

Social Capital and Audit Fees: Evidence from Indonesia

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ABSTRACT

A surge of problems is haunting the accountants to date, one of which is the absence of audit fees' standard. Although there have been many studies on the factors that influence audit fees, this issue still requires study. This study examines the effect of social capital on the amount of audit fees for go public companies in Indonesia in 2015-2019. A total of 610 observations representing 122 companies became the sample of this study. Hypothesis test is conducted on two groups of data based on the social capital index, namely the low and the high social capital index. Multiple regression analysis was used for data processing and analysis. This study indicate that the company's social capital has an influence on the audit fee. Firms domiciled in areas with a high social capital index pay lower audit fees and vice versa. Our study explains an understanding of how social capital works in accounting settings, especially in the field of auditing and provides recommendations to public accountants to consider social capital factors in determining audit fees. This study contributes to both theoretically and practically by showing that the social environment can form a trust between auditors and clients, and have an impact on the audit fees.

JEL Code: M42, P16, O16, Z13

Keywords: Social Capital, Audit Fees, Indonesia

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I. Introduction

Many studies have examined the factors that affect audit fees, for example the impact of industry specialization (Carson, 2009), role of audit firm size, impact of audit risk (Sonu et al. 2017), dan client size (Kikhia, 2015). Although there have been many studies on the determinants of audit fees, this issue still a concern. A surge of problems is haunting the accountants to date, one of which is the absence of audit fees' standard (Sinaga, 2015). Considering the absence of audit fees' standard, various questions arise, whether audit fees are in accordance with the challenges faced by auditors in auditing? Or vice versa, audit fees are not in accordance with their work as indicated by (Sinaga, 2015)? Empirical studies are needed to confirm this.

Simunic (1980) argues that the higher audit fees is the result from more audit work (auditor effort) and higher estimated losses /litigation risk. Causholli et al (2010) have analyzed various variables that have an impact on auditor effort/ litigation risk that may affect audit fees (e.g. elements of audit market and audit production). Furthermore, (Jha & Chen, 2015) investigates non-financial factors, namely the influence of social capital and client located on audit fees. A sense of mutual trust that is formed within the community (Jha & Chen, 2015) is called social capital which forms a cooperative attitude and forms collective action/behavior to achieve synergy between social and economic aspects that have an impact on behavior and contribute to audit fees (Liu, 2017).

When the level of social capital in society is high, the auditor's efforts reflected in audit fees will be lower because social capital can reduce opportunistic behavior (Callois & Angeon 2004). Social capital can make people guilty if they do something unethical (Fukuyama 1997) and can reduce opportunistic behavior and have an impact on audit risk (Jha & Chen 2015; Sánchez-Ballesta & Yagüe 2021; Jha 2019). Companies that are headquartered in areas with high social capital tend to pay lower audit fees because they tend to manipulate financial information less (Yue 2010; Jha & Chen 2015; Chen et al. 2021; Sánchez-Ballesta & Yagüe 2021). In other words, the quality of financial reports is highly dependent on the quality of the social environment (McGuire et al. 2012).

Jha & Chen (2015) show that auditors actually consider the condition of a company's social capital in determining the amount of audit fees. The study (Jha & Chen, 2015) was conducted on companies headquartered in the US. However, it is not clear whether their findings can be generalized to other countries, especially developing countries such as Indonesia, where the quality of people's welfare (health, income, human capital) and the purchasing power are generally still below the international average ([https://www.youtube.com/watch? blogs.worldbank.org/](https://www.youtube.com/watch?blogs.worldbank.org/)). In addition, management performance in Indonesia is generally assessed based on company profitability. Based on bonus plan hypothesis, the manager will choose a decision that can increase

the bonus earned (Jaya et al. 2021). The question arises whether social capital in Indonesia can encourage managers to behave more honestly, or whether the phenomenon of financial pressure to achieve profit will triggers managers to manipulate financial reports and affect the amount of audit fees.

In Indonesia, studies on social capital issues are still very limited. By going through the topic of audit fees in Indonesia in the national accredited journals and the proceedings of the national accounting symposium in recent years, only three articles with the topic of audit fees were found, but none of them were associated with social capital variables. Therefore, this research aims to analyze whether social capital plays a role in economic decisions in Indonesia, by analyzing relationship between social capital and amount of audit fees in Go Public companies in Indonesia.

