

Detection of financial and non-financial factors affecting the acceptance of going concern opinion

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Abstract

Financial statements are source of information for investors in determining which companies to invest in. Therefore, the reliability of financial statements has an important role. In order for financial reports to be reliable, there are two important things, namely reporting quality and earning quality factors. The auditor gives a fair opinion as a form of reporting quality. Thus, the going concern opinion is one of the opinions given by the auditor on earning quality. This study tries to examine what factors encourage the auditor to give going concern opinion to the company. The method used is a quantitative method using inferential statistics. In particular, the instrument used is logistic regression. The findings of this study are that companies that tend to get a going concern opinion have certain characteristics, among others, are large companies that have profits and have a fairly high level of debt. This finding can then be used by investors to identify companies that have the potential to get a going concern opinion.

Keywords: *going concern opinion; company size; profitability ratio; leverage ratio; auditor size; and risky company*

Abstrak

Laporan keuangan merupakan sumber informasi bagi investor dalam menentukan perusahaan yang akan diinvestasikan. Oleh karena itu keandalan laporan keuangan memiliki peran penting. Agar laporan keuangan menjadi andal terdapat dua hal penting yaitu faktor reporting quality dan earning quality. Auditor memberikan pendapat wajar sebagai bentuk reporting quality. Sedangkan opini going concern adalah salah satu opini yang diberikan auditor terhadap earning quality. Penelitian ini mencoba meneliti faktor apa yang mendorong diberikannya opini going concern oleh auditor kepada perusahaan. Metode yang digunakan adalah metode kuantitatif dengan menggunakan statistik inferensial. Secara khusus alat yang digunakan adalah statistik regresi logistik. Temuan dari penelitian ini adalah bahwa perusahaan yang cenderung mendapatkan opini going concern memiliki karakteristik tertentu antara lain adalah perusahaan besar yang memiliki profit dan memiliki tingkat utang yang cukup tinggi. Temuan ini selanjutnya dapat digunakan oleh investor untuk mengenali perusahaan-perusahaan yang berpotensi mendapatkan opini going concern.

Kata kunci: *opini going concern; ukuran perusahaan; rasio profitabilitas; rasio leverage; ukuran audit; perusahaan beresiko*

INTRODUCTION

Financial statements provide a role as a source of information for investors to decide to invest in a company. As a source of information, the financial statements need to have reliability. One of the sources of reliability is the opinion that comes from public accountants. The opinion consists of several levels ranging from the highest opinion to unqualified opinion. In the unqualified opinion, the financial statements are stated to be fairly prepared using the applicable accounting standards. However, apart from the level of fairness, there are other things that audit firms must consider in providing an opinion, namely the sustainability of the company. The sustainability of the company is an investment indicator for investors. The company does not receive money from investors so that it can close, but rather so that it can continue its business and provide returns to investors. Kuruppu and Oyelere (2012) found that the absence of a going concern opinion will reduce investor confidence in financial statements.

There are several indicators from the financial statements that can be used to determine whether the company has sustainability. These indicators can consist of financial indicators and non-financial indicators. Financial indicators are by looking at the size of the company, the profitability and liquidity of the company. In addition to these indicators, this study also wants to examine whether the size of the audit firm has an effect on the tendency of public accounting firms to provide going-concern opinions.

This study aims to determine what variables affect the going concern opinion received by the company. Theoretically, there are factors that are considered to affect the sustainability of the company. The consequence is that most of the firm's value comes from the firm's terminal value. Because of the importance of growth, growth is one of the factors that support the sustainability of the company. Growth itself is influenced by the company's ability to generate profits or profitability. Meanwhile, in short the company's ability to fulfill all its obligations including obligations to investors is reflected in the company's liquidity. One of the other indicators used to examine the acceptance of going concern opinions is the size of the company and the size of the audit firm. This is in accordance with the opinion of Kaplan & William (2012) which states that there is a relationship between company size and the acceptance of going concern opinions. In fact, audit firm size and going concern opinion acceptance has been studied as well and there is a significant relationship between audit firm size and going concern opinion provision.

This study not only aims to find the relationship between the going concern opinion acceptance variable and the factors that influence it but also to understand what conditions influence these factors in Indonesia. Furthermore, this research can be useful for several parties. For academics, this can provide additional literature on the factors that influence the acceptance of going concern opinions. For investors, the sustainability of the company has an important role in determining the company to invest in and how long to invest in the company.

