

# The Influence of Professional Ethics, Enterprise Risk Management, Accounting Information Systems and Corporate Governance of the Quality of Income and Implications in the Scope of Audit: Analysis in BEI LQ 45

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## Abstract:

*Earnings quality and scope of the audit, which is associated with ethical issues and risk management studies have been conducted. This study aims to examine the factors that become determinant in the scope of the audit. If the signal is analyzed through theory (signaling theory), the results of this study support the theory. The company's capital expenditure (capex) seems very important in the effort to enhance shareholder value. Target population in this study is a state that has gone public on the Indonesian Stock Exchange (BEI) LQ45, which consists of 13 state-owned enterprises that have gone public on the 140 state-owned enterprises (SOEs Performance Report 2003 until 2007). Measurement techniques used to transform qualitative data from the questionnaires into a quantitative data is Summated Rating Method - The Likert Scale, which is an ordinal scale of measurement. Subject measured is not limited to only two alternative answers. Scores for the second assessment criterion variable calculated by 5-point scale: agreement / disagreement. Income or additional variables Management Accounting System to be one of the determining factors for the company's earnings quality. Earnings quality has a high precision will be positive for the stock value. The influence of earnings quality enough to give simplifying the Scope of Audit.*

## Keywords

*Professional Ethics, Enterprise Risk Management, Accounting Information Systems, Corporate Governance and Earnings Quality*

## 1. Introduction

Bankruptcy or collapse of the leading companies in the world have resulted in the level of public confidence in financial reporting and public accounting profession is becoming increasingly fade (lose faith). Steward Hamilton and Alicia Mick Lethwait [1] mentions that the main cause of bankruptcy can be grouped into six categories, namely Poor Strategic Decisions, Over Expansion and Ill-Judged Acquisitions, Dominant CEO's, Greed, hubris, and The Desire for Power, Failure of Internal Controls at All Levels from The Top Downwards and Ineffectual or ineffective Boards (Enron, Tyco, Swissair). This phenomenon indicates that the financial statements have failed to meet the information needs of users of financial statements. Profit as the part of the financial statements do not present the actual facts about the economic condition of the company so that the profits are expected to provide information to support decision making becomes questionable quality. Profits do not show the actual information about management performance can mislead the users of the report. Earnings quality in particular and the quality of financial reporting in general is important for those who use the financial statements due to the investment decision making contract objectives [2]. Factors that affect the quality of earnings is their corporate governance mechanisms (for example audit committee, independent commissioner, ownership) which is modeled as discretionary accruals using three models: the model modified ones, Jones models and De Angelo models.

Tests conducted on 45 manufacturing companies listed in Indonesia Stock Exchange (BEI LQ45) that generate profits (earnings) and implement corporate governance during 2008-2012. Testing of this study is using classical assumption test and multiple

regression analysis. This research is the topic of earnings quality and scope of the audit, particularly those related to ethical issues and risk management. According to the researchers of this topic becomes important and very relevant for further investigation at this time, because of the actions of management in the management company cannot be separated from the problem of interest, as described in agency theory. Problem interests of company ultimately very familiar with the ethical and moral issues. The research problems are comprised of:

- 1.1. The influence of the Quality of Earnings Professional Ethics and its implications on the Scope of Audit.
- 1.2. The influence of Enterprise Risk Management on the Quality of Earnings and the implications for the Scope of Audit.
- 1.3. The influence of Accounting Information Systems on the Quality of Earnings and the implications for the Scope of Audit.
- 1.4. The influence of the Quality of Earnings corporate Governance and its implications on the Scope of Audit.

## 2. Research Purposes

The purpose of research is desirable to achieve is to get empirical evidence about the influence of Professional Ethics on the Quality of Earnings and the implications for the Scope of Audit, the influence of the Enterprise Risk Management on the Quality of Earnings and the implications for the Scope of Audit, the influence of Accounting Information Systems on the Quality of Earnings and the implications for Scope audit and Corporate Governance influence on the Quality of Earnings and implications on the Scope of the audit.

## 3. Theoretical Framework

Business ethics resulting from the interaction of personal moral and processes as well as business purposes can be said that business ethics is nothing more than personal views on right and wrong are applied in business [3]. Ethics is generally defined as moral principles or values. Each person has a different set of values, although cannot be disclosed explicitly. Ethical principles contained in the code of conduct the public accounting profession is Integrity, Objectivity, Competence and Prudential, Confidentiality and Principles of Professional Conduct.