This study provides contribution on both theory and practice. Considering that there are still very few studies which study the social capital in literature of accounting, this research is a stepping stone for accounting researchers to understand how social capital works in accounting settings. The results of the study provide an explanation of the impact of social capital (social environment) on managerial decisions (determining the amount of audit fees), such as companies in an environment with high social capital has an impact on reduction in audit fees. This study also provides recommendations for public accountants to consider social capital in determining the amount of audit fees. This study also adds much needed references to the research literature in the field of auditing, particularly the issues of social capital and audit fees in developing country.

II. Theory & Hypothesis Development

2.1 Audit Fees

Audit fee refers to a number of rewards in the form of money (economic rewards) for auditors who perform audit services. Audit fee is also an agency fee that refers to certain standards and criteria, including the consideration of risk compensation and profit requests (Liu, 2017). In Indonesia, the determination of audit fees must consider the needs of the client; duties and responsibilities according to the law; independence; the level of expertise and responsibility attached to the work conducted, the level of complexity of the work; the length of time required to complete the work; and the basis for determining the agreed fee (Indonesian Institute of Certified Public Accountants No.024/IAPI/VII/2008). The two most important determinants of audit fees are (1) audit effort and (2) litigation risk/losses arising from litigation (Simunic 1980; Venkataraman et al, 2008). Audit fees may be higher because of larger estimated losses and/or because of more audit work.

2.2 Social Capital

Social capital refers to mutual trust in society and is a norm that facilitates collective actions (Woolcock, 2001). Social capital is associated to the existence of beliefs, official values and shared norms among group members which allows them to collaborate (Guiso et al, 2008).

Social capital is also associated with trust because trust can create cooperation between groups (Putnam 1993a). Trust is at the heart of social capital and can reduce social costs, lower transactional costs, facilitate inter-organizational relationship and enhanced manager-subordinate relationship (Doney et al. 1998). Social capital is a norms and networks that accelerate collective action (Woolcock, 2001; Jha & Chen, 2015). Social norms represent intrinsic motivation and network density represents extrinsic motivation to be selfless. Strong social capital has an effect on increasing penalties for deviant behavior and at the same time encouraging good behavior and creating a conducive cooperation culture (Deller & Deller, 2010). (Jha, 2019) Strong social networks, make people rely on one another, and encourage the tendency to respect obligations, develop mutual trust, pass on morals to the next generation and all these values are internalized into community groups, thus making people behave in certain ways that are in accordance with the values held by the group (Fukuyama, 1997); (Portes, 1998). Previous studies have shown that social capital is negatively related to opportunistic (dysfunctional) behaviors, examples corruption (LaPorta et al, 1997), crime (Buonanno et al, 2009), and the definition of transaction costs related to financial markets (Guiso et al, 2004). Strong social capital not only encourages good behavior but also increase punishment for deviant behavior (Spagnolo 1999).

2.3. Social Capital and Audit Fees

The audit fee depends on the auditor's efforts in planning and carrying out the audit work. Planning and implementation audit works requires management integrity, Management integrity is an important factor that auditors consider when deciding how much audit effort is required and how much in charging the clients (Beaulieu, 2001). Management integrity is closely associated to the quality of financial report and this is related to the social capital environment in where the client is located. Social capital affects the quality of financial report (McGuire et al, 2012); (Kang et al, 2010).

The auditor's efforts in planning the auditing (identifying things that are riskier and which require more resources) influenced by the social capital in which the company is located. Companies that are based in the areas with a high social capital are thought to have a high corporate culture as well. The psychology literature states that companies hire and retain employees who share their own values and employees prefer to work for companies that share their own values (McGuire et al. 2012). Social capital in the area where the company is based at is thought to have an impact on the auditor's trust in the companies' managers. Auditors feel less confident when companies are based in areas with a low social capital. Lack of trust will increase audit effort and worry about litigation, thereby increasing the client costs.

If there's a lack of trust of the auditor towards the management, then more substantive procedures will be carried out by the auditor to ensure that the financial statements are fairly

presented (Beaulieu, 2001). When the company is in an area with high social capital, managers will tend to be more honest in presenting financial statements (Jha, 2019), and auditors will have more trust in clients and reduce auditor efforts.

