

THE EFFECT OF CEO POWER ON THE SELECTION OF QUALIFIED AUDITORS WITH PROFITABILITY AS MODERATOR

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ABSTRACT

This study aims to determine the effect of CEO Power on the selection of qualified auditors with profitability as a moderator. This study uses a sample of small and medium-sized enterprises listed on the PEFINDO 25 index May 2023, the data used is company data from 2020-2022. Hypothesis testing using logistic regression analysis. The results of the study show that profitability does not moderate the influence of CEO Power on the selection of qualified auditors. The results of this study are expected to increase literacy regarding what factors can influence the selection of auditors. In addition, the CEO of the company also must consider thoroughly when selecting auditors for his/her company in order to maintain the quality of company's financial reporting.

Keywords: CEO power, profitability, selection of qualified auditors, audit quality

ABSTRAKSI

Penelitian ini bertujuan untuk mengetahui pengaruh CEO Power terhadap pemilihan auditor berkualitas dengan profitabilitas sebagai moderator. Penelitian ini menggunakan sampel perusahaan kecil dan menengah yang terdaftar di indeks PEFINDO 25 Mei 2023, data yang digunakan adalah data perusahaan tahun 2020-2022. Pengujian hipotesis menggunakan analisis regresi logistik. Hasil penelitian menunjukkan bahwa profitabilitas tidak memoderasi pengaruh CEO Power terhadap pemilihan auditor yang berkualitas. Hasil penelitian ini diharapkan dapat meningkatkan literasi mengenai faktor-faktor apa saja yang dapat mempengaruhi pemilihan auditor. Selain itu, CEO perusahaan juga harus mempertimbangkan secara matang dalam memilih auditor untuk perusahaannya guna menjaga kualitas pelaporan keuangan perusahaan.

Kata Kunci: CEO power, profitabilitas, pemilihan auditor berkualitas, kualitas audit

INTRODUCTION

Companies in the current era of globalization are increasingly advancing and developing, ranging from family companies to companies that have gone public. The more advanced go public companies are, the more they are required to provide quality financial reports. To ensure the quality of financial reports, a qualified auditor is also needed. Reliability and a high level of trust in financial reports can be obtained by having audit activities carried out by high-quality external auditors because the resulting audit results can guarantee that the information is correct (Destin & Margani, 2018).

Several previous studies have succeeded in proving that auditor quality affects the quality of audited financial statements. Research conducted by (Sitorus, 2019) succeeded in showing that auditor quality proxied by KAP size and audit capacity stress affects the quality of financial reports. Research conducted by (Alzeban, 2020) also shows that the quality of external auditors has a positive influence on the quality of financial reports.

Investors are one of the company's external stakeholders who will use the information in the company's financial statements. Decision making by investors will certainly affect the company. Thus, the selection of an auditor who will audit the company's financial statements is one of the important things that must be considered by the company, because investors will certainly consider more positively the quality of financial reports.

The selection of the external auditor is the process of selecting a Public Accounting Firm registered with the OJK. As of August, 2022 there were 363 KAPs registered with OJK. Of the hundreds of KAPs registered throughout Indonesia, there will be differences in the quality of auditors from one to another.

Auditor quality can be measured through various measurement tools, one of which is by looking at the size of the Public Accounting Firm. The size of a Public Accounting Firm can be said to be large if the Public Accounting Firm is affiliated with Big 4, and the size of a Public Accounting Firm is said to be small if it is not affiliated with Big 4 (Aprianti & Hartaty, 2016). Research conducted by (Hamid, 2013) shows that Big 4 Public Accounting Firms are of higher quality than Non-Big 4 Public Accounting Firms. This indicates that auditors registered with Big 4 Public Accounting Firms show better quality than auditors who are not registered. at the Big 4 Public Accounting Firm.