Factors considered to influence the attitudes and ethical behavior of accountants as well as factors that are considered the most dominant influence on the attitudes and behavior of unethical accountants are religiosity, education, organizational, emotional

quotient, family environment, life experiences, remuneration, legal, and position or position.

The conceptual framework underlying this study is based on a Grand Theory of the Agency Theory [4] which defines an agency relationship as a contract in which one or more (principal) hired another person (the agent) to perform some service on their behalf by delegating some decision-making authority to the agent.

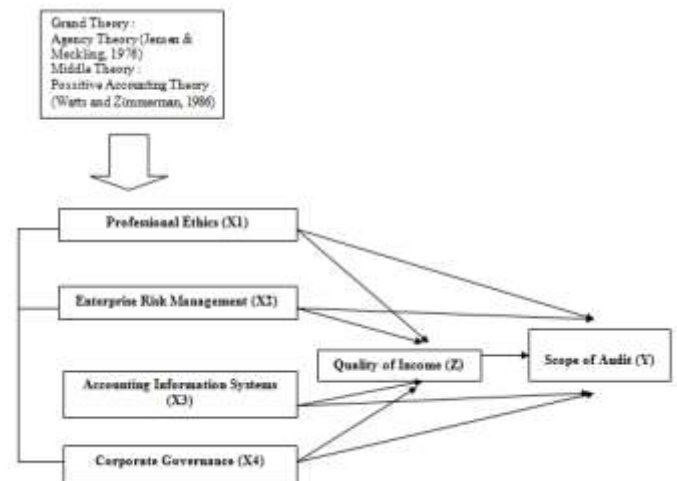


Figure 1. Conceptual Framework of Research.

Enterprise Risk Management is a process that is influenced by the board of directors, management, and personal other entities, applied in strategy implementation and applied throughout the enterprise, designed to identify potential events that may affect the entity, and manage risk in order to stay within range of risks, so that can provide reasonable assurance regarding the achievement of the organization.

Accounting Information Systems (AIS) is an information system that handles everything with regard to accounting. Accounting is actually an information system. SIA formed an important function in an organization include:

- Collect and store data about the activities and transactions.
- Processes data into information that can be used in the decision making process.
- Perform precise control of the assets of the organization.

Corporate Governance can be translated as corporate governance. The word governance is derived from Old French meaning that governance control (control) or regulated and can be regarded as a state that is under controlled conditions. The influence of implementation of corporate governance at the corporate level of the quality of earnings will be influenced by the level of protection for investors in the country. The legal environment in a country with regard to investor protection will affect the

implementation of corporate governance at the company level.

Earnings quality is closely related with the objective presentation of financial information (objective of financial reporting). Earnings quality accounting is accounting income have little or no perceptual disturbances (perceived noise) therein and may reflect the financial performance of the real (Chandrarain, 2003) in [5], while the other states that accounting earnings quality is said if the elements that make up the profit can be interpreted and understood satisfactorily by an interested party [6]. Earnings quality may be indicated as the ability to gain information to respond to the market.

The scope of the audit is an examination of which will be conducted by an auditor in an audit process. The audit scope can be defined broadly or narrowly by an auditor during the audit planning. Broad or narrow a scope of the audit is related to the large amount of evidence that must be collected by the auditor, to give him confidence in the provision of audit opinion after the audit carried out. The scope of the comprehensive audit means that an auditor require material evidence more, while the narrow scope of the audit means that an auditor does not require proof that many in the audit process.

Economic approach to the need for an independent auditor in auditing perspective can be attributed to the basic theory of agency / agency (the agency theory), namely the relationship between the owner (principal) and management (agent). With the development of the company the greater the frequent conflicts between the principal in this case are the shareholders (investors) and the agent represented by the management (board of directors). The assumption that management is involved in the company will always maximize the company's value is not always met. To reduce the agency problem, it needs an independent party who can be the mediator in the handling of the conflict known as the independent auditor or KAP [7].

The Positive Accounting Theory clearly stated by Watts and Zimmerman [8]. This theory seeks to understand why the accounting policy becomes an issue for the company and the parties concerned with the financial statements, and to predict its accounting policies to be chosen by the company under certain conditions. This theory is based on the view that the company is a "nexus of contracts".

#### 4. Research Methodology

Hypothesis their alleged relationship logically between two or more variables in the formulation of propositions that can be tested empirically [9]. The following research hypothesis elaborated in

accordance with the paradigm of research variables linkages are arranged as follows:

- 4.1. Professional Ethics influence of the Quality of Earnings and Implications Scope of Audit
- 4.2. Enterprise Risk Management influence of the Quality of Earnings and Its Implication Audit Scope either simultaneously or individually
- 4.3. Influence of Earnings Quality and Its Implication of Audit Scope either simultaneously or individually
- 4.4. Quality of Earnings influences the Scope of Audit.

