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The Connection Between Corporate Governance and Audit Report Lag: An Indonesian Case

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ABSTRACT*:* *This study examines audit report lag in the context of Indonesia Stock Exchange where the regulator has been established the good corporate governance program. Audit report can affect the timeliness of accounting information releases. Delay to publish audit report will affect many aspects such as the value of information which may cause a bad sign of companies' conditions. The objective of this research is to examine the relation between corporate governance and audit report lag in Indonesian public listed companies. The corporate governance characteristics examined are audit committee size, audit committee independence, audit committee meetings, audit committee financial expertise, size of the board and independent commissioner. The research result of the relation between Coporate Governance and Audit Report Lag are varies. First, audit committee size is proved to have significant relationship towards audit report lag in a negative direction. Second, audit committee independence is proved to have insignificant relationship towards audit report lag in a negative direction. Third, audit committee meetings is proved to have insignificant relationship towards audit report lag in a negative direction. Fourth, audit committee expertise is proved to have insignificant relationship towards audit report lag in a negative direction. . Fifth, board siz is proved to have significant relationship towards audit report lag in a negative direction. . Lastly, independent commissioner is proved to have insignificant relationship towards audit report lag in a negative direction*

Keywords: *Corporate Governance, Audit Report Lag, Indonesia Stock Exchange.*

I. INTRODUCTION

Audit report lag is defined as the number of days between the dates of fiscal year and the date of auditor report. (Bemby et al 2013). There is an opposite relationship between the audit timeliness and the quality of the financial statements. Moreover, the quality of accounting information may be less relevant with the passage of time (Atiase et al 1989). In year 2013, in Indonesia Stock Exchange (IDX), there are a 398 companies out of 422 that submitted their audit report on time. The results are aligned with the Financial Services Authority requirement which stated that publicly listed company must submit an annual financial statements report along with the independent auditors' report no later than the end of third month (90 days) after the date of the annual financial statements. Data from the Government shows that there are 24 companies that exceeded the 90 days period for publishing their annual and audit report which means that those companies suffers audit delay. On the other hand, Indonesia Stock Exchange has successfully implemented the Good Corporate Governance (GCG) as they are the facilitator and regulator of capital markets in Indonesia. The guidelines, frameworks, and principles of CG have been successfully implemented by IDX for its listed companies. In addition, IDX has been committed to do continuous improvements in practicing corporate governance in the future (Indonesia Stock Exchange, 2010). Based on the above evidences, this research will answer the following research question: Do Corporate Governance facets affect the audit report lag of the Indonesian public listed company?

II. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

IDX requires every listed company to compose their audit committee not fewer than three members which is amongst its directors. According to Mohamad-Nor et al (2010), if a company has large audit committee, the potential problem in a company are more likely to be uncovered and resolved. The situation might happen if only larger committee size could increase the resources available for the audit committee to conduct the audit and improve the audit quality. Apadore and Noor (2013) show that audit committee size are significantly associated with audit report lag in a negative direction. Furthermore, Mohamad-Nor et al (2010) also reveals a negative relationship between audit committee size and audit report lag. It shows that companies with more members in the audit committee are likely to release their audit report in a timely manner without

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delaying the audit and further audit report lag.The author then develops the following hypothesis about the relationship between audit committee size related with audit report lag: *Hypothesis 1: There is a negative relationship between audit committee size and audit report lag.*

Fama & Jensen (1983) researched about the separation of ownership and control and they argued that independent audit committee improve corporate governance because their existence help the company to resolve any disagreement that occur among internal managers and may oppose any controversial issues among internal auditors (Zain & Subramaniam, 2007). Furthermore, another empirical research by McMullen & Raghunandan (1996) show that by having independent audit committee member in a company may reduce financial reporting problem. Different from those other researchers, the research conducted by Krishnan (2005) shows that audit committee independence relation with internal control problems over financial reporting are less significant. Mohamad-Nor et al (2010) can not show any evidence that show any negative association between audit report lag and audit committee indepencence. Combining all of those findings and perspectives by other researchers, then the hypothesis is: *Hypothesis 2: There is a negative relationship between audit committee independence and audit report lag.*