Several researchers have tried to examine the factors that influence the selection of external auditors, one of which is CEO Power. Research conducted by (Palembangan & Dewi, 2018) succeeded in proving that CEO power has a significant influence on auditor selection. CEO is the highest position in a company that has the duty to lead the company and has responsibility for maintaining the stability of the company (Noval, 2015).

A powerful CEO is a person who consistently influences key decisions within the company despite opposition from other executives (Adams et al., 2005; Sudana & Aristina, 2017). CEO power is the power possessed by the CEO through company share ownership, the greater the number of shares owned by the CEO, the greater the CEO's power in the company (Pandiangan, 2022). Research by (Ouyang et al., 2015) shows that the relationship between CEO power and auditor selection is positive, this means that the greater the CEO's power, the CEO tends to prefer quality auditors. Therefore, CEO Power influences the selection of qualified auditors.

Profitability is a measuring tool in the form of a ratio that describes a company's ability to generate profits (Toni et al., 2021). Companies with increased profitability will tend to choose quality auditors, because with this increase in profits, they are able to pay for the services of a higher quality auditor (Sinaga et al., 2021). In this study, it will be tested whether profitability can moderate the relationship between CEO power and the selection of quality auditors. CEOs who have share ownership in companies that have good profitability will tend to choose qualified auditors.

THEORY, LITERATURE REVIEW, AND HYPOTHESIS

Contingency theory in the context of organizational theory pays attention to the identification of contextual and situational variables that can have potential implications for organizations, especially in management control systems (Chenhall, 2006). Specifically, it is also stated that the contingency approach in organizational behavior is that different environments lead to different behaviors (Irfan et al., 2016). Several studies have proven that several contextual variables can determine the selection of auditors, such as corporate governance which has a positive influence and corporate complexity which has a negative influence (Trisnawati, 2015). Research by (Ouyang et al., 2015) proves that the CEO power variable influences the selection of quality auditors. Profitability is thought to moderate the relationship between CEO power and the selection of quality auditors. CEOs who have share ownership will tend to choose qualified auditors to show that the quality of their financial reporting is good, this will be strengthened if the company has high profits because the company will be able to pay more qualified auditors. Therefore, the hypothesis to be tested is:

H1: Profitability is able to moderate the CEO Power relationship and the selection of quality auditors.

