

# FIRM SIZE, PROFITABILITY, AUDIT DELAY ON AUDITOR SWITCHING

Helen Weilia Tantri<sup>1</sup>, Nia Yuniarsih<sup>2\*</sup>

<sup>1</sup> Accountancy Department, Universitas Katolik Darma Cendika, Surabaya, Indonesia

<sup>2</sup> Accountancy Department, Universitas Katolik Darma Cendika, Surabaya, Indonesia

\*Corresponding Author: [nia.yuniarsih@ukdc.ac.id](mailto:nia.yuniarsih@ukdc.ac.id)

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**Abstract:** This study aims to examine the effect of firm size, profitability, audit delay on auditor switching in manufacturing companies on the Indonesian Stock Exchange in 2021-2022. This study uses a quantitative descriptive method, using secondary data and documentation study collection techniques. The sampling technique was purposive sampling method which resulted in a sample of 55 companies. Data analysis using logistic regression. The test results show that firm size has no significant effect on auditor switching, profitability has a significant effect on auditor switching and audit delay has a significant effect on auditor switching. Suggestions for further research to have an increased research period and use primary data for more accurate research results.

**Keywords:** Firm Size, Profitability, Audit Delay, Auditor Switching

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## 1. Introduction

Financial reports have an important role in measuring and assessing the performance of a firm as well as a form of corporate accountability that can be used to provide information to external parties. In presenting financial statements, an independent auditor is needed. Each auditor is required to provide guaranteed, quality, and reliable information. Therefore, an auditor is required to make regular auditor changes. The independence of public accountants is influenced by the length of the relationship that exists in accordance with Financial Accounting Standards. Reduced auditor independence occurs due to the length of the relationship that is built, the more likely it is to create closeness between the public accountant and the firm's clients. Indonesia is one of the countries that creates mandatory auditor switching regulations. The government stipulates the Regulation of the Minister of Finance of the Republic of Indonesia Number 17/PMK.01/2008 (amendment to the Decree of the Minister of Finance Number 359/KMK.06/2003). The regulation contains the provision of general audit services that can be carried out by a Public Accounting Firm which becomes 6 (six) consecutive financial years and by a public accountant 3 (three) consecutive years (Article 3 paragraph 1). Then the Public Accounting Firm and public accountant can re-audit the client firm's financial statements after 1 (one) fiscal year of not providing audit services for the same client's financial statements (Article 3 paragraphs 2 and 3). Then the regulation was updated to Government Regulation Number 20 of 2015 in article 11 containing: the provision of audit services on historical financial information of an entity by a Public Accountant is limited to a maximum of 5 (five) consecutive financial years (paragraph 1). Public Accountants can provide audit

services on historical financial information to entities after 2 (two) consecutive years of not providing such services (paragraph 4).

Auditor switching is a policy carried out by firm management by terminating the Public Accounting Firm (KAP) or Public Accountant (AP) contract and changing to a KAP or AP that has better quality and service (Ramadan et al., 2022). Auditor switching can be done compulsorily (mandatory) and voluntarily (voluntary). Mandatory auditor switching is carried out due to government regulations that require a firm to change auditors within a predetermined period of time. Voluntary auditor changes are made at the firm's own management decision before the deadline set by the government due to a certain time (Azlin & Taqwa, 2023: 758). Voluntary auditor changes can trigger suspicion by interested parties because the length of the engagement has been determined by the government.

The size of a large firm is considered to have a high level of complexity compared to a small firm. So most companies that have small tend to change auditors or look for large who are considered capable of making the firm more advanced (Sarumaha et al., 2020)

Another factor that can affect auditor switching is profitability. Profitability is the firm's ability to earn profits in a certain period, in previous studies profitability that affects auditor switching. Profitability can affect auditor switching, if the firm gets an increase in profitability then the firm is experiencing growth in the firm thus companies that are experiencing growth will tend to do auditor switching. In this study, the authors will conduct research on profitability with the measurement ratio using the sales profit margin generated by the firm. the greater the net profit margin, the more investors like the firm because it shows the firm gets good results exceeding the cost of goods sold. The greater the level of corporate profits generated, the firm can afford to hire a higher quality Public Accounting Firm (Nana, 2022).