In areas with higher social capital, it is easier for auditors to obtain evidence from customers, banks, suppliers, as well as stakeholders and they might be more precise. Therefore, it is easier for audit efforts to obtain sufficient and appropriate audit evidence which will result in lower audit fees. Auditors also perceive a lower lawsuit risk from companies located in areas with higher social capital (Simunic, 1980). Auditors' concerns about litigation risk can increase audit fees (Guiso et al, 2004).

In the environment with a low level of trust, litigation risk will be higher and finally require greater effort in carrying out audit work. Therefore, for companies located in areas with a low social capital, auditors are likely to apply more effort and demand higher audit fees and instead, if companies are located in areas with high social capital, auditors are likely to apply less effort and demand lower audit fees.

Several previous studies have shown the relationship between social capital and behavior along with the relationship between social capital and audit fees. Audit fees may vary due to the workload of auditing and/or losses that are expected to be greater. Auditors need more time before signing their reports for clients who live in areas with low social capital.

The probability of litigation involving auditors is also higher in the areas with low social capital (Simunic, 1980). Auditors also identify a higher risk of lawsuits from companies that are in the areas of low social capital. Companies tend to behave poorly and third parties may have an unfavorable opinion of the management. Fear/worry about litigation risk can increase audit fees because litigation costs are relative to audit fees, so auditors tend to consider the trustworthiness of their clients. In an environment of low trust, the auditor's effort and litigation risk will be higher. Therefore, auditors are likely to exert more effort and demand higher audit fees on companies which are located in areas with low social capital. On the other hand, auditors will exert less effort and demand lower audit fees if the companies are based in an area with a high social capital.

Previous research found that the effect of social capital on audit fees will be tripled if the audit offices are located closer to the client, i.e. when the auditor is located within a 100-kilometre (62.13 mi) radius from the client or in the same metropolitan area as the client if compared to when they are located further away. Guiso et al, 2008b; Grullon et al (2010), state that these results provide strong evidence that auditors would consider the social capital of where the company is based, in assessing / determining the amount of audit fees.

Regarding the relationship between auditor attitudes and audit fees, previous research has shown that the level of skepticism of auditors varies based on where their clients are located. The social environment affects the quality of financial reporting (Kang et al 2010; McGuire, et al 2012). Jha (2013) found that when companies are based in areas with low social capital, the quality of financial reports will also be low. In particular, the degree of accrual earning management, real earning management, and the tendency of financial fraud will be high. There is a belief that the auditor will consider the low quality of reporting produced by the client or the auditor is more skeptical if the client is located in an area with low social capital.

Managers may be more honest in areas with high social capital and norms. Managers are

encouraged to behave more honestly in the areas with high social capital. Classical literature holds that social norms affect individual decisions (Cialdini et al, 1991). When someone deviates from social norms, guilt will arise. In the context of managerial reporting behavior, stakeholders (institutional investors, bankers, managers) are more likely to interact which leads to greater information exchange, more effective supervision, and leads to more honest behavior (Wu 2008).

2.4. Research Gap

Simunic (1980) argues that the higher audit fees is the result from more audit work (auditor effort) and higher estimated losses /litigation risk. Guiso et al (2008) & Grullon et al (2010) argues that in determining audit fees, auditor consider the social capital where the company is headquartered. Social capital affects the quality of financial report (McGuire et al, 2012); (Kang et al, 2010). Jha (2013) found that companies are headquartered in areas of low social capital, the quality of financial reports is also low. So, it can be said that one of the things can affect audit fees is social capital

Jha & Chen (2015) show that auditors actually consider the condition of a company's social capital in determining the amount of audit fees. The study (Jha & Chen, 2015) was conducted on companies headquartered in the US. However, it is not clear whether their findings can be generalized to other countries, especially developing countries such as Indonesia, where the quality of people's welfare (health, income, human capital) and the purchasing power are generally still below the international average (<https://www.youtube.com/watch?blogs.worldbank.org/>). In addition, management performance in Indonesia is generally assessed based on company profitability. Based on bonus plan hypothesis, the manager will choose a decision that can increase the bonus earned (Jaya et al. 2021). The question arises whether social capital in Indonesia can encourage managers to behave more honestly, or whether the phenomenon of financial pressure to achieve profit will triggers managers to manipulate financial reports and affect the amount of audit fees.

