

Construction of Financial Statement Integrity Model in Indonesia

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Abstract

This study investigates financial statement integrity's crucial role in guiding stakeholders' economic decisions, embodying trust, honesty, reliability, and loyalty. Using a saturation sample of 40 banking companies listed on the IDX in 2022, data on independence, organizational commitment, and audit quality are collected through questionnaires. Information on the audit committee and financial statement integrity is obtained from idx.co.id. The partial least square analysis reveals that organizational commitment strengthens the link between the audit committee, independence, and audit quality. Audit quality, as a mediator, amplifies the impact of the audit committee and independence on financial statement integrity. This research contributes by introducing organizational commitment as a moderator and examining the mediating role of audit quality in the theoretical understanding of financial statement integrity. Organizations should prioritize and enhance organizational commitment to influence financial statement integrity. Limitations include the focus on banking companies and the use of a saturation sample, potentially limiting generalizability.

Keywords: audit committee, audit quality, financial statement integrity, independence, organizational commitment.

INTRODUCTION

The integrity of financial statements refers to the presentation of accurate information that aligns with actual conditions. This aims to ensure that stakeholders are not misled in making economic decisions. In the context of the capital market, honesty in financial reporting is a crucial factor in building and maintaining investor confidence. The integrity of financial statements could be enhanced if an independent Public Accountant (PA; Akuntan Publik (AP)) conducts the audit process. To ensure corporate financial transparency and maintain investor confidence, Public Accountants must uphold audit quality by strictly adhering to the Public Accountant Professional Standards and the Public Accountant Professional Code of Ethics. This commitment is crucial not only for the credibility of financial reports but also for the sustainability of the audited company and the Public Accounting Firm (PAF) itself. However, in practice, auditor independence remains a challenge, often compromised by conflicts of interest and ineffective audit oversight mechanisms (Nugrahanto & Alhadi, 2021).

The controversy surrounding the financial statements of Garuda Indonesia Airways in 2019 serves as an example. The 2018 financial report indicated a net profit of 809.85 thousand USD, a

stark contrast to the 216.5 million USD loss reported in 2017. This sharp increase sparked debate, as two commissioners of Garuda Indonesia raised concerns that the 2018 financial statements did not comply with the Statement of Financial Accounting Standards (SFAS). This case underscores the ongoing discussion on audit quality and financial statement integrity, highlighting the need for further research to address gaps in regulatory compliance and reporting transparency. The case of Garuda Indonesia highlights concerns regarding audit quality and financial statement integrity, particularly in relation to auditor independence. The airline included profits from PT Mahata Aero Teknologi, a company that had yet to fulfill its financial obligations for the installation of Wi-Fi routers. Tanubrata, Sutanto, Fahmi, Bambang, and Rekan (Member of BDO International) ultimately secured approval from the Ministry of Finance for their provisional agreement (Hartomo, 2019). This phenomenon underscores the critical role of audit quality as a mediating factor in ensuring the reliability of financial statements. Furthermore, the lack of organizational commitment to ethical financial reporting may have exacerbated the situation, highlighting the need for stronger governance frameworks to uphold auditor independence and maintain financial statement integrity.

In 2020, PT Asuransi Jiwasraya (Persero) faced another financial reporting issue, highlighting concerns over financial statement integrity. An investigation by the Supreme Audit Board (SAB) and the Badan Pemeriksa Keuangan (BPK) into Jiwasraya's 2017 profit bookings revealed discrepancies in its financial reporting. The audit findings indicated that the reported profit of IDR 360.3 billion was significantly affected by a reserve shortfall of IDR 7.7 trillion. This discrepancy suggested that, had the company adhered to the required reserve provisions, it would have incurred substantial losses. Subsequently, Jiwasraya reported an unaudited loss of IDR 15.3 trillion in 2018, which was later estimated at IDR 13.7 trillion by the end of September 2019 following a completed audit (Lisa & Halim, 2023). This case underscores the critical need for a robust financial statement integrity model, incorporating moderation and mediation factors to enhance transparency and compliance. Additionally, it reinforces the importance of regulatory oversight, corporate governance, and auditor independence in mitigating financial misstatements and strengthening public trust in financial reporting.