Menon and Williams (1994) argued that the numbers of audit committee meeting is not to reliable to assess the work of audit committee because it does not truly reflect the effectiveness of the audit committee in improving the quality of a financial report. Nevertheless, lesser number of audit committee meetings do show lack of monitoring which will then show a less efficient work of audit committeee work on monitoring the management's activity. On the other hand, conducting an examination to identify the linkage between audit committee meetings and audit report lag by Bédard et al (2004) reported that number of audit committee meetings is not important if the members of audit committees are already dominated by the financial expertise and are independent. Moreover, Lin et al., (2006) also reported that audit committee meeting is not associated with the occurrence of financial report restatements that may lead to audit delay. According to these arguments, then the hypothesis is: *Hypothesis 3: There is a negative relationship between an audit committee that meets at least four times a year and audit report lag.*

A research conducted by Salleh & Baatwah (2014) examines whether audit committee chair with financial expertise enhances the role of its audit committee in order to improve financial reporting quality. They found out that audit committee chair with financial expertise improve the timeliness of audit reporting and reduce the possibility of any occurrence of audit delay. In addition, Ashton et al. (1989), as well as Davidson et al (2004) also argued that audit committee with financial expertise finish the audit quicker than the non-expertise. In addition, Krishnan and Lee (2009) concluded that firm that faced high litigation risk requested financial expertise to be among its audit committee in the firm. Oppositely, Tanyi et al. (2010) argued that audit report lags change after auditor switching occurred. Yatim et al. (2006) showed a contrasting result that audit committee with financial expertise led to higher audit fees. They argued that higher fees may be related to the audit quality demanded and may led to a longer audit report length and also audit delay. According to these arguments, then the authors hypothesis is: *Hypothesis 4: There is a negative relationship between audit committee financial expertise and audit report lag.*

According to Lipton and Lorsch (1992), large boards are less likely to criticise any policies to top management. Furthermore, larger board tends to discuss less meaningful discussion which is caused by too many directors that are involved, making the discussion to be time consuming and making it more difficult to attain cohesiveness. Jensen (1993) discovered that too many people inside the same geographical location may face difficulties when they are working together and could be less effective. In accordance with the research done by Lipton and Lorsch (1992) and Jensen (1992), another research done by Judge and Zeithaml (1992) concluded that larger board size tend to be less involved in making strategic decision. Moreover, Forbes and Miliken (1999) concluded that large board size may led to coordination problem in a company. Overall, referring to the widely obtained results prior related researchers described above, its it determined that large board size will enhance the timeliness of audit reporting which will then reduce possibilities of any audit delay. Then, the hypothesis is: *Hypothesis 5: There is a positive relationship between board size and audit report lag.*

Independent commissioner of a company must remain truly independent to be able to resist any influence or pressure from other parties, including shareholders, who have an interest in the company's purpose. Additionally, Indonesia Stock Exchange stated that every listed companies at the stock exchange should have independent commissioner which are equal with the number of shares owned by the minority of shareholders. Abdelsalam and Street's (2007) primary findings using multivariate analysis provide evidence that show a negative relation between board independence with audit timeliness. According to the Indonesia Stock Exchange rule, the minimum proporion of independent commissioner in a company is 30% of the entire board of commissioner. The proportion of independent commissioner is measured by counting the number of independent commissioner in a company. The results show that the percentage of independent commissioner has negative impact towards audit report lag. It means that greater percentage of independent commissioner will shorten the audit report lag. The the hypothesis is: *Hypothesis 6: There is a negative relationship between independent commissioner and audit report lag.*

III. RESEARCH METHOD

The data is collected from annual report taken from Indonesia Stock Exchange for the year 2013. Data analyzed will be used multiple regression and statistical tests. In this study, the authors use six independent variables to determine the companies' audit report lag as the dependent variable in this research. These six independent variables are audit committee size (ACSIZE), audit committee independence (ACIND), audit committee meetings (ACMEET4), audit committee financial expertise (ACEXP), board size (BSIZE) and independent commissioner (BIND). The model of multiple linear regressions is as follows:

$$Y_i = \beta_o + \beta_1 X_{1i} + \beta_2 X_{2i} + \ldots. + \beta_k X_{ki} + \in_{i,} \quad i = 1,2, \ldots., n$$