LITERATURE REVIEW

Company size

Kaplan & William (2012) stated that company size is one indicator that determines the acceptance of going concern opinions. In theory, large companies that are in a steady state already have dominance over market share. This dominance then provides predictability of cash flows. When there is predictability of cash flows, the sustainability of the company will be maintained.

Tsipouridou & Spathis (2014) found things that small companies tend to be more difficult to get a going concern opinion because small companies are vulnerable to economic changes. The volatility of the company's cash flows related to this economic condition will reduce the company's sustainability.

H₁: Company size negatively influences the acceptance of going concern opinion.

Profitability ratio

Saladrigues (2016) states that profitability has a positive effect on the acceptance of going concern opinions. Profit is the source of the company's free cash flow. When the company has a stable profit, the company can accumulate cash flow and will increase its sustainability.

H₂: Profitability ratio negatively influences the acceptance of going concern.

Leverage ratio

To be able to continue to operate, companies need to continuously invest. Investment here can be made in investment into working capital or capital expenditure. In order to be able to invest, the company needs funding. One source of funding comes from debt. The consequence of debt is that the company needs to set aside a portion of its cash flow to pay the interest on the debt and the principal on the loan. The optimum level of debt will provide added value to the company but when the debt level is too high it will cause financial distress.

H₃: Leverage ratio positively influences the acceptance of going concern opinion.

Auditor size

Kaplan & William (2012) found that large audit firms have a higher probability of providing a going concern opinion compared to small audit firms. In particular, there is a term to distinguish large audit firms from small audit firms. Large audit firms are often referred to as Big-4 or big four which shows the earnings ranking of audit firms. In Indonesia, the majority of audit fees are obtained by these large audit firms.

H₄: Auditor size has impact on the acceptance of going concern opinion.

Risky industry

Each industry has different characteristics. There are industries that require high capital to enter, there are industries where the companies in them are tightly regulated and there are industries where the failure rate of companies in them is low. This industry risk affects how a company gains market share, maintains market share and generates cash flow. Furthermore, in industries where there are high barriers to entry and it is difficult to gain market share, the company's ability to generate cash flow will be limited. In the end, the company's limitations in obtaining cash flows will affect the company's level of sustainability. Therefore, companies in risky industries will find it more difficult to accept going-concern opinions.

H₅: Risky industry has a significant impact on the acceptance of going concern opinion.

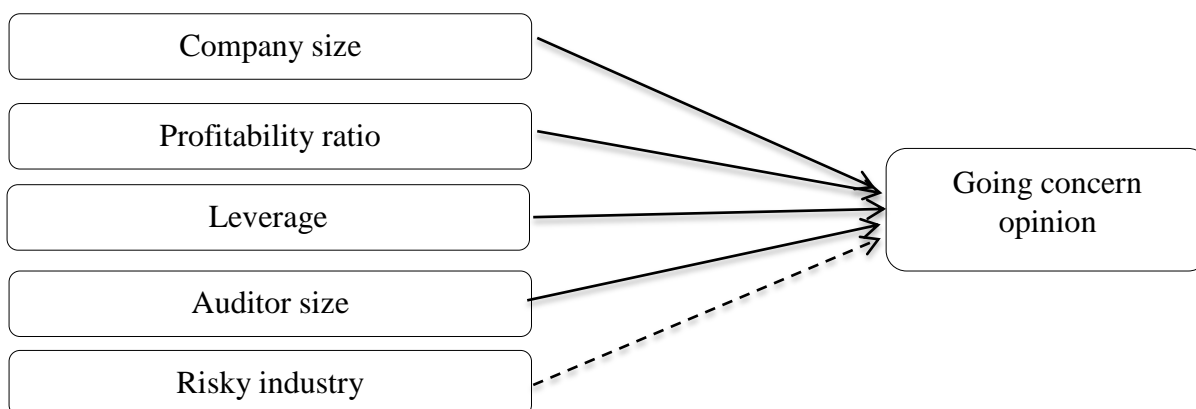


Figure 1. Research framework

RESEARCH METHOD

Sampling process

The data used in this research is obtained from the company's financial statements issued by the company which can be accessed on the Indonesian stock exchange website. Data reliability is obtained by relying on data sources. In this case the data comes from financial reports issued by the regulator, namely the Indonesian stock exchange. Another source of reliability is that the financial statements that are used as sources have been audited by an audit firm. It is assumed that the opinion of the public accountant reflects the quality of the financial statements. This assumption can be made because public accountants are bound by a code of ethics and laws and regulations. The amount of data obtained is shown in table 1 below.