The predicament contributing to the highlighted controversies is attributed to the suboptimal quality of audits conducted by PA, casting a shadow of doubt on the integrity of the scrutinized financial statements. The ramifications of such inadequacies permeate the financial landscape, breeding uncertainty and undermining confidence in the veracity of the reported financial data. A crucial aspect in this scenario pertains to the pivotal role played by the caliber of audits, a component that, when executed with utmost proficiency, serves as a safeguard against financial misstatements.

An exemplary audit by a PA possesses the capacity to unearth and rectify significant inaccuracies within financial accounts, thereby fortifying the reliability of the audited information. Furthermore, it plays a pivotal role in narrowing the knowledge gap between principals and agents, enhancing transparency, and fostering trust in the financial reporting process. The significance of these outcomes is underscored by Dang et al. (2024), who emphasize that a robust audit not only

ensures the accuracy of financial information but also acts as a guardian of stakeholder interests. In essence, the standard of audits serves as a crucial component in safeguarding the integrity of financial reporting, exerting a significant impact on the dynamics between various stakeholders and the entities subject to audit scrutiny.

Through his research, DeAngelo (2020) demonstrates that audit quality is a combination of two possibilities: the auditor is competent in detecting or finding violations and material misstatements in the client's financial statements, and the auditor is independent in reporting these findings. Both of these possibilities are necessary for audit quality to be achieved. The audit quality model that was proposed by DeAngelo (2015) has been examined in a number of research, like the ones that were carried out by Iryani (2017), and Amalia et al. (2019). Throughout the course of their individual study initiatives, it has been established that independence has a substantial impact on audit evaluation quality. A number of studies, including Kabiru and Abdullahi (2020), Himawan et al. (2019), and Kertarajasa et al. (2019), demonstrate that the presence of independence does not have any impact on the quality of audits. In the meantime, Babatolu et al. (2016) demonstrate that independence has a detrimental impact on the quality of audits undertaken.

The model that DeAngelo (2015) had built served as the foundation for the development of a new model that was established. With the understanding that the Board of Commissioners is responsible for providing assistance to the audit committee in the performance of the monitoring function, the competency variable was changed to the audit committee variable. This was done in consideration of the fact that the audit committee is responsible for assisting. This process includes evaluating the effectiveness of the internal audit function, the quality of the financial statements, and the internal control system of the company (Peraturan Otoritas Jasa Keuangan No. 55/Pojk.04/2015). All of these aspects are examined as part of this process.

Both the internal and exterior environments are subject to the monitoring mechanism. Both the Board of Commissioners and the Audit Committee are responsible for carrying out the necessary internal monitoring. For the purpose of controlling the opportunistic conduct of management in the preparation of financial statements, this monitoring is anticipated to be effective. However, in the meanwhile, an independent PA is involved in the process of carrying out external monitoring. A mechanism of corporate governance that ensures the integrity of the process of financial reporting is the audit process. This mechanism is one of the mechanisms. It is the responsibility of the PA function to guarantee that the presented financial information is in accordance with accounting standards. Through coordination with the internal audit function and audit committee, PA has the potential to improve the efficiency of internal control effectively (Bardhan et al., 2023).

The findings of studies that have been conducted on the audit committee, such as those conducted by Anafiah and his colleagues (2017), indicate that the audit committee has an effect on the quality of the audit. On the other side, Adeyemi and Fagbemi (2020), all indicate that the audit committee does not have any impact on the quality of the audit. There are several of these research that have outcomes that are inconsistent or contradictory, both in terms of their relevance and their direction. According to Jogiyanto (2019), if the findings of earlier studies are

contradictory, both in terms of significance and direction, then it is possible that other variables are responsible for moderating the occurrence. In light of this, the research that was conducted included the organizational commitment variable as a moderating variable in the link that exists between audit committees, independence, and audit quality. In addition, the findings of this study establish audit quality as a variable that acts as a mediator between the impact of audit committees and independence on the integrity of financial statements.

Individual judgments of loyalty, determination, and expectations that are formed by certain systems, beliefs, or norms are referred to as organizational commitment, which is a critical moderating factor (Arifin et al., 2021). By doing so, individuals are prompted to stick to the procedures that have been set, which guarantees that they will carry out their responsibilities with a higher level of success. According to Greenberg and Baron (2023), organizational commitment is a reflection of the degree to which an individual identifies with the organization and desires to continue being a part of the organization. Auditors who have higher degrees of organizational commitment demonstrate greater independence in resolving conflicts across responsibilities, keeping their attention on their work, and following professional standards and procedures in a more stringent manner. The effectiveness of the audit is improved as a result of this increased commitment. Drawing from Allport's (2016) attitude theory, which is articulated in Azwar, the audit committee and independence make it easier for organizations to modulate their commitment (2024). A prospective inclination to respond in a specific manner when confronted with a stimuli that requires a response is what attitude is supposed to convey, according to the idea. When it comes to this particular investigation, the stimulant is the commitment of the organization. Additionally, Azwar (2024) distinguishes attitude into three distinct components: cognitive, emotional, and conative characteristics.