Audit delay can usually result in companies losing potential investors because their financial reports are too late to be published to the capital market. Audit delay is the time required by the auditor to complete the audit report on the financial statements he audits starting from the closing date of the financial statements until the audit report is submitted and signed. According to Naili & Primasari (2020) audit delay has a significant effect on auditor switching. Researchers want to prove whether audit delay still affects auditor switching or not with different data and periods from previous researchers.

## **2. Literature Review**

### **Agency theory**

Agency theory describes agency relationships as relationships that arise because of a contract agreed with the principal to carry out tasks that are in the principal's interest (Jensen & Meckling, 1976). Due to the conflict between the two parties, it is necessary to have an independent party, namely an independent auditor who has a mediating role between the two parties.

### **Firm Size**

The size of the firm is a scale used in classifying the size of the firm. Large companies in this case are believed to be able to solve the financial problems they face compared to small companies. Large total assets in the firm indicate that the size of the firm is relatively large and small total assets indicate that the size of the firm is relatively small, a large firm size will have a high level of complexity compared to a small firm. This causes to prefer companies that are classified as large to audit because they are considered to have independent auditor services that are capable and skilled in examining financial statements.

Firm size is the size of a firm which will be expressed in total assets, sales and market capitalization. Large assets will get more capital to be invested, so that there will be more sales

and turnover of money invested later. The more and the greater the market capitalization, the more likely the firm will be known to the public. The size and size of the firm is measured using total assets (Sanulika, 2018)

### **Profitability**

Profitability is a ratio used to measure the firm's ability to generate profits from its normal business activities and aims to measure the level of management effectiveness in carrying out firm operations. In this measurement, the level of profitability of the firm assumes that sales are the main activity of the firm and the profit generated is the most important factor in the development of the firm. The use of profitability ratios for companies is believed to be important in terms of determining the firm's future actions. Profitability ratios for 4 parties related to the firm, namely to measure the firm's ability to generate profits during a certain period, assess the firm's profit position in the previous year with the current year, assess profit development, measure the amount of net profit from each rupiah of funds in total assets, measure the amount of net lab to be generated, measure gross profit margin on net sales, measure operating profit margin on net sales, and measure net profit margin on net sales (Arsih & Anisykurlillah, 2015)

### **Audit Delay**

Audit delay is the number of days required by an auditor to produce an audit report from the closing date of the firm's financial statements (December 31) until the signing of the audit report. The complexity of the audit process affects the length of the audit delay. audit delay is the length of time to complete the audit process which is calculated from the closing date of the financial year until the audit report is signed by the auditor. The level of complexity of the audit process affects the length of audit delay. The higher the level of complexity of the audit process, the more time it will take to audit the parent firm and its subsidiaries. Regulations regarding the reporting and disclosure of financial statement information are regulated in the Peraturan Orientasi Jasa Keuangan Number 29 / POJK.04 / 2016 which states that the audited annual financial statements must be submitted to OJK no later than the end of the fourth month after the closing date of the firm's financial year (Adelany & Harlyn L. Siagian, 2022)

### **Auditor Switching**

Auditor switching is behavior carried out by companies to switch Public Accounting Firms either mandatory or voluntary (Voluntary). In Indonesia, the regulation governing auditor switching is Regulation of the Minister of Finance of the Republic of Indonesia Number 17 / PMK.01 / 2008 article 3 concerning "Public Accountant Services" regarding the provision of general audit services for the financial statements of an entity that can be carried out by a Public Accounting Firm for a maximum of 6 consecutive financial years (article 3 paragraph 1) and then a maximum of 3 consecutive years. Public Accounting Firms and Public Accountants can re-accept audit assignments for clients after 1 (one) fiscal year of not providing general audit services for the same client's financial statements (article 3 paragraph 2 and 3).