Table 1. Research sampling

| Description | Number of companies |
|--|---------------------|
| Special notation companies as of September 2021 | 113 |
| Adverse and disclaimer opinion | (8) |
| Incomplete data | (41) |
| Number of sample | 64 |
| Number of samples run for the analysis (3 years) | 192 |

Operational definition of variables

The hypothesis testing is using logistic regression analysis equation below;

$$\ln[GCO/(1 - GCO)] = \beta_0 + \beta_1 \text{Size} + \beta_2 \text{Prof} + \beta_3 \text{Lev} + \beta_4 \text{Aud_Siz} + \beta_5 \text{Risk_Co} + \varepsilon$$

Where:

Size: measured by firms total asset.

| | |
|------------------|---|
| Profitability: | measured by using return on asset as shown as comparison between firm net income compared to total asset. |
| Liquidity ratio: | represents debt to assets which is formulated as total debt/total assets. |
| Auditor size: | measured by using a dummy variable. It will be given 1 if it is from big-4 audit firm and 0 if otherwise (Kaplan & William (2012)). |
| Risky Industry: | measured by using dummy variables based on SIC categorization. |

RESULTS AND DISCUSSION

Descriptive analysis

The research method used in this study is a quantitative method. One of the statistical tools used to see the characteristics of the data is descriptive statistics. This statistic serves to see the distribution of the data. By looking at the distribution of the data, it can be seen whether the data is normally distributed. Furthermore, the normality of the data will be important so that it can be processed further. Table 2 shows the size of the data in the form of the largest data size, the smallest data size, data concentration and data distribution.

Table 2. Descriptive statistics

| | N | Minimum | Maximum | Mean | Std. deviation |
|--------------------|-----|---------|---------|-------|----------------|
| GCO | 192 | ,00 | 1,00 | ,83 | ,36 |
| Company size | 192 | -10,48 | 15,89 | 11,59 | 3,07 |
| Profitability | 192 | -1,36 | 8,76 | -,02 | ,68 |
| Leverage | 192 | ,10 | 9,22 | ,92 | 1,02 |
| Auditor size | 192 | ,00 | 1,00 | ,10 | ,31 |
| Risky industry | 192 | ,00 | 1,00 | ,60 | ,48 |
| Valid N (listwise) | 192 | | | | |

Multicollinearity test result

In addition to normally distributed data, so that the independent variables can be related to the dependent variable, the independent variables must not have a too close relationship. When the independent variables have a relationship that is too tight, the error value will tend to be too low, making the model appears to have a small error value outside the expected value. Thus, as if the model has a high degree of suitability. This problem of multicollinearity can be detected by analyzing the correlation between these variables. Furthermore, the collection of error correlations between these variables is combined in a matrix called the correlation matrix.

Table 3. Multicollinearity table

| | Constant | Firm SIZE | PROF. | Leverage | Auditor SIZE | Risky industry |
|--------------|----------|-----------|-------|----------|--------------|----------------|
| Constant | 1,00 | -,99 | -,77 | ,26 | ,28 | -,06 |
| Company size | -,99 | 1,00 | ,81 | -,33 | -,36 | ,02 |

| | | | | | | |
|----------------|------|------|------|------|------|------|
| Profitability | -,77 | ,81 | 1,00 | -,57 | -,46 | -,11 |
| Leverage | ,26 | -,33 | -,57 | 1,00 | ,29 | ,04 |
| Auditor size | ,28 | -,36 | -,46 | ,29 | 1,00 | ,24 |
| Risky industry | -,06 | ,02 | -,11 | ,04 | ,24 | 1,00 |

Hair et al. (2010) stated that the correlation consists of a conservative measure and a maximum measure. The maximum acceptable correlation is 0.9 while the conservative measure is 0.7. In the correlation matrix in this study, there are no variables that have a correlation of more than 0.9. Thus, there are no variables that neither have errors nor are connected to each other.

Logistic regression

In this research, the impact of the independent variables towards the dependent variables implies probability of the occurrence for the dependent variable. In fact, the type of regression used is logistic regression.