The quality of the audit acts as a moderating variable, and it is widely acknowledged that a high-quality audit is one of the most critical factors that determines the credibility of financial statements (Saeed & Al-Abedi, 2020). In addition, a quality audit offers valuable information that can be utilized for the purpose of making economic decisions. In addition, it is emphasized that a quality audit has the potential to reduce the likelihood of conflicts of interest occurring between principals and agents, which in turn improves the dependability and integrity of financial statements (Jerry & Saidu, 2018). One of the most interesting aspects of this study is that it investigates the impacts of moderation and mediation within the context of developing a model for the integrity of financial statements. As a consequence of this, the fundamental interests of this investigation are twofold. In the first place, the objective is to create a model for the integrity of financial statements that takes into account the role of organizational commitment as a moderating element in the connection between the audit committee and independence and audit quality. In the second part of the research project, the objective is to analyze the role that audit quality plays as a moderating factor in the relationship between the audit committee and the integrity of financial statements.

RESEARCH METHODS

The population in this study consists of two categories: (1) banking companies listed on the Indonesia Stock Exchange (IDX), totaling forty entities, and (2) the forty public accountants responsible for auditing these banks. Using a saturation sampling technique, the study includes all forty banking companies and their respective auditors as the sample. The units of analysis are the financial statements of IDX-listed banking companies and the auditors conducting their financial audits.

Primary data collection was conducted through questionnaires distributed via Google Forms, focusing on variables such as organizational commitment, auditor independence, and audit quality. Meanwhile, secondary data, including audit committee characteristics and financial statement integrity, were obtained from company financial reports available on the IDX website (idx.co.id).

The variables in this study include (a) audit committee as an independent variable (X1) with indicators referring to Azim (2020), (b) auditor independence as an independent variable (X2) with indicators referring to Beattie et al. (2019), and Halim et al. (2021), (c) organizational commitment as a moderating variable (X3) with indicators referring to Smith & Hall (2016) and Halim et al. (2021), (d) audit quality as a mediating variable (Y1) with indicators referring to Gramling & Stoner (2025), Craswell et al. (2022a), and Halim et al. (2021), and (e) the integrity of the audit financial statements as an independent variable (Y2) with indicators referring to Hamdan et al. (2017).

The data analysis technique uses Partial Least Square (PLS). However, before being analyzed, tests were first carried out: validity, reliability, linearity, and goodness of fit model. A T-test was used to test the hypothesis.

RESULT AND DISCUSSION

Test Results of Validity, Reliability, Linearity, and Goodness of Fit Model

The p-value, obtained through the Pearson correlation validity test, is less than 0.05, confirming that the questionnaire items are valid. The reliability assessment using Cronbach's alpha produced values greater than 0.6, indicating that the questionnaire items are reliable. The curve fit method was employed to examine the linearity assumption, with all nine hypotheses showing linear model significance values below 0.05, confirming the model's linearity. The goodness-of-fit test, based on an R^2 value of 0.7712 (77.12% predictive relevance), suggests that the model explains 77.12% of the variance, while the remaining 22.88% is attributed to other variables and error terms. These findings support the robustness of the PLS model, which can effectively be used to test the hypotheses. Moreover, the statistical tests substantiate the significance of the relationships among the variables, reinforcing the mediating role of audit quality in financial statement integrity.

Hypothesis Testing Results

The results of hypothesis testing using PLS are presented in Table 1 below.

Table 1. Summary of Hypothesis Test Results Using PLS

Description	Coefficient <i>inner weight</i>	<i>p-value < alpha 5%</i>	<i>Hypothesis Summary (H)</i>
Y1 => Y2	0.526	0.041	H-1 accepted
X1 => Y1	1.412	0.028	H-2 accepted
X1 => Y2 (direct effect)	0.224	0.025	H-3 accepted
X1 => Y1 => Y2 (non-direct effect)	using the Sobel test		H-4 accepted
X2 => Y1	1.123	0.027	H-5 accepted
X2 => Y2 (direct effect)	0.333	0.043	H-6 accepted
X2 => Y1 => Y2 (non-direct effect)	using the Sobel test		H-7 accepted
X1*X3 => Y1	1.524	0.039	H-8 accepted
X2*X3 => Y1	1.635	0.034	H-9 accepted

Source: This research's primary data was processed by using PLS.