Auditor Switching is a change of auditors or KAP carried out by the firm. The period of engagement between the auditor and the client can cause limitations on the period of engagement so that auditor switching can occur. Auditors have the aim of providing an audit opinion on the fairness of the financial statements so that outsiders can prove the validity of the financial statements. Companies that do not get an unqualified audit opinion are likely to look for a new auditor and make a change of auditors who can later provide an auditor opinion that is expected to be even better than the previous audit opinion (Anggadi & Triyanto, 2022) There are 2 types of Auditor Switching methods, namely mandatory and voluntary. Mandatory Auditor Switching can occur due to government regulations that require companies to change

KAP and Auditors according to a predetermined time period. Meanwhile, voluntary Auditor Switching occurs voluntarily or before the specified time period. There are many factors that can cause changes in KAP and auditors, such as the absence of regulations that limit companies to replace before the time period, or can come from auditors who resign or from the client having a decision to dismiss the auditor.

### **Research hypothesis**

H1 : Does Firm Size affect auditor Switching ?

H2 : Does Profitability affect auditor switching ?

H3 : Does Audit delay affect auditor switching ?

### **3. Method**

The population used in this study is the manufacturing industry that has been listed on the Indonesia Stock Exchange (IDX) in 2021-2022. The sampling technique in purposive sampling was used in this study by using criteria in determining the sample with certain considerations. In this study, the number of samples that met the criteria amounted to 55 companies, researchers used several criteria in taking research samples, including the following:

- a) Manufacturing companies listed on the Indonesia Stock Exchange continuously during the study period, namely in 2021-2022.
- b) Manufacturing companies that do not present financial reports using the rupiah currency for the 2021-2022 period.
- c) Manufacturing companies that reported losses during 2021-2022.
- d) Manufacturing companies that IPO during the period 2021-2022

### **Operational definition**

#### **Firm size**

Firm size is a value that indicates the size of a firm (Sarumaha et al., 2020). Firm size in this study is measured using the natural logarithm value with the formula:

$$\text{Firm Size} = \text{Ln} (\text{Total Asset})$$

#### **Profitability**

Profitability is a ratio used to measure the level of efficiency in utilizing the firm's resources. This ratio can also provide a measure of the level of effectiveness of firm management which can be shown from the profit earned from sales or from equity (Sanulika, 2018).

$$\text{ROE} = \text{profit for the year} / \text{Equity}$$

#### **Audit Delay**

The audit delay variable is the length of time for audit completion which is calculated from the closing date of the financial year until the audit report is issued and signed by the auditor. This variable is measured quantitatively by calculating the difference in the number of days between the issuance of the financial statements (December 31) and the date of issuance of the audit report (Santos & Yanti, 2021). The calculation of the difference is done with the following formula:

$$\text{Audit Delay} = \text{Audit Report Issue Date} - \text{Financial Statement Issue Date}$$

#### **Auditor Switching.**

In this study, researchers used Permenkeu No.17 / PMK.01 / 2008 concerning public accounting services where in these regulations changes in public accounting firms in

companies can be assessed by looking at the length of the audit engagement. Companies can carry out audit engagements with public accounting firms for 6 (six) financial years continuously and must change their public accounting firm if there has been an audit engagement for 6 (six) financial years continuously. Researchers use a dummy variable proxy to measure Auditor Switching. If the firm does not carry out a change in public accounting firm (auditor switching) during the monitoring year, the firm will be given a value of 0. Meanwhile, if the firm changes the public accounting firm (auditor switching) during the monitoring year, the firm will be given a value of 1 (Naili & Primasari, 2020)

## 4. Result and Discussion

### Assessing the overall model

The statistic uses the Likelihood function. The Likelihood L of the model is the model probability that the hypothesized model describes the input data. To test the hypothesized model fit with the data and alternatives, L is transformed into  $-2\text{LogL}$ .