Where:
Y_i = the *i*-th observation of the dependent variable Y
X_{ji} = the *i*-th observation of the independent variable X_j, j = 1, 2,.., k
β_o = the intercept of the equation
$\beta_{1,\ldots,}\beta_k$ = the slope coefficients for each of the independent variables
$\in_I$ = the error term
N = the number of observations

Based on the general model of multiple linear regressions above, the model of this research is as follows:

$$AUDLAG = \beta_o + \beta_1 ACSIZE + \beta_2 ACIND + \beta_3 ACMEET4_i + \beta_4 ACEXP + \beta_5 BSIZE + \beta_6 BIND + \in_{i,}$$

Where:
β_o = the intercept of the equation
AUDLAG = Number of days from fiscal year end to the date of audit report
ACSIZE = Number of audit committee members
ACIND = Number of independent auditors divided by total number of audit committee members
ACMEET4 = Dummy variable 1, if at least 4 audit committee meetings are held during one year period, 0 otherwise
ACEXP = Number of audit committee who have accounting or related financial expertise divided by total number of audit committee members
BSIZE = Number of board of director and board of commissioner members *BIND* = Number of independent commissioner members divided by total number of board members

In multiple regression analysis, accuracy of the result from the regression model will be determined by the overall goodness-of-fit tests. In order to understand the regression model using goodness-of-fit, there are three tests that will be conducted which are F-test, t-test and adjusted R^2(DeFusco, McLeavey, Pinto, & Runkle, 2007). Adjusted R^2 is used to identify whether the independent variables in this research can explain the variation in dependent variable. The use of adjusted R^2 measurement is believed to be more reliable than R^2 because of the regression's goodness-of-fit of this research has been adjusted and it does not automatically change due to the addition of new variable in the regression (DeFusco, McLeavey, Pinto, & Runkle, 2007). To calculate the value of adjusted R2, the following formula should be applied:

$$\bar{R} = 1 - \left(\frac{n-1}{n-k-1}\right)(1 - R^2)$$

Where:
n= sample size
k= number of independent variables
The higher value of adjusted R^2, then the capability of independent variables to explain the changes of dependent variables will also rise.

IV. FINDING AND DISCUSSION

Table 1. Descriptive Statistics of Independent Variables

Descriptive Statistics

	N	Minimum	Maximum	Mean	Median	Std. Deviation
ACSIZE	422	2	8	-	3	.604014257
ACIND	422	.25	1.00	.63062796	-	.104314838
ACMEET4	422	0	1	-	1	.312015066
ACEXP	422	0	1.000000	.52061611	-	.217474139

BSIZE	422	3	27	-	8	3.460183497
BIND	422	.071429	.666667	.19642287	.19642287	.071553267

The first variable measurement of audit report lag is audit committee size which variable is symbolized with ACSIZE. The second variable measurement of audit report lag is audit committee independence and the variable is symbolized with ACIND which minimum value is 0.25 and maximum value is 1. The third variable measurement of audit report lag is audit committee meeting which variable is symbolized with ACMEET4. This variable uses dummy variable of 1, which indicates that the audit committee meeting is held for at least 4 times during one year period, and 0 otherwise. The fourth variable of audit report lag is audit committee expertise which variable is symbolized with ACEXP. Moreover, the maximum value of ACEXP is 1 which means that all members in the audit committee have accounting or financial expertise. The fifth variable measurement of audit report lag is board size which variable is symbolized with BSIZE. The variable has a minimum value of 3. Furthermore, the average number of board size is presented in the median section of BSIZE with the amount of 8 board members and the standard deviation is 3.46. The last variable measurement of audit report lag is independent commissioner (board independence) which variable is symbolized with BIND. The minimum value of this variable is 0.714. The mean of BIND is 0.196 and standard deviation of 0.071.