Based on Table 1, the moderating and mediating effects on the integrity of financial statements can be drawn, and the PLS results are as follows:

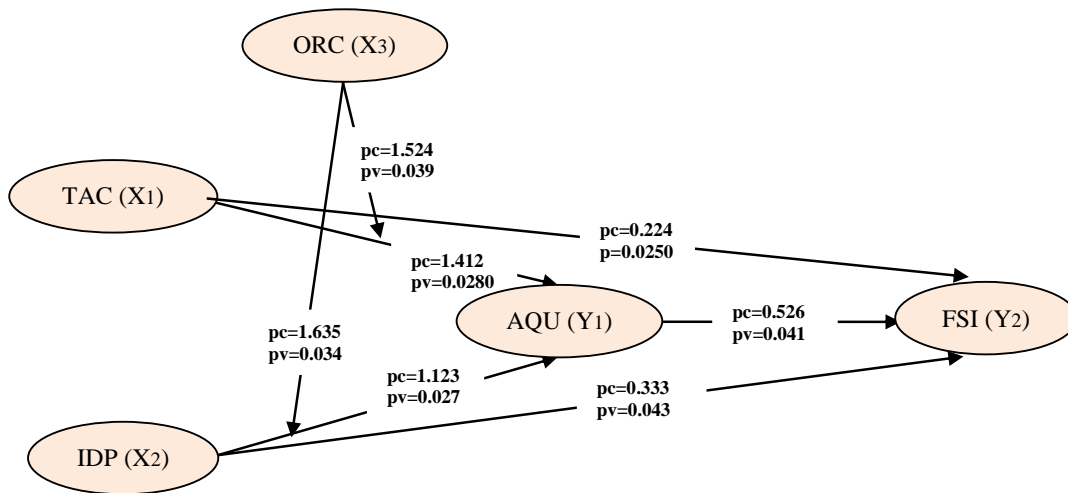


Figure 1. PLS Results of the Financial Statement Integrity Model

Description:

TAC	= The Audit Committee	FSI	= Financial Statement Integrity
IDP	= Independency	PC	= Path Coefficient
AQU	= Audit Quality	PV	= Probability Value
ORC	= Organizational Commitment		

The p-values for the indirect effects $X1 \Rightarrow Y1 \Rightarrow Y2$ and $X2 \Rightarrow Y1 \Rightarrow Y2$ are $0.000 < \alpha 5 \%$, as determined by the Sobel test. Therefore, it can be concluded that the impact of audit committees and independence on the integrity of financial statements can be enhanced through the mediating variable of audit quality. The inner weight coefficient $X1 * X3 \Rightarrow Y1$ is positive with a p-value of $0.039 < 0.05$, as shown in Table 1 and Figure 1. This implies that by acting as a moderating variable, organizational commitment can enhance the correlation between the audit committee and audit quality. With a p-value of 0.034, which is less than 0.05, the inner weight coefficient $X2 * X3 \Rightarrow Y1$ is found to be positive. This implies that the relationship between audit quality and independence can be strengthened by organizational commitment as a moderating variable.

Based on the results of hypothesis testing presented in Table 1 and Figure 1, the following picture of the findings of this study can be made:

