International Journal of Social Science (IJSS)
Vol.3 Issue.2 August 2023, pp: 249-258
ISSN: 2798-3463 (Printed) | 2798-4079 (Online)
DOI: https://doi.org/10.53625/ijss.v3i2.63130

THE INFLUENCE OF CORPORATE GOVERNANCE AND AUDIT QUALITY ON TRUSTED FINANCIAL STATEMENTS THROUGH FINANCIAL DISTRESS IN BUMN HOLDINGS IN INDONESIA

By
Indra Setiawan[1*], Tri Widyastuti[2], Derriawan[3], Amilin[4], Zulkifli[5]
[1,3,5]Pancasila University
[2]Bhayangkara Jakarta Raya University
[4]Syarif Hidayatullah State Islamic University Jakarta
Email: [1]ind_setiawan78@yahoo.com

Article Info
Article history:
Received May 22, 2023
Revised June 20, 2023
Accepted July 21, 2023

Keywords:
BUMN, Trusted Financial Reports, Corporate Governance, Audit Quality, Financial Distress

ABSTRACT
This study aims to analyze the effect of corporate governance and audit quality on trusted financial reports through financial distress. The analytical tool used in this study is the Structual Equation Model (SEM) with Partial Least Square (PLS), while the sample used in this study is 68 BUMN Holding business units in Indonesia. The research respondents were auditors who had experience in auditing BUMN Holdings. The results of the study show that corporate governance has a positive effect in encouraging the creation of trusted financial reports. Corporate governance has no significant effect in encouraging the creation of BUMN Holding financial distress in Indonesia. Audit quality has a positive effect in encouraging the creation of trusted financial reports. Audit quality has a positive effect on financial distress. Financial distress has a negative effect on trusted financial reports. This research provides insight into the field of financial risk management research. The insignificant relationship between corporate governance and financial distress is an important finding, because most previous studies have concluded that corporate governance variables have a direct effect on financial distress, both positive and negative. Given the complexity of the relationship between corporate governance and financial distress, more in-depth further research can be conducted to explain in more detail why this relationship is not significant. Qualitative approaches such as case studies, interviews or comparative analysis can be used to gain deeper insight into the context and mechanisms underlying these findings

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Corresponding Author:
Indra Setiawan
Pancasila University
Email: ind_setiawan78@yahoo.com

1. INTRODUCTION

The government is currently carrying out a strategic step in the form of merging BUMNs in the same sector to become several holding companies. The thinking underlying the formation of this BUMN holding is to optimize management, effectiveness and cost efficiency. According to Permana et al. (2020) through grouping SOEs into holdings, it is possible to form a high market value creation. The formation of a holding can also create BUMN synergy for each of the same sectors. In the context of increasing the profitability of BUMN, this can be achieved through company synergy and efficiency (Renstra Deputy ELKP Ministry of BUMN, 2015-2019). To increase public trust in the management of BUMN, one of the issues that need to be investigated is related to financial reports. For the past one year, the public has been excited about issues related to the financial reports of BUMNs, such as Garuda Indonesia,

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Jiwasraya and Asabri. The corporate scandal has created a crisis of confidence in financial reports and the audit process and in the accounting profession (Demetriades & Owusu-Agyei, 2021).

In the last two decades, accounting and financial reporting scandals have continued to be revealed to the public, especially since the global financial crisis and the disclosure of accounting scandals at several large companies in the United States, which were previously considered credible companies with good performance and good governance. The peak of the crisis of trust occurred in large world-class companies that were known to be innovative with fast growth, and had the title of managing the company efficiently and well, namely the Enron case in 2001-2002 (Khudhair et al., 2019; Monahan, 2012; Montesdeoca et al. ., 2019). **Although the international community has long pushed for the implementation of International Financial Reporting Standards (IFRS), based on the results of research conducted by Donelson et al. (2021); Moffitt (2018) and O'Leary, (2021) incidents of fraud and fraud against financial reports, continue to this day, and tend to increase from time to time**.