Table 2. Statistical Summary

Model	**Tolerance**	**VIF**	**t**	**Sig**
(Constant)			10.679	.000
ACSIZE	.829	1.206	-3.932	.000
ACIND	.924	1.082	-.324	.746
ACMEET4	.990	1.010	-.310	.756
ACEXP	.998	1.002	-.136	.892
BSIZE	.839	1.193	-4.225	.000
BIND	.952	1.051	-.793	.428

The value of adjusted R-square is 0.103 which means that 10.3% of the variation in AUDLAG as the dependent variable can be explained by the variances of the public listed company's ACSIZE, ACIND, ACMEET4, ACEXP, BSIZE and BIND. The rest 89.7% is affected by other factors which are not presented in the regression model. The first hypothesis assumes that audit committee size has a negative relationship towards audit report lag and the result of the regression shows the acceptance of hypothesis. This hypothesis has proven that ACSIZE is significantly affects the company's AUDLAG in a negative direction. This means that companies with more members in the audit committee are more likely to produce their audit reports in a timely manner without any further audit report lag which may result in audit delay. Hence, the hypothesis H1 is accepted. This result is consistent with the findings found by Mohamad-Nor, Shafie, & Wan-Hussin (2010) on their study over the corporate governance and audit report lag in Malaysian public listed companies in 2011, which claims that audit cocmmittee size have a significant negative relationship with audit report lag. The justification of negative significant effects given by audit committee size to audit report lag is also conculded by other researchers including Apadore & Noor (2013) and also by Bemby, Abukosim, Mukhtarudin, & Mursidi (2013).

The second hypothesis assumes that audit committee independence has a negative relationship towards audit report lag. However, the result of the regression shows that ACIND has a negative insignificant effect towards the company's AUDLAG and hypothesis H2 is rejected. This means that companies with more independent audit members in the audit committee are more likely to produce their audit reports in a timely manner without any further audit report lag. The result is inconsistent with the research done by Apadore & Noor (2013)with their research of analyzing the relation between the characteristics of corporate governace and audit report lag among 180 sample companies listed at Bursa Malaysia. Furthermore, the contradicting result is also generated by Mohamad-Nor, Shafie, & Wan-Hussin (2010) which research shows that there is a significant relationship between audit independence with audit report lag, however the beta value of regression also show a negative relationship towards audit report lag. The third hypothesis assumes that audit committee that meets at least four times a year has a negative relationship towards audit report lag. However, the result of the regression shows that ACMEET4 has a negative insignificant effect towards the company's AUDLAG. This means that companies that held audit committee meeting for at least four times a year means that they provide better accomplishment of the company's audit report lag. Hence, the hypothesis H3 is rejected. The negative value of the beta of t-test shows that the more number of meetings that the audit committee held, it will shorten the audit report lag of the company. The average number of meetings that the Indonesia public listed sample companies is seven meetings in a one year period. The average number is above the Indonesian Corporate Governance requirement which requires the public listed companies to held audit committee meeting for at least four times a year (or in a quarterly manner). The consistent result given in this research is align with the research done by Hashim and Rahman (2011) which shows that audit committee meeting that meet for at least four times in one year period has a negative insignificant influence towards audit report lag. However, the result does not show any significant influence between audit committee meeting and audit report lag which is contradicting with the result generated by Mohamad-Nor, Shafie, & Wan-Hussin (2010) which shows a significant relationship between the two variables.

In addition, another contradicting result is generated by Apadore & Noor (2013) which shows that there is a positive relationship which means that the audit committee meeting is positively affecting the audit report lag.However, the result of this research is aligned with the research done by Uzun et al. (2004), which the result of the research shows that there is an insignificant association between audit committee meeting held with audit report lag. In order to improve the quality of audit report, the company needs to ensure that in every audit committee meeting, the member should raise and resolve issued with the company's management (Hashim and Rahman, 2011). The fourth hypothesis assumes that audit committee financial expertise has a negative relationship towards audit report lag. However, the result of the regression shows that ACEXP has a negative insignificant effect towards the company's AUDLAG. This means that companies with more audit committee expertise does not means that they provide better accomplishment of the company's audit report lag. However, with a negative direction of the t-test result, it shows that the more number of audit committee expertise in a company, it will improve the quality if the audit report which will then shorten the audit report lag. Hence, the hypothesis H4 is rejected.