**Table 1. Likelihood L Early**

Step	-2 Log Likelihood	Coefficient Constant
0	32.564	0.000

**Table 2. Likelihood L End**

Step	-2 Log Likelihood	Cox & Snell R Square	Nagelkerke R Square
1	11.756	0,645	0.803

**Table 3. Omnibus Test of Model Coefficient**

Step 1		Chi-square	df	Sig
		Step	20.808	4
	Block	20.808	4	0.000
	Modell	20.808	4	0.000

Based on the results table 1 output likelihood L gives a number 15.796 which is not significant at 5% alpha, so table 2 output likelihood L gives a number 11.756. The final  $-2LL$  value (step 1) decreased by 20.808 which can be seen in table 3, then the decrease in  $-2LL$  value gives the conclusion that the regression model is better value gives the conclusion that the regression model is better or the hypothesized model fits the data.

### Hosmer and Lemeshow Test

Testing the feasibility of this logistic regression model is assessed using Hosmer and Lemeshow's Goodness of Fit Test as measured by the chi-square value. This model is used to test the null hypothesis that the empirical data fits or fits the model (there is no difference between the model and the data so that the model can be said to be fit). The significance value listed is then compared with the significance level ( $\alpha$ ) of 5% (Ghozali, 2018). If the value of Hosmer and Lemeshow's Goodness of Fit Test is equal to or less than 0.05, there is a significance difference between models so that the goodness of fit of the model test is not good because it cannot predict the value of the observation, and vice versa.

**Table 4. Hosmer and Lemeshow Test**

Step	Chi-square	df	Sig.
1	9,803	3	0,290

Sources: SPSS 25

Based on the table 4, it can be seen that the statistical value of the Hosmer and Lemeshow's Goodness of Fit Test as measured by the Chi Square value is 9.803 with a significance value of 0.290. The significance value is greater than 0.05, which means that the regression model is able to predict the value of the observation. These results also show that the model is said to fit with the observation data and the model is acceptable because it matches the observation data so that the hypothesis testing model can be carried out or this model can be used for further analysis.

### Coefficient of determination test

The Nagelkerke R. Square test on Tabel 2, which is the coefficient of determination test is a test used to explain how much variability the independent variables are able to explain the variability of the dependent variable. The coefficient of determination in binary logistic regression is indicated by the Nagelkerke R. Square value. This test ensures that the Nagelkerke R. Square value varies from 0 (zero) to 1 (one), where the Nagelkerke R<sup>2</sup> value can be interpreted like the R<sup>2</sup> value in multiple regression. Based on the results table 3, the magnitude of the coefficient of determination is shown in the form of the Nagelkerke R. Square value, where the coefficient of determination is 0.803 or 80,3%. This means that the variability of the dependent variable (auditor switching) can be explained by the independent variables in this study is 80.3%. While the remaining 19,7% is explained by other independent variables outside the variables used in this research model.

### Classification Matrix

This test is used to ensure the strength of the observations from the logistic regression model that allows for auditor changes made by the firm.

**Table 5. Classification Table**

		Predicted		
		Firm		Percentage
Observed		.00	1.00	Correct
Step 1	Auditor Switching	0.00	71	100%
		1.00	39	0%
Overall				35.45%
Percentage				

Table 5 above shows the predictive power of the regression model to predict the possibility of auditor switching and non-auditor switching. From the regression model results it can be seen that there are 39 samples that do auditor switching and 71 samples that do not do auditor switching. This means that with the proposed regression model there are 71 samples that do not do auditor switching and of the 110 samples, there are 71 samples that are correctly predicted not to do auditor switching, so the predictive power of samples that do not do auditor switching is 100%. The accuracy of the prediction of the entire regression model used for companies that do auditor switching and companies that do not do auditor switching is 35.45%.

### Logistic Regression Model Equation

Parameter estimation of the model can be seen through the regression coefficient. The regression coefficient of each variable tested shows the form of relationship between one variable and another. Hypothesis testing in this study is to examine the effect of financial distress, audit delay, and auditor reputation variables on the dependent variable auditor switching using binary logistic regression.