Likewise with the report submitted by the Association of Certified Fraud Examiners (ACFE) in its biennial report, public sector companies in the last two decades have always ranked second after private companies as institutions exposed to corporate scandals and fraud which have resulted in a reduction or even loss of public trust in financial reports. Even though the percentage does not show a significant amount, there are indications that there has been an increase from year to year until this research was conducted. These events in general have had an impact on reducing public trust in financial reports and audit-related functions (Kaawaase et al., 2021) and the audit process (Robert Knechel et al., 2013). As predicted by Whittington (2000) that accounting scandals that have an impact on reducing the trust of these financial statements will continue to occur in the future. Along with the development of digital technology, the borderless nation and the behavior of the millennial community and investors are developing very rapidly at present and in the future, which can increase public distrust of financial reporting in the future (Sailendra, 2019).

Likewise with financial distress, which is one thing that can explain healthy financial reports) or even experiencing bankruptcy. However, in reality many large companies in Indonesia have experienced bankruptcy or bankruptcy. In order to increase and to rebuild public trust in financial reports, especially in the newly formed BUMN Holding, research is needed that seeks to increase trust in financial reports by involving corporate governance, audit quality and of course financial distress. Based on the research that the author did, the Ministry of BUMN website does not provide complete information on all the BUMNs it manages. Even the audit report is now no longer provided. Some SOEs don't even have a website, or they have a website but don't provide any information. Based on international transparency data (2021), out of 116 BUMNs, 88 BUMNs publish annual reports, 23 BUMNs do not publish them. Out of 88 SOEs, 17 do not publish the latest annual reports and even 20 SOEs have no financial information at all (International transparency).

This research is the first step towards efforts to increase public confidence in the financial statements of the newly formed BUMN Holding. There has not been a single study that preceded this research that examined holding as a whole, because the holding process continues and the last SOE holding was successfully formed in October 2021. This research aims to answer questions especially those related to the influence of corporate governance and audit quality on trusted financial reports through financial distress.

2. LITERATURE REVIEW

2.1. Trusted Financial Report

Financial statements are a structured presentation of the financial position and financial performance of an entity (Dzomira, 2017). The trusted dimension of financial reports varies greatly depending on the research object (Sailendra, 2019). In this study it was constructed referring to the qualitative characteristics of the financial reporting framework (IAI, 2016). Using six elements of trust extracted based on existing literature consisting of (1) benevolence, (2) accountability, (3) credibility, (4) capability, (5) transparency, and (6) integrity (BAKATI) which corresponds to the qualitative characteristics financial reports (IAI, 2018).

2.2. *Corporate* Governance

Corporate governance is a system that controls and directs corporate governance to achieve balance and sustainability by taking into account and protecting shareholder interests based on applicable rules and norms (Soltanizadeh et al., 2016). However, according to the Institute of Directors (IodSA, 2018) the principles of good corporate governance can be assessed through five dimensions, namely Board effectiveness, Audit and risk/external accountability, Remuneration and awards, Shareholder relations, Stakeholder relations.

2.3. Audit Quality

Audit quality can be interpreted as whether or not an examination has been carried out by the auditor (Lisic et al., 2015). Referring to previous studies (Choi et al., 2010; Ismail et al., 2019; Knechel, 2016; Pham et al., 2017) this study proposes dimensions of audit quality consisting of reliability, responsiveness, assurance, and empathy.

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2.4. *Financial Distress*

Financial distress is a condition of a company's inability to fulfill its obligations (insolvency) (Vianez et al., 2020). Based on previous studies, this research refers to the dimensions proposed by Ratna and Marwati (2018), which consist of internal and external dimensions.

2.5. Research Hypothesis

2.5.1. The effect of corporate governance on financial report trustees

The results of Zhang's (2006) research state that the implementation of good corporate governance can positively improve company performance, because the decision-making process is carried out to be better. Likewise, research conducted by Ramadan & Abdallah (2019) states that corporate governance has a positive effect on financial performance, which can affect trusted financial reports. In line with the results of research conducted by Pintea et al. (2020) which states that corporate governance has a positive effect on financial reports which can improve trusted financial reports. Based on the description above, the first hypothesis is made as follows:

H_1: *corporate governance has a positive effect on trusted financial reports*.