The method used in the study was a survey approach to census taking and non experimental. Target population in this study is a state that has gone public on the Indonesian Stock Exchange (BEI), which is composed of 13 state-owned enterprises that have gone public on the 140 SOEs (Performance Report SOE 2003 until 2007), this research is done by taking the entire company as a population to be the object of research. The unit of analysis of this research is a state that has gone public on the Indonesian Stock Exchange. Respondents in this study are: Financial Manager, External Auditors, and the Audit Committee of the SOEs to go public on the Indonesian Stock Exchange. Measurement techniques used to transform qualitative data from the questionnaires into a quantitative data is Summated Rating Method - The Likert Scale, which is an ordinal scale of measurement. Subject measured is not limited to only two alternative answers. Scores for the second assessment criterion variable calculated by 5-point scale: agreement / disagreement. Income or additional variables Management Accounting System to be one of the determining factors for the company's earnings quality.

The research data was obtained by submitting a list of questions to respondents through the questionnaire, the answers of the respondents to this question is a measure that will be tested. Data obtained from the respondents need to be tested for validity and reliability to avoid things that are biased and question the validity of this study. The variables used in this study are the following: Professional Ethics (X1) and Enterprise Risk Management (X2), Accounting Information Systems (X3) and Corporate Governance (X4) as an independent variable. The Quality of Earnings (Z) and Scope of Audit (Y) as the dependent variable.

To analyze the data in this study used path analysis (path analysis) with the help of IBM SPSS Software 2.0. The use of path analysis with the consideration that the pattern of relationships between the variables in this research is correlative and causal. Path analysis is used because it is conceptually inter variable exogenous relations. With

path analysis can know the level of influence of each independent variable, either directly or indirectly.

## 5. Research Results Analysis

### 5.1. Measurement Data

Description of the result of the measurement data of each variable in the distribution of questionnaires still are in a situation of normality. Influence factors show that:

- 5.1.1. Professional Ethics. Measurement data obtained are in the Normal Distribution with Value Expectations of Professional Ethics of 6.7 and a standard deviation of 0.88. Pengaruh professional ethics is quite significant for the respondents, with the value of this expectation can be said that two thirds of respondents strongly uphold professional ethics.
- 5.1.2. Enterprise Risk Management (ERM). Measurement data obtained are in the Normal Distribution with Enterprise Risk Management Expected Value of 6.4 and a standard deviation of 0.77. ERM significant influence. More than 60% of respondents are considering the company's refineries risk.
- 5.1.3. Accounting Information Systems. Measurement data obtained are in the Normal Distribution with Enterprise Risk Management Expected Value of 8.4 and a standard deviation of 0.49. Effect of Accounting Information Systems has become of primary importance for the respondents.
- 5.1.4. Corporate Governance. Measurement data obtained are in the Normal Distribution Rated Corporate Governance expectations of 7.7 and a standard deviation of 0.94. Influence of Corporate Governance is indispensable for the respondents to carry out their duties.
- 5.1.5. Quality of Earnings. Measurement data obtained are in the Normal Distribution Rated Quality Earnings Expectations of 8.4 and a standard deviation of 0.63. Effect of Earnings Quality is also a major component to earn a good profit results and sustainable.
- 5.1.6. Scope of Audit. Measurement data obtained are in the Normal Distribution Rated Quality Earnings Expectations of 2.1 and a standard deviation of 0.51.
- 5.1.7. Scope of Audit has been well understood by the respondents that the scope of the integrated audit would be very efficient.

### 5.2. Linear Regression Analysis

Withdrawal relation to each independent variable to variable Scope of Audit can be stated that:

- 5.2.1. Relation Quality of Earnings has a coefficient of linear relationships were very weak on Professional Ethics, namely the determination coefficient of 0.0142. However it has a tendency to increase the professional ethics that will raise slightly Quality of Earnings.
- 5.2.2. Relation Quality of earnings has a coefficient of linear relationships were very weak against the ERM, namely the determination coefficient of 0.0524. However it has a tendency that the increase of professional ethics will shrink slightly Quality of Earnings.
- 5.2.3. Relation Quality of Earnings has a coefficient of linear relationship better against Accounting Information Systems, namely the determination coefficient of 0.3459. So it is apparent that the tendency of the influence of Accounting Information Systems will simply increase Earnings Quality
- 5.2.4. Quality of Earnings coefficient relation weak relation to corporate governance, namely the determination coefficient of 0.1016. However it has a tendency that sufficient improvement of corporate governance will increase the Quality of Earnings.