**Table 6. Estimated Parameters**

		B	S.E.	Wald	df	Sig.	Exp(B)
Step 1	FS	2.311	3.573	1.874	1	.178	23.457
	ROA	1.342	1.451	5.334	1	.012	4.520
	AD	0.987	0.859	7.875	1	.002	2.008
	Constant	0.458	1.223	5.764	1	.021	1.097

The table above shows the results of hypothesis testing using binary logistic regression at a significance level of 0.05 (5%). Based on the results of logistic regression testing, the binary logistic regression equation can be obtained as follows:

$$\text{LN} = \frac{\text{SWITCH}}{1-\text{SWITCH}} = a + b_1 \text{FS} + b_2 \text{ROA} + b_3 \text{AD} + e$$

$$\text{SWITCH} = 0.458 + 2.311 \text{FS} + 1.342 \text{ROA} + 0.987 \text{AD} + e$$

Table 6 also shows the results of parameter estimation testing and its interpretation as seen from the regression coefficient value and significance for each independent variable with a significance level of 0.05 which is used to answer the following hypothesis:

### **Firm Size has no significant effect on Auditor Switching**

The firm size variable has no influence on auditor switching. This study shows that the size of a firm does not make consideration for auditor switching. These results reject the hypothesis that the tendency of large companies to do auditor switching is smaller than that of small companies. Companies whose size is large or small choose auditors according to the size of the firm. Because when the firm is satisfied with the auditor's performance, it tends to retain the auditor. The results of this study are consistent with research conducted Sinaga et al., (2021) ; Arsih & Anisykurlillah (2015) which proves that firm size has no effect on auditor switching.

### **Profitability has a significant effect on Auditor Switching**

Profitability is proven to have a positive and significant effect on auditor switching, namely based on the and p-value 0.012 (<0.05). The higher the profitability owned by the firm, the greater the tendency of the firm to do auditor switching. Auditor switching will be greater, and vice versa. This research is in line with Sanulika (2018), that if profitability is higher, it will be more effective in managing firm assets and showing that the firm is getting better. If the profitability of the firm is higher, the firm will hire a more qualified auditor to improve the quality of the financial statements. However, this research is not in line with the results of research conducted by where this study produces a statement that profitability has no effect on auditor switching. This is because when profitability goes up or down it is not the main reason for companies to do auditor switching. But the results of this study are inconsistent with research conducted by Sinaga et al., (2021) which proves that firm size affects auditor switching.

### **Audit Delay has a significant effect on Auditor Switching.**

The audit delay variable as measured by looking at the number of days from the firm's closing date on December 31 to the date the audit report has been submitted shows that the significance value of 0.002 is smaller than 0.05. This study proves that the audit delay variable has a significant effect on auditor switching. Audit delay is calculated from the length of time required by the auditor in completing the audit activities starting from the closing of the book until the signing of the annual financial statements of the firm being audited, when the firm is not on time or takes a long time to publish the firm's financial statements, it will cause questions for investors and investors. firm is not right or takes a long time to publish the firm's financial

statements will cause questions for investors and make investors suspicious of manipulation by the firm. make investors suspicious of manipulation by the firm. Therefore the firm will improve In terms of changing a more competent auditor so that the publication of the firm's annual financial statements is on time. Based on the test results, this study is in line with the results of research conducted by Anggadi & Triyanto (2022) ; Santos & Yanti (2021) state that audit delay has a positive effect on auditor switching.

## 5. Conclusions

This study aims to examine the influence of firm size, profitability and auditor switching variables. Based on the research that has been done, it can be proven that the profitability and audit delay variables have a significant influence on auditor switching. While the firm size variable is proven to have no influence on auditor switching.

This study has limitations that can affect the research results, namely research data is only limited to secondary data downloaded through online sites so that the results of this study are not accurate enough. Therefore, researchers suggest that future researchers use primary data as research data. Primary data will provide more accurate results regarding the factors that influence companies to make voluntary auditor changes. This is because researchers will get information directly.

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