2.5.2. Effect of audit quality on trusted financial reports

The results of research conducted by Sinaga & Sinaga (2019) state that audit quality by proxy of audit fees has a positive effect on financial reports which can affect trusted financial reports. Further research conducted by Farouk & Hassan (2014) proves that audit quality has a positive effect on the performance of financial reports which can affect trusted financial reports. These results are supported by the results of other studies conducted by Matoke & Omwenga (2016); Wang et al. (2014) that audit quality has a positive effect on performance and disclosure of financial statements as a way to increase trusted financial reports. Based on the description above, a second hypothesis is made, as follows:

H_2: Audit quality has a positive effect on trusted financial reports.

2.5.3. The effect of corporate governance on financial distress

Corporate Governance is needed to reduce agency problems between owners and managers and reduce the occurrence of information asymmetry and financial distress. In the corporate governance mechanism there is a board structure and ownership structure. The board of directors is the executor, decision maker, and manager of a company. According to agency theory, the larger the size of the Board of Directors will bring superiority in decision making (Permana et al., 2020). The greater the Managerial Ownership, the less likely the Financial Distress condition will be. If agents or management in a company own the company's shares, then decision making can harm the company and the possibility of Financial Distress will decrease.

H_3: *Corporate governance influences financial distress*

2.5.4. Effect of audit quality on Financial distress

There are inconsistent results in research between audit quality and financial distress. Research ever conducted by Indrasari et al. (2016) found that audit quality has an effect on financial distress, while Saraswati et al., (2020) found that audit quality has no effect on financial distress. Jombrik & Tamami (2021) found that financial distress is proven to have a positive influence on the acceptance of audit opinions. Meanwhile Elevendra & Helmayunita (2021) show that audit quality has a significant negative effect on financial distress. Meanwhile, Karina (2018) argues that audit quality has a significantly positive effect on financial distress. Based on the results of these studies, this study proposes a fourth hypothesis:

H_4: Audit quality affects financial distress

2.5.5. The effect of financial distress on trusted financial reports

The quality of financial reports greatly influences accountability, with good quality financial reports that will provide dedication to accountability or responsibility for the financial reports that are made which will affect the fairness of the financial information presented (Alsmairat et al., 2019). This opinion is also supported by Ardelean (2015); Berglund & Kang (2013); Dunstan (2017) which states that, the better the company's financial condition, the less likely it is to have high trust in financial reports. The company's financial condition is a condition that can be measured quantitatively to describe the state of the company. Based on the explanation above, the research hypothesis proposed is:

H_5: *Financial distress has an effect on trusted financial reports*

Based on the theoretical studies that have been presented and a review of the results of previous studies, the authors summarize the research hypothesis in the form of a hypothetical framework as follows:

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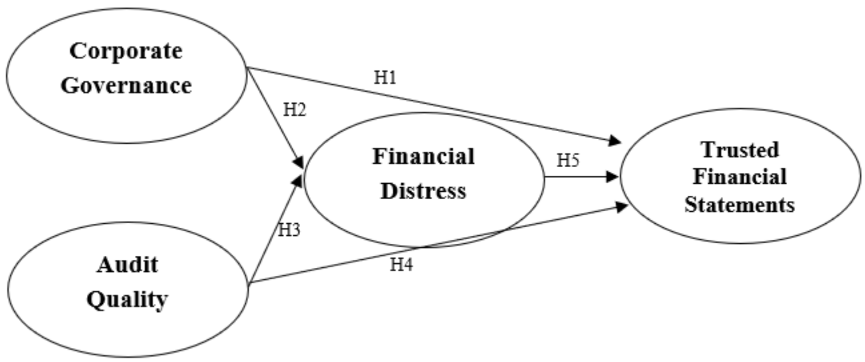

Figure 1. Research Hypothesis Framework

Based on the hypothetical framework as shown above, the following summarizes the hypotheses involved in this study:

H_1: Corporate governance has a positive effect on trusted financial reports.
H_2: Corporate governance influences financial distress.
H_3: Audit quality has a positive effect on trusted financial reports.
H_4: Audit quality affects financial distress.
H_5: Financial distress has an effect on trusted financial reports.