2.5. Hypothesis Development

Previous studies have shown that the level of auditor skepticism was varied based on where the client is located. Auditors are more skeptical and considering the low quality of reporting expected from clients who live in areas with low social capital. Managers may be more transparent and honest in areas with high norms and social capital. Companies located in areas that have high social capital will encourage their managers to behave more honestly. Classical literature thinks that social norms in society have an effect on the individual decision making (Cialdini et al, 1991). When a person deviates from social norms, guilt will arise. In the context of managerial reporting behavior, stakeholders interact more frequently which leads to greater information exchange, more effective supervision, and leads to a more honest behavior (Wu, 2008).

Grullon et al (2010) also state that auditors consider the social capital in where the companies are located, in determining the amount of audit fees. A strong evidence that auditors in determining audit fees, will consider the social capital where the company is located (Jha & Chen, 2015). The effect of social capital is stronger when the office is located closer to the client. The results show that when auditors are located in the social capital area as the clients, the effect of social capital on audit fees is three times higher if compared to when they are located further away (located in different cities). (Jha & Chen, 2015) also show that social capital has become stronger in 2004 (after the Sarbanes-Oxley Act), when audit practices become more auditing works (more complex) due to the implementation of the Sarbanes-Oxley Act (SOX).

Trust between companies, stakeholders, and investors is built through social capital (Lins et al. 2017). Jha & Chen (2015) also prove that auditors take and need more time and judgment to sign audit reports of clients who are in a low social capital environment. Auditor trust will decrease in companies which are located in areas with lower social capital, because they tend to have lower quality financial reports and tend to manipulate financial reports / financial statements (Jha, 2019). Due to the reduced auditor trust in companies located in areas with low social capital, so audit fees will increase. Conversely, high social capital encourages managers to behave more honestly which will lead to a decrease in audit risk and audit fees (Yue 2010; Jha 2019). High social capital is expected to reduce earnings manipulation due to feeling of guilt, monitoring, and punishment (Sánchez-Ballesta & Yagüe 2021).

Social capital in the area where the company is located, is suspected to have effect on the auditor's trust in managers. There is a lack of trust from Auditors when the company is located in an area with low social capital. Lack of trust will increase audit effort and concerns of litigation is suspected to increase client fees. Based on this argument, this study presumes that

H: Companies located in areas with a high social capital index will pay lower audit fees, or vice versa.

III. Research Method

3.1 Variable Measurement

Audit Fees

Audit fees are rewards in the form of money (economic rewards) given to auditors who perform audit services, which are often called agency fees according to certain standards or criteria, including the consideration of risk compensation and profit requests (Liu, 2017). Data on audit fees are taken from companies which disclose the amount of audit fees, and are listed on the Indonesia Stock Exchange (IDX) in the period 2015–2019. The natural logarithm of audit fees is used to measure audit fees. Natural logarithms are used to minimize the difference in numbers that are too far from the data that has been obtained as the research sample. Disclosure of the amount of audit fees in the financial reports of companies in Indonesia is still rare, because the disclosure of audit fees data in Indonesia is regarded as voluntary disclosures. Audit fees will be symbolized by AUFEE in the equation.

Social Capital

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Social capital is defined as a mutual trust in society and is a norm that facilitates collective action (Woolcock, 2001). Social capital is measured using the regional/provincial social capital index developed by the Statistics Indonesia in 2014 (<https://www.bps.go.id/>) (<https://www.bps.go.id/>). This social capital index is the last issued by Statistics Indonesia which is still in use today. This social capital index remains relevant to be used to analyze its effect on audit fees for five years (2015-2019). This assumption is based on (Anheier, Gerhards, & Romo, 1995) who state that unlike human and physical capital indexes, social capital indexes are "sticky". The idea is also confirmed by (Jha & Chen, 2015) who found the correlation between the social capital index in the United States for a period of almost a decade, 2000-2009, which was 0.91.

The 2014 Social Capital Statistics publication provides information that describes the condition of social capital in Indonesia is described in three groups of indicators, which are collective action, membership in local associations and networks, trust and tolerance. This publication provides input for policy makers in designing, implementing, and evaluating development programs both at the regional and central levels.