Table 4. Logistic regression analysis

| | B | S.E. | Wald | df | Sig. |
|----------------|-------|-------|-------|----|------|
| Company size | -3,22 | ,81 | 15,49 | 1 | ,00 |
| Profitability | -7,21 | 2,01 | 12,85 | 1 | ,00 |
| Leverage | 2,46 | ,99 | 6,11 | 1 | ,01 |
| Auditor size | 3,40 | 1,10 | 9,45 | 1 | ,00 |
| Risky industry | ,72 | 1,37 | ,27 | 1 | ,59 |
| Constant | 40,73 | 10,93 | 13,87 | 1 | ,00 |

$$\frac{\ln GCO}{1 - GCO} = 40,730 - 3,223 \text{ Size} - 7,211 \text{ Prof} + 2,462 \text{ Lev} + 3,406 \text{ Aud_Siz} + 0,724 \text{ Risk_Co} + \varepsilon$$

Determination coefficient test result

Table 5. Determination coefficient test

| Step | -2 Log likelihood | Cox & Snell R square | Nagelkerke R square |
|------|---------------------|----------------------|---------------------|
| 1 | 41,592 ^a | ,487 | ,830 |

When the model has a high degree of conformity, the model can be used to explain the deviation of the dependent variable. In the table above using the Cox & Snell method the model can explain 48.7% of the variation of the dependent variable. Meanwhile, using the Nagelke model can explain 83% of the variation.

Autocorrelation test result

Table 6. Autocorrelation test

| Model | R | R square | Adjusted R square | Std. error of the estimate | Durbin-Watson |
|-------|-------------------|----------|-------------------|----------------------------|---------------|
| 1 | ,597 ^a | ,356 | ,339 | ,299920 | 2,101 |

Besides, the errors of the independent variables should not be related to one another or no issue on autocorrelation. The ideal value to be free from autocorrelation is when the indicator shows a value between 1.5 and 2.5; thus, it is shown in this table.

Discussion

This study found that large companies have a higher probability of getting a going concern opinion. These results are consistent with findings from Feldmann & Read (2010). In the Indonesian context, where large publicly listed companies tend to take the form of conglomerates and are owned by a small number of families. One of the advantages of large companies in the form of conglomerates is company integration. The company has suppliers and distributors who are actually subsidiaries. This creates a synergy. This synergy then makes the company will have a stable cash flow so that the possibility will be higher for the company to get a going concern opinion.

Besides, the result does not find a significant relationship between profitability and acceptance of going concern opinions. One of the conclusions drawn is that as long as a company has positive profitability, the company will be more likely to accept going concern opinions compared to companies that have negative profits.

However, it is found that the level of debt affects the probability of receiving a going concern opinion. The use of debt can increase the company's free cash flow, especially when viewed from the point of view of free cash flow to the firm. One thing that needs to be considered is not to let the company owe too much, causing financial distress.

Futhermore, Hossain, et al. (2020) stated that large audit firms tend to provide going concern audit opinions. This study found something similar. In the Indonesian context this is understandable. Large audit firms tend to have large companies as their clients. Large companies tend to have a stable market share and cash flow. Therefore, it is natural that the opinion given by a large audit firm tends to be a going concern opinion.

Eventually, Kaplan & William (2012) state that companies in risky industries tend not to accept going-concern opinions. However, this study found different results. One of the reasons why risky industries do not have a significant relationship in this study is because risky industries in Indonesia have different characteristics. Large companies in Indonesia are conglomerate companies owned by a handful of families. Because it is a conglomerate, the company's risk becomes diversified. Therefore, companies in the conglomerate company system cannot be seen only from the risks borne by each company.

CONCLUSION

This study found that large companies tend to be given a going concern opinion. This finding is consistent with the theory that large companies that are already in the established phase tend to have market share and thus have stable incomes which ultimately affect the company's sustainability. However, this research profitability has a positive but not significant relationship. This means that as long as the company is able to generate positive profits, this condition will not affect the going concern opinion. Another finding from this study is that the level of corporate debt has a significant relationship with the probability of granting a going concern opinion. When the company has a high level of debt, this will force the company to allocate some of its cash flow to pay debt interest and principal debt. In addition to the company's internal factors, external factors such as external factors, namely the size of the audit firm also affect the probability. The larger the audit firm, the more likely it is that the firm will provide a going concern opinion. However, this can be because large audit firms tend to be hired by large companies that have a higher level of sustainability. Meanwhile, large companies in this study tend to get a going concern audit opinion. These independent variables need to be seen in the relationship as a model. This relationship is important because the model will provide a clearer picture of the relationship between the independent variables in determining the probability of the dependent variable in this case is in determining the probability of receiving a going concern opinion.

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