3. RESEARCH METHOD

This study analyzes the empirical phenomenon of trusted financial reports for state-owned enterprises that have become holding companies. There are 9 SOEs that have become holding companies. However, the last BUMN holding that was successfully formed was the tourism BUMN holding in October 2021. Therefore, it has not yet reached 1 year of age, so its financial reports cannot be trusted. Therefore, the object of research is 8 BUMN holding companies with 59 subsidiary companies, plus 8 parent companies, the total BUMN is 67 companies. The target of this research is accountants who follow the financial developments of BUMN Holding. According to data from the Indonesian Institute of Certified Public Accountants (IAPI), the number of public accountants who have a Certified Public Accountant (CPA) is 4,000 people, while those who do not have a CPA cannot be detected with certainty. So to determine the number of respondents, refer to expert opinion, for example, Ferdinand (2014) recommends that in quantitative research the appropriate number of samples is 100 people. Sekaran & Bougie (2016) propose a rule of thumb that for most studies, sample sizes range from 30 respondents to 500 respondents. Thus the number of 100 respondents deserves further analysis. This study used the Structural Equation Model (SEM) analysis technique with Partial Least Square (PLS). SEM with PLS analysis was carried out in three stages, namely outer model analysis, inner model analysis, and hypothesis testing.

4. RESULTS AND DISCUSSION

Based on the data collected, it is known that based on gender, the respondents consisted of 69.23% male while 33.77% female. Several studies have shown that there is an effect of gender on audit quality, while other studies have found that gender differences are not significant in this regard (Eriandani & Dewi, 2022). Meanwhile, based on education, the respondents consisted of 69.23% Bachelors, 23.08% Masters and 7.69% Doctoral. Education is an important factor in shaping the competence and knowledge of an auditor. Auditors with higher levels of education tend to have a deeper understanding of auditing theory, principles, and practice. They may have more extensive knowledge of the framework governing auditing practices, ethical standards, and relevant regulatory demands (Hidayat, 2019). A good education can also provide a solid foundation in terms of analytical abilities, communication skills, and broad business understanding (Andri & Ridwan, 2018). Based on the data collected, it is known that based on the age of the respondents consisted of <30 years 3.85%, 31-40 years 38.46%, 41-50 years 26.92% and > 40 years 3.85%. In practice, auditing firms often seek a combination of auditors with varying levels of experience and ages. An audit team consisting of auditors of all ages can benefit from a variety of perspectives, experience and skills.

4.1. Quantitative Research Results

4.1.1. Outer Model Analysis

There are three criteria in the use of data analysis techniques with SmartPLS to assess the outer model, namely Average Variance Extracted (AVE), Cronbach Alpha and Composite Reliability. Convergent validity of the measurement model with reflexive indicators is assessed based on the correlation between the item score/component score estimated by the SmartPLS3 Software. The following is a table of analysis of the outer model.

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According to Newsted, (1999) for the construct reliability test it was measured by composite reliability and Cronbach's alpha. A construct is declared reliable if it has a composite reliability value above 0.70 and Cronbach's alpha above 0.50. Meanwhile, the adequate average variance extracted (AVE) value to measure validity is 0.5 (Ghozali, 2011). The following table presents the average value of Construct reliability and Validity.

Table 2. The average value of Construct reliability and Validity

No	Criteria	Average	Standart	Result
1	*Composite Reliability*	0,837	>0,7	All aspects of the BUMN Holding outer model meet the standards
2	*Average Variance Extracted* (AVE)	0,541	>0,5	
3	*Cronbach Alpha*	0,754	>0,6	

Source: Processed by researchers (2023)

4.1.2. Inner Model Analysis

Evaluation of the inner model can be seen from several indicators which include; coefficient of determination (R2); Predictive Relevance (Q2); Goodness of Fit Index (GoF). The following is a calculation for each indicator.

1. Coefficient of Determination (R^2)
   The following shows the R2 output value of the smartPLS 3 software.

Table 3. R^2 Test Result

	R Square	R Square Adjusted
Financial distress	0,980	0,979
Trsuted Financial Report	0,680	0,670

Source: Output smartPLS 3

According to Newsted, (1999), the R square value must be above 0 (zero), if the value obtained is 0.19 to 0.33 it indicates a weak coefficient of determination, if the value obtained is 0.33 to 0.67 it indicates a coefficient of determination which is moderate, whereas if the value obtained is above 0.67 it indicates a strong coefficient of determination. So this research model is categorized as having a moderate variable relationship between corporate governance and financial distress; between corporate governance and Trusted financial reports; between audit quality and financial distress and between audit quality and Trusted financial reports. shows a strong relationship.