### 5.3. Multiple Linear Regression Analysis

Linear regression equations for four independent variables can be expressed as follows,

$$z = f(x_1, x_2, x_3, x_4) = \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_3 + \beta_4 x_4 + C$$

Where,

- z = Quality of Income (RLA)
- X1 = Enterprise Risk Management (ERM)
- X2 = Professional Ethics (EP)
- X3 = Accounting Information Systems (AIS)
- X4 = Corporate Governance (CG)
- $\beta_1, \beta_2, \beta_3, \beta_4$  = Coefficient of determination.
- C = Constant

T tests were used to determine whether the independent variables partially real effect or not on the dependent variable. The degree of significance used was 0.05. If the value is significantly smaller than the degree of confidence then we accept the alternative hypothesis, which states that partially independent variables affect the dependent variable. T test results can be shown in Table 1 below.

Table 1. Test Results

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Correlations
	B	Std. Error	Beta			Zero-order
(Constant)	2.345	2.241		1.047	0.305	
EP	0.022	0.116	0.03	0.187	0.853	0.119
ERM	-0.059	0.137	-0.073	0.434	0.668	-0.229
SIA	0.851	0.229	0.51	2.84	0.009	0.588
CG	0.113	0.111	0.171	1.021	0.317	0.319

F test used to determine whether the independent variables simultaneously significant effect on the dependent variable. Confidence level used was 0.05. If the F value calculation result is greater than the value F according to the table then the alternative hypothesis, which states that all independent variable simultaneously significant effect on the dependent variable. Test results simultaneously  $x_1$ ,  $x_2$ ,  $x_3$  and  $x_4$  to y can be shown in Table 2 below.

Table 2. F Test Results, ANOVA<sup>a</sup>

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	4.257	4	1.064	3.743	.016 <sup>b</sup>
Residual	7.109	25	.284		
Total	11.367	29			

- a. Dependent Variable: KL
- b. Predictors: (Constant), CG, ERM, EP, SIA

### 5.4. The Coefficient of Determination (R<sup>2</sup>)

The results of the correlation calculations and determinations are shown in Table 3 below.

Table 3. Correlation Coefficient and Determination

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics		
					R Square Change	F Change	df1
1	.612 <sup>a</sup>	0.375	0.274	0.533	0.375	3.743	4

The results of the correlation calculations and determinations (R<sup>2</sup>) value is 37.5%, or 0,375. This value has good impact strength. Simplification implications for earnings quality analysis of the scope of the audit, the analysis used is the analysis of the linearity of the method of least squares linear regression. Linearity simulation calculation results are shown in Tables 4 and 5 as follows.

Table 4. Simulation Results and Linearity

Model	Unstandardized Coefficients		Standardized Coefficients	Sig.
	B	Std. Error	Beta	
(Constant)	3.419	1.272		2.688
KL	-0.152	0.15	-0.188	-1.014

Table 5. Correlation Coefficient Linearity

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics		
					R Square Change	F Change	df1
1	.188 <sup>a</sup>	0.035	0.001	0.507	0.035	1.028	1

The coefficient relationship with R<sup>2</sup> = 0.035, or 3.5%, showing the influence of Earnings Quality on Scope of Audit is very weak. But with gradient = -0.152 (negative) indicates the relationship is in the opposite direction, in other words with increasing earnings quality will far Scope of Audit.

## 6. Conclusion and Recommendation

### 6.1. Conclusion

Study (paper) aims to examine the factors that become determinant in the scope of the audit. The conclusions of this research are as follows:

- 6.1.1. There is a good influence on the Quality of Professional Ethics and its implications Profit Audit Scope.
- 6.1.2. There is a good influence between Enterprise Risk Management (ERM) on the Quality of Earnings and the implications for the Scope of Audit

- 6.1.3. There is a good influence between Accounting Information Systems on the Quality of earnings and its implications on the Scope of Audit.
- 6.1.4. The existence of good Corporate Governance Influence on the Quality of Earnings and the implications for the Scope of Audit.
- 6.1.5. There is a good influence between Earnings Quality to Scope of Audit.

## 6.2. Recommendations

Referring to the opinion that the object of this research is the influence of Professional Ethics, Enterprise Risk Management, and Accounting Information Systems on the Quality of Earnings and the implications for the Scope of Audit. The next study is inserting or adding variables Management Accounting System. Management Accounting System is one of the company's internal factors as a determinant profits quality for the company.

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