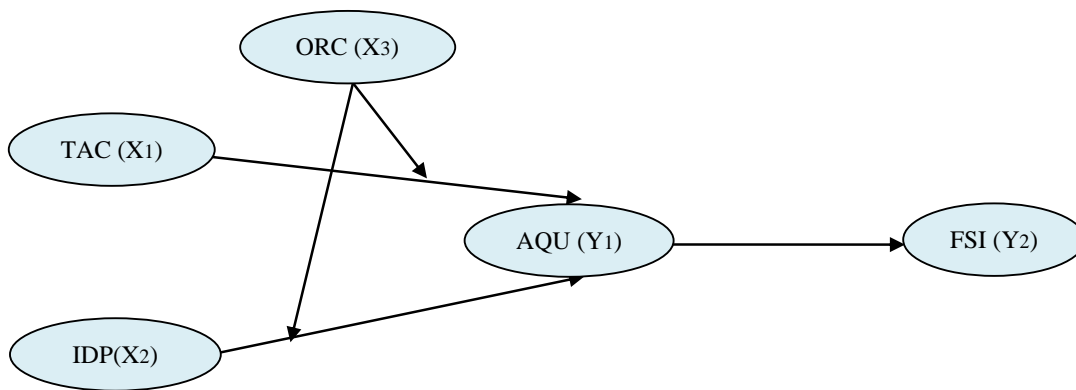


Figure 2. Financial Statement Integrity Model

According to the findings of this study, audit quality can act as a mediating variable, which means that it can improve the effect that audit committees and independence have on the integrity of accounting statements. It is advised that PA and PAF improve the quality of their audits by placing emphasis on industry-specific specialization in light of the audit quality indicators that were found in this study. When it comes to the assumption that audit quality is positively connected with the specialization of PAs in a particular industry, the findings that were reported provide more evidence in support of this argument. When it comes to improving the quality of audits, Cahan et al. (2024) claim that the participation of PAs who have the experience that is relevant to the industry is absolutely necessary. Because they have superior knowledge and make significant investments in industry-specific expertise, they are able to provide audit services of a higher quality. PAF is considered to have achieved the status of an industry specialist when the proportion of its clients exceeds twenty percent of the overall clientele, as stated by Gramling and Stone (2025) and Craswell and colleagues (2022a). When it comes to grasping and improving the quality of audits carried out by the PAF, industry specialization is a relevant measure that should be considered.

According to Mayhew and Wilkins (2022b) strongly advocate for specialization as a fundamental requirement for both Public Accountants (PA) and Public Audit Firms (PAF). In the pursuit of a competitive edge, PAFs must strategically differentiate themselves by delivering high-quality services that prove challenging for other PAFs to replicate. Through a dedicated emphasis on differentiation, PAFs can systematically carve out opportunities to tailor their services to the unique needs of their clientele. It is imperative for PAFs to provide services distinguished by their uniqueness, not easily replicated or imitated by industry peers. The core focus of differentiation should center primarily around client-specific characteristics and various service types, encompassing aspects such as size, segmentation, industry participation, legal requisites, and financial capacities.

According to Mayhew and Wilkins (2022b) underscore the significance of client industry involvement as a critical factor in discerning and addressing specific client requirements. The ability of PAFs to adeptly implement differentiation strategies across numerous enterprises sharing similar features underscores the paramount importance of industry specialization. Foreseeably, industry specialization is anticipated not only to enhance PAF sales but also to serve as a catalyst for elevated market standing. Research examining industry-specific personal assistants sheds light on their remuneration, indicating that they command higher salaries compared to their non-specialized counterparts (Kharuddin & Basioudis, 2022a). Hogan and Jeter (2018), leveraging insights from industry professionals, conducted a meticulous analysis of PAF market shares, revealing a noteworthy correlation between heightened audit concentration among industry professionals and the augmentation of market shares.

Moreover, Ferguson et al. (2022c) furnish compelling evidence that market perception and appreciation of industry-specific PAFs are inherently tied to industry-leading firms. This corroborates the conclusions drawn by Choi et al. (2019), who assert the dominance of the industry specialist market within the broader audit landscape. The consistency between this information and their findings serves to reinforce the pivotal role played by industry specialization in shaping the dynamics of the audit market. This expanded exploration affirms the fundamental tenets of the initial argument, underlining the transformative potential of specialization for both PAs and PAFs within the competitive landscape of the auditing profession.

According to Neri and Russo (2022), attaining a thorough understanding of audit quality and its regulation for ensuring financial statement integrity requires careful consideration by regulators and academic researchers. An essential aspect to incorporate into this understanding is the pivotal role played by stakeholders in establishing connections with audit quality. This extends beyond the linear relationship of input => process => output and delves into the broader spectrum of audit quality drivers, some of which are not under the direct control of Public Audit Firms (PAF). These drivers can be effectively managed, exerting a positive influence on audit quality.

The inputs influencing the auditing process are multifaceted, encompassing various factors. Within the realm of the audit process and quality control methodologies, the prevailing culture within a Public Accounting Firm (PAF) is of paramount importance. This encompasses the values, ethics, attitudes, as well as elements of time, knowledge, and skills brought to bear on the auditing

process. Rigorous audit methods and adherence to quality control protocols are mandated for auditors to ensure compliance with all relevant laws, rules, and standards.