2. Predictive Relevance (Q^2)
   To calculate Q2, the formula can be used.
   Q^2 = 1-(1-$R1^2$) (1-$R2^2$)……(1-Rn^2)
   Q^2= 1-(1-0,980) (1-0,460)
   Q^2=0,99

This test was conducted to determine the predictive capability with the blinfolding procedure. According to Newsted, (1999), the value obtained must be greater than 0 (zero). If the value obtained is between 0.02 and 0.15, the model has little predictive capability. If the yag value is between 0.15 and 0.35 then the model has moderate predictive capability. And if the value obtained is above 0.35 then the model has great predictive capability. The calculation of the Q2 value yields a result of 0.99, so the model has great predictive capability.

3. *Goodness of Fit Index* (GoF)
   The GoF value in SEM with PLS was calculated manually (Tenenhaus M., et al, 2005) using the formula:

$$GoF = \sqrt{AVE^2 x R^2}$$

$$GoF = 0.65$$

According to Tenenhaus M., et al, (2005), the value of small GoF = 0.1, medium GoF = 0.25 and large GoF = 0.38. Based on the calculation of the GoF value of 0.65, it means that the model has a large GoF value so that the model formed represents a real phenomenon.

4.1.3. Hypothesis test

To test the hypothesis in PLS SEM, a bootstrapping process is carried out which produces a T-count value. If the t-count value is greater than the t-statistic with a 95% confidence level (> 1.96), then the hypothesis is significant. Here are the bootstrapping results.

Table 4. *Path Coefficients* (Mean, STDEV, t-Value)

Hypothesis	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values	Conclusion
corporate governance -> trusted financial report	0,815	0,844	0,019	42,833	0,001	Accepted
corporate governance -> financial distress	-0,004	0,016	0,003	1,126	0,377	Rejected
audit quality -> trusted financial report	0,734	0,603	0,090	8,165	0,015	Accepted
audit quality -> financial distress	0,990	0,989	0,002	448,329	0,000	Rejected
financial distress -> trusted financial report	-0,764	-0,651	0,067	11,355	0,008	Rejected

Source: Output *SmartPLS, 2023*

4.2. Discussion of Research Results

The results of the study show that there is a significant influence of corporate governance on trusted financial reports. Previous research has shown that corporate governance has a significant influence on trusted financial reports. Corporate governance refers to the systems, policies and practices that govern the relationship between shareholders, the board of directors, management and other parties with an interest in the company. Research conducted by Bauer et al. (2003) found that companies with good corporate governance tend to have a higher level of trust in their financial statements. Research by Jombrik & Tamami (2021) highlights the important role of the board of directors in maintaining the integrity and quality of corporate financial reporting. They find that boards of directors that have an independent composition, adequate knowledge of accounting, and the capacity to oversee management effectively tend to produce more reliable financial reports. This shows that factors in corporate governance, especially the quality of the board of directors, can contribute to a trusted financial report.

This study also proves that there is no significant effect of corporate governance on financial distress. Referring to various previous studies, the results of research on the effect of corporate governance on financial distress are inconsistent. Several studies have found a significant relationship between corporate governance variables and financial distress, while other studies have shown different results. This could be due to differences in research methodology, the context of the companies studied, or other factors that influence the relationship. In line with previous research, this study reveals that corporate governance has an important influence on corporate financial distress. Through an effective board of directors structure, significant institutional ownership, transparency and good financial reporting, protection and appreciation of shareholders, and good risk management, companies can reduce the risk of financial distress and improve long-term financial health. However, keep in mind that corporate governance is only one of the factors that can affect financial distress, and other factors such as market conditions, business strategy, and economic factors also need to be considered in analyzing a company's financial risk.