The contradicting result is generated by Apadore & Noor (2013) which research shows the beta value of regression results in a positive relationship between audit committee expertise towards audit report lag. The result is consistent with the research done by Mohamad-Nor, Shafie, & Wan-Hussin (2010) whose research resulted in a insignificant negative influence between audit committee expertise and audit report lag. It is true that if the audit committee's composition is dominated by committee that has accounting and financial background, it will affect the timeliness of audit reporting. Even though it is good to have so, but it is not really significant with the audit timeliness. In the rule also stated that it needs at least one member with the finance and accounting background already fulfill the criteria and if there is more than one, it will not really affect the audit report lag. This is also related to the agency theory which is agency cost. It is costly to hire professional rather than people that have more experience to do the audit. In the real world, resources are limited and time is also limited. So by having so, the company can lower the agency cost in the company. This result is also consistent with the findings by Hashim and Rahman (2011) whose research resulted that audit cocmmittee with accounting and financial expertise have a insignificant negative relationship with audit report lag.

The fifth hypothesis assumes that board size has a positive relationship towards audit report lag. The result of the regression shows that BSIZE significantly affects the company's AUDLAG in negative direction. This means that the broader the size of the board, then the length of the audit report lag will decrease. The broader size of the board makes it easier for the board to monitor the work of the ones who are making the audit report and also the work of the board itself, rather than a smaller size of board. Based on the regression result, the hypothesis H5 is rejected. This outcome contradicts with the previous findings which is done by Mohamad-Nor, Shafie, & Wan-Hussin (2010) when they conducted the research among Malaysian public listed companies. They concluded that board size of a company have a positive relation towards audit report lag. However, with the insignificant result generated by their research, this demonstrates that according to their research the board size variables are not as important as the audit committee size in determining the audit report lag of the companies. Furthermore, a broader size of the board may increase the effectiveness of the work of the board for monitoring the audit committee's performance. If the performance of audit committee is satisfying, then the audit report timeliness will also resulted in a satisfying manner. This has explained why the relationship between board size and audit report lag are negatively associated.

The last hypothesis assumes that independent commissioner has a negative relationship towards audit report lag. However, the result of the regression shows that BIND has a negative insignificant effect towards the company's AUDLAG and hypothesis H6 is rejected. This means that companies with more independent commissioners in the company's board are more likely to produce their audit reports in a timely manner without any further audit report lag. This result is consistent with the findings by Bemby, Abukosim, Mukhtarudin, & Mursidi (2013) on their research which claims that board independence have a insignificant negative relationship with audit report lag. In contrast, the outcome of this research contradicts with the conclusions made by Mohamad-Nor, Shafie, & Wan-Hussin (2010) and Apadore & Noor (2013) when they studied on the companies listed in Bursa Malaysia.

V. CONCLUSION

This research is intended to examine the relation between corporate governance facets and the audit report lag in Indonesia, especially the firms listed in the Indonesia Stock Exchange. First, audit committee size is proved to have significant relationship towards audit report lag in a negative direction. The evidence of the research indicates that companies with more members in their audit committee are more likely to produce their audit report in a timely manner and without any further audit report lag. Second, audit committee independence is proved to have insignificant relationship towards audit report lag in a negative direction. Therefore, if there is more independent committee composition in the audit committee, then audit report lag may be reduced. Third, audit committee meetings is proved to have insignificant relationship towards audit report lag in a negative direction. This shows that the more meetings that are held by the audit committee could reduce the audit report lag on the sample companies.

The evidence of this research indicates that more audit committee meeting may affect the timeliness of audit reports. Fourth, audit committee expertise is proved to have insignificant relationship towards audit report lag in a negative direction. This means that companies may improve the timeliness of their audit report if the composition of its audit committee is filled with more audit committee that has accounting and financial expertise. Through the negative direction given as the result, it indicates that audit committee that has more accounting and financial knowledge may shorten the audit report lag. Fifth, board siz is proved to have significant relationship towards audit report lag in a negative direction. A broader size of the board may increase the effectiveness of the work of the board for monitoring the audit committee's performance in preparing the audit report in a timely manner.

Lastly, independent commissioner is proved to have insignificant relationship towards audit report lag in a negative direction. This means that companies with more independent commissioners in the company's board are more likely to produce their audit reports in a timely manner without any further audit report lag. However, the result of this study also suggests that more emphasis should be implemented in this research in order to strengthen the influence of board independence towards audit report lag.In conclusion, the number of audit committee has a significant influence towards the audit report lag. The other five variables will also help the company to reduce the time needed to produce the audit report, however it will not as significant as the audit committee size. The Authority/regulator then should strengthen the regulations for all public listed company in order to create a good synergy to improve the implementation of Corporate Governance in Indonesia.

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