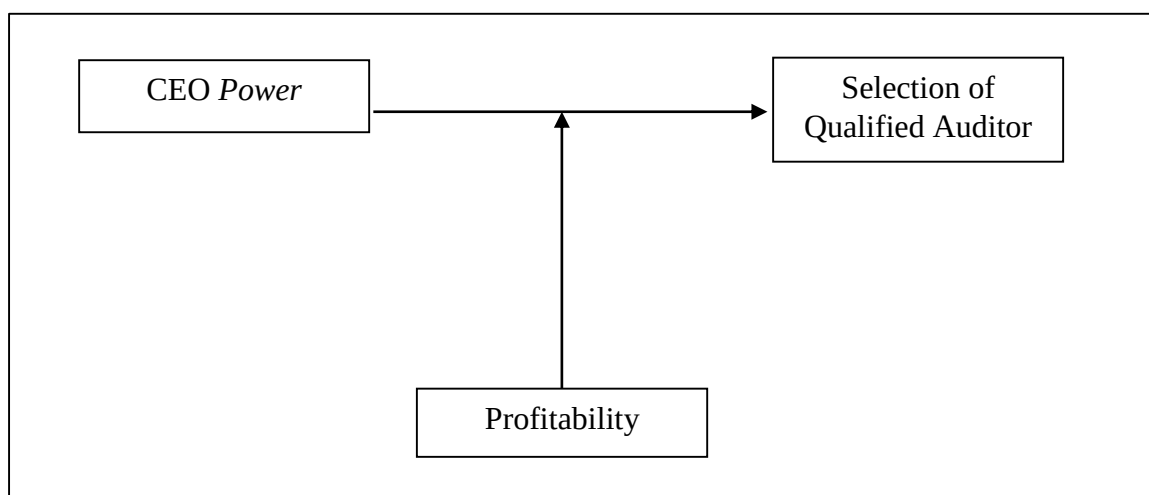


Figure 1.
Research Framework

RESEACRH METHODS

Population and sample

Population of this study is all the company listed in IDX. The sample in this research is 25 small and medium enterprises indexed in Pefindo 25 for the period May 2023. This index consists of shares of small and medium enterprises with good fundamental and liquidity performance which are listed on the IDX. The data used is data from these 25 enterprises from 2020-2022.

Variable Measurements

Table 1.
Variable Measurements

Variables	Measurements
CEO Power	CEO share ownership; If the CEO is listed as owning shares, then it is given a score of 1, if not, it is given a score of 0
Profitability	Return on Asset (RoA)
Qualified Auditor	Quality auditors are also measured by a dummy, if the KAP used is included in the BIG 4 and its affiliates, it is given a score of 1, if not then given the number 0.

Analytical Technique

To test the hypotheses in this research, logistic regression method was used. Logistic regression is a statistical analysis method for modeling the relationship between variables using a nominal or ordinal scale (Muflahah, 2017).

RESULTS AND DISCUSSION

The results of hypothesis testing using logistic regression are shown in the following table:

Table 2.
Hypothesis Test Results

	B	S.E.	Wald	df	Sig.	
ROA	0.065	0.054	1.409	1	0.235	
CEO_Power(1)	-0.877	0.0858	1.046	1	0.306	
ROA_Power (Moderating Effect)	0.009	0.080	0.013	1	0.908	H1 Not Supported
Constant	0.835	0.608	1.883	1	0.170	

The statistical testing showed the significance number of 0,908 which is higher than 0,05. Based on this result, the hypotheses in this research which stated that profitability moderate the relationship between CEO power and the selection of quality auditors cannot be supported. In accordance with the contingency theory, the contextual and situational variables in this study show different results from the initial assumption. Profitability is not statistically proven to strengthen or weaken CEO Power's decision in choosing a qualified auditor.

FINDINGS AND CONCLUSION

This research examines 25 small and medium companies included in the Pefindo25 index. The Pefindo25 index consists of 25 stocks selected based on their financial performance and liquidity, as well as high amounts of public ownership. The research period starts from 2020-2022, 75 data are analyzed. The results of statistical tests show that profitability does not significantly affect the relationship between CEOs who own shares of companies indexed at Pefindo25, and the selection of qualified auditors. Based on the data collected, 76% of CEOs own company shares, and 68% of companies use qualified auditors. With an average profitability of 10.57% and a significance value in the hypothesis test, profitability has not been able to strengthen or weaken the relationship between CEO power and the selection of quality auditors. It is possible that there are other factors that can moderate or mediate the relationship between CEO power and the selection of qualified auditors.

The limitation of this research is that the number of companies is too small. The Pefindo25 index was chosen because they chose 25 small and medium companies listed on the IDX, but the results showed that the hypothesis was not supported, so future researchers can use other index that have a larger number, or use a specific company size measurement scale, such as sorting total assets. from the smallest to the medium, so that the company data studied becomes broader and truly describes small and medium-sized companies. The theoretical implications of the results of this study are expected to increase literacy regarding what factors can influence the selection of auditors. Even though the result of this study shows no moderating relationship of profitability to CEO Power and the decision to choose high quality auditor, it is relevant to say that the decision to choose high quality auditor is an important decision to make for the CEO. Auditor choice could determine the quality of financial reporting and future improvement of the company (Behbahaninia, 2022) thus the company's CEO has to consider thoroughly when choosing the auditor for his/her company. Regarding to the future research, it is suggested to expand the sample and investigate another factor which can affect auditor choice in the company such as agency cost, expertise of CEO or board members, etc.

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