This study proves that the influence of audit quality variables on trusted financial reports is significant. This result is in line with several previous research results, which show that there are findings indicating that audit quality has a significant impact on trusted financial reports. Research conducted by Eyenubo et al. (2017) found that audit quality has a positive effect on trusted financial reports. Audit quality is a measure of the extent to which an independent and objective audit is carried out by the auditor. This study shows that the higher the audit quality, the greater the trust placed by stakeholders in the company's financial statements. Another study conducted by Garcia-Blandon et al. (2020) conducted in European countries shows that audit quality plays an important role in creating trusted financial reports. High audit quality is measured through the independence and competence of the auditors as well as the tight supervision and review carried out during the audit process. The results of this study indicate that companies that experience high audit quality have financial reports that are more reliable and can be trusted by stakeholders. In addition, research by Sembiring et al. (2022) concluded that there is a positive correlation between audit quality and trusted financial reports. In this study, audit quality is measured through the auditor's reputation, strict supervision by the board of directors, and the use of more sophisticated auditing techniques. These findings indicate

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that auditors who have a good reputation and use better audit methods can provide additional assurance on the reliability of financial reports.

The results of the hypothesis test prove that there is a significant influence of the audit quality variable on the financial distress variable. The results of previous studies have provided diverse insights about the effect of audit quality on the level of financial distress of a company. Some research proves there is a negative influence, some research shows a positive relationship. Research conducted by DeFond (2017) shows that there is a negative relationship between audit quality and financial distress. In this study, audit quality is measured based on the independence, competence, and quality of work performed by the auditors. The findings show that companies that undergo audits with a high level of audit quality tend to have a lower level of financial distress. This shows that auditors who perform their duties properly can help prevent or reduce the risk of financial distress faced by companies.

The original negative financial distress sample value indicates that the financial distress variable has a significant negative effect on the trusted financial report. The results of a review of previous research revealed that the effect of financial distress on trusted financial reports is a fairly interesting research subject in the field of accounting and finance. A number of studies have been conducted to identify the relationship between financial distress and the level of confidence in the company's financial statements. One of the relevant studies is that conducted by Muñoz-Izquierdo et al. (2020) show that companies experiencing financial distress tend to face significant financial pressures, which in turn can affect the integrity and quality of the financial reports presented. Companies that are in financial distress have incentives to carry out aggressive or non-conservative accounting practices to try to improve their financial image or meet the desired financial targets. This can reduce stakeholder confidence in the company's financial statements.

5. CONCLUSION

The discussion here generally attempts to examine the relationship between variables based on financial literature. Corporate governance has a positive effect in encouraging the creation of trusted financial reports. This is because various factors such as remuneration/compensation, effectiveness of the board of directors, commitment to shareholder interests, transparency of information, and strong internal control mechanisms play an important role in ensuring the integrity, quality and reliability of the financial statements of BUMN Holding companies. Corporate governance has no significant effect in encouraging the creation of trusted BUMN Holding finance in Indonesia. This study indicates that external factors, such as market conditions that have experienced extraordinary turmoil due to the Covid-19 pandemic in the past two years or company financial policies to support government infrastructure project policies, have a greater influence in creating trusted financial conditions. In some cases, the influence of corporate governance becomes insignificant when there is interaction with these economic environmental factors. Audit quality has a positive effect in encouraging the creation of trusted financial reports. This study shows that the higher the audit quality, the greater the trust placed by stakeholders in the company's financial statements. Because with a quality audit, financial reports become more reliable, accurate and trustworthy, which in turn increases stakeholder confidence in the company concerned. Audit quality has a positive effect on trusted financial. Because with good audit quality, companies have a better opportunity to maintain their financial health, manage risk better, and increase stakeholder confidence in the company's financial statements. Trusted financial has a negative effect on trusted financial reports. Because when a company experiences trusted finance that faces significant financial pressure, this in turn can affect the integrity and quality of the financial reports presented. Companies that are in a trusted financial condition have incentives to carry out aggressive or non-conservative accounting practices to try to improve their financial image or meet the desired financial targets. This can reduce stakeholder confidence in the company's financial statements. Financial pressures faced by companies experiencing trusted finance, which resulted in the company's top priority shifting from the quality of financial reporting to the company's survival. As a result, the level of confidence in the company's financial statements may decrease. When the company's management is tempted to do accounting practices that are not correct or not conservative to show a better financial condition than it actually is. This can reduce trust in the company's financial reports and affect the trusted financial report.

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International Journal of Social Science (IJSS)
Vol.3 Issue.2 August 2023, pp: 249-258
ISSN: 2798-3463 (Printed) | 2798-4079 (Online)

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