The output, or the culmination of this intricate process, acknowledges the dynamic aspect of stakeholder influence on the outcome. Regulatory bodies, for instance, possess the ability to impact the final results. On the contrary, the output, manifested in the form of the auditor's report, tends to exhibit a more standardized nature when viewed by certain stakeholders such as investors. In conclusion, a nuanced understanding of audit quality necessitates delving into the multifaceted relationships between inputs, processes, and outputs. Stakeholder dynamics, both direct and indirect, play a crucial role in shaping the outcome of the auditing process, emphasizing the need for comprehensive regulatory and academic consideration.

The outcomes of this research provide compelling insights into the critical role played by organizational commitment as a moderating variable. Its significant impact is evident in the enhancement of both the efficiency and independence of the audit committee, thereby contributing positively to the regulation of audit quality. This, in turn, results in a notable improvement in the integrity of financial statements. Consequently, organizations operating within sectors like finance and entities such as the Public Administration Fund (PAF) are strongly encouraged to foster heightened levels of organizational commitment within their organizational frameworks proactively. By doing so, these entities can facilitate the cultivation of enduring relationships and effectively mitigate the likelihood of prematurely terminating connections with the involved parties.

Barner's (2016) insightful framework provides a nuanced understanding of the indicators used to assess an individual's commitment to a relationship, namely, satisfaction and participation. The first indicator involves evaluating the extent to which a relationship fulfills fundamental needs and delivers valuable outcomes. The second indicator delves into the qualitative comparison of alternatives, assessing achievements against the ideal expectations of the partner. Both of these satisfaction factors exert a significant influence on the level of commitment within a relationship. Furthermore, the depth of commitment is intricately linked to the level of investment, which can manifest in terms of time, emotional energy, or personal sacrifice. A person's reluctance to terminate a relationship often stems from the perceived investment in it, reflecting a profound sense of connection. This understanding becomes a driving force for individuals to persist in maintaining and nurturing the relationship, driven by the realization that terminating the connection would equate to a wasteful dissipation of the time and effort invested.

In summary, organizational commitment emerges as a pivotal factor fortifying the audit committee's effectiveness and independence, thereby contributing to the regulation of audit quality and the subsequent improvement in financial statement integrity. Barner's framework enhances our comprehension of the nuanced dynamics within relationships, emphasizing the crucial role played by satisfaction, participation, and investment in sustaining meaningful connections.

CONCLUSION

The study's findings emphasize the development of a model that enhances financial

statement integrity, with organizational commitment serving as a crucial moderator, reinforcing the relationship between audit committee independence and audit quality to increase the likelihood of positive audit outcomes. A strong positive correlation is evident between the audit committee's independence and audit quality, with this connection becoming more pronounced as organizational commitment strengthens, while audit quality functions as a mediator, further amplifying the impact of audit committee independence on financial statement accuracy. To enhance audit quality, regulatory bodies and policymakers should implement measures that strengthen audit committee independence, such as stricter governance requirements and mandatory training programs for committee members. The study also highlights the essential role of Public Audit Firms (PAFs) in maintaining high-quality audits by specializing in specific industries, enabling them to develop in-depth expertise, address industry-specific challenges, and ensure more rigorous financial oversight; however, implementing such specialization requires overcoming barriers such as the high costs of industry-specific training, resistance to change, and the need for continuous regulatory adaptation. PAFs should focus on differentiation by offering tailored audit services that align with industry needs, positioning themselves as leaders in their respective fields, while policymakers could introduce incentives for PAFs that develop specialized audit frameworks, encouraging firms to deepen their industry expertise while ensuring compliance with evolving regulations. Furthermore, the study underscores the importance of fostering organizational commitment within both banking institutions and Public Audit Firms, as McShane and Glinow (2016) emphasize that organizational commitment is a key moderator directly influencing audit effectiveness. Building this commitment requires targeted policies prioritizing employee well-being, fairness, and ethical values, where institutions should implement structured support systems, enforce transparent policies, and promote a culture of accountability to strengthen commitment and trust within their organizations. By instilling shared values and encouraging employee involvement, organizations can enhance overall audit quality and contribute to the integrity of financial reporting, while future research should explore the practical challenges of implementing these recommendations to ensure that proposed policies effectively translate into real-world improvements in audit quality and financial transparency.

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