be minimized if the financial markets operate efficiently (Kularatne 2002).

Financial deepening is a picture of the enhancement of the role and activities of financial services to the economy. The higher financial deepening showed that a growing number of financial facilities particularly access to capital market which is owned by the public, thus the greater individual access to finance and investment facilities. The greater public access to a wide range of financial instruments and investments can reduce the risk and vulnerability of one of the financial sub-sector by government regulation framework to ensure public interests. This explanation is in line with policy of privatization that monitoring of market will be able to improve companies performance (Megginson et al. 1994). Companies can improve efficiency because of market pressures supervisions by public / investors / creditors. Public supervisions will stimulate company to make best policies for stakeholders. External parties tend to affect policy formulation of the company (Megginson et al. 1994).

De Gregorio (1999) shows that financial deepening would increase economic growth. Economic growth can run faster for more effective if allocation of funds goes to potential sector. Company will respond to this phenomenon by making optimal policy so that the performance of the company will obtain an optimal response from the market. One of policy must be made by the company is to determined audit firm.

Economic growth of countries is affected by financial sector. Financial sector mediates all parties that have interest in business process. Financial deepening as the picture supervisions of the public will encourage companies to make the best policy for the various parties related to company's business, including policy of auditor switching. Existence of well public supervisions will make high demand audit quality, so company will switch auditor with more qualified auditor. This result illustrates that financial deepening affect on auditor switching positively.

#### 5. Conclusion

Aim of this research is to examine factors that affect auditor switching in five countries of ASEAN. Audit opinion affect auditor switching, indicates that dissatisfaction of qualified opinion makes company switches auditor. Audit firm reputation affects auditor switching, indicates that company will not switch audit firm if it already have high reputation. Size affect auditor switching, indicates more complex business leads to auditor switching. Financial deepening affect auditor switching, indicates that existence of well public supervisions will make high demand audit quality, so company will switch auditor with more qualified auditor. In the other hand, ownership, financial distress, management change, audit committee, and independent commissioner does not affect auditor switching.

This research will be information and extra literature to public accountant profession, regulators and scholars about auditor switching practices by companies, to draw up rules and ethical framework and clarify the literature on agency theory and professional ethics of auditors. The phenomenon of auditor switching can be captured more integrated and can be interpreted appropriately; so investors and creditors can make the best economic decision. The use of macro-economic factor could explain the phenomenon of auditor switching as well, especially in open market, such as ASEAN economic community.

This research finds that ownership have no effect on auditor switching because of entrenchment effect by controlling



shareholders. This research is not considering controlling shareholders to controls effect of ownership on auditor switching. Future research can use entrenchment effect by controlling shareholders to controls effect of ownership on auditor switching. This research finds that financial distress have no effect on auditor switching because of increasing of audit fee. This research is not considering audit fee to controls affect of financial distress on auditor switching because of limited data accesses. Future research can use audit fee as control variable to controls effect of financial distress on auditor switching.

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