Social capital in Indonesia was measured in 2010 using a national survey for social and economic aspects conducted in 2009. In 2014, the social capital index was calculated using the exploratory factor analysis method with data on a scale of 10, for the purpose of identifying relationships between variables and dimensions of social capital through principal component analysis as an extraction method. There are seven factors shown from the social capital index, which consist of trust, ethnic tolerance, reciprocity, collective participation, group participation, religious tolerance and networking. These seven factors of social capital are grouped into three indicators, namely networks, trust and collective action.

With a scale of 0-100, in 2014, the national social capital index was 49.45. The magnitude of this social capital index varies between provinces with the difference between the highest and lowest index being 17.62. The highest index is in Province of Central Java at 55.62, while the lowest index is in the Riau Islands with 38.00. This study divides the social capital index into two categories, namely low and high by dividing the two parts of the difference between the highest and the lowest index. If the social capital index is in between 38.00 - 46.81, then it is regarded as low and if it is in between 46.82 - 55.62, it is categorized as high.

Control Variable

The control variable is intended to exercise control so that the influence of the independent variable on the dependent is not influenced by external factors that are not the focus of research (Sugiyono, 2016).

This study uses 15 (fifteen) control variables at the firm-level, which are Size, Leverage, Inherent Risk, Profitability, Type of auditor, Auditor Business, Public exchange, Audit Tenure, Audit issues (Audit Opinion and Going Concern); Regional characteristics (cost of living; population density; population density growth); and Audit Quality.

Size is measured with the natural logarithm of total assets (LnTA); Measuring leverage \ by calculating Total Liabilities divided by Total Assets; Inherent risk is calculated by adding up (Receivable + Inventory)/Asset; Profitability is measured by ROA and a dummy variable to

show the losses experienced by the company (score 1, if the company suffers losses in that year and/or otherwise, score 0); The type of auditor is divided into Public Accounting Firm (PAF) non-Big 4 and Big 4 by using a dummy variable, namely if the PAFs are considered as Big 4, then it will be given a score of 1 and if it is non-Big 4, it will be given a score of 0; Auditor effort is measured using the lag between the date of the auditor's signature and the date of the end of the fiscal year (day to sign), the audit fee is estimated to be higher if the lag between the signing date of the audit report and a greater date of the end of the fiscal year. This indicates that there was a delay in the publication of financial statements due to problems that arose during the audit period; Public exchange is proxied with a dummy variable, namely a score of 1 if the company's shares are exchanged on the main board, while a value of 0 if the company's shares are exchanged on the development board. Companies whose shares are listed on the main board are companies that have large sizes and track records, for example, have an unqualified opinion for the last 2 years, posted operating profit in the last 1 financial year, have net tangible assets of > IDR 100 billion and the number of shareholders of > 1000 parties. Companies with good track records will make it easier for auditors to conduct the audit process, so that it has an effect on the audit fees. Audit tenure is proxied by auditor exchange. One of the reasons why clients change auditors is to obtain lower audit fees. Audit problems are proxied by issuing an audit opinion using a dummy variable (score 1, if an unqualified opinion is issued and a score of 0, if a non-qualified opinion is issued). If the resulting opinion is not an unqualified opinion, it is assumed that there are problems that can increase the risk of higher audit fees. Audit problems are also proxied by the issuance of going concern reports by using a dummy variable, namely a score 1, if the auditor issues a going concern audit report or otherwise, score 0. Regional characteristics are measured by the cost of living in the area, population density, per capita income, and population growth (Jha & Chen, 2015). The larger the population and the greater the per capita income in an area, the higher the audit fee will be. Audit Quality, proxied by big4 PAFs. When a company is audited by one of Big4 PAFs that has quality in conducting a good audit process, the audit fees will be greater than if the company uses a non-Big 4 PAFs.

3.2 Population and Sample

All go public companies in Indonesia for the 2015-2019 period are the population of this study. The five-year period is considered because it is the latest data that can be obtained and is deemed to be able to obtain sufficient and adequate results to explain the factors that affect audit fees. Purposive sampling method was used to select samples, namely the method of selecting samples based on certain criteria to obtain a representative sample. The sample criteria are go public companies that are listed on the Indonesia Stock Exchange in 2015-2019 and have been listed on the IDX by December 31, 2011 at the latest; not delisting during the observation period; Companies that provide annual reports along with financial statements that have been audited by independent auditors and companies that disclose the amount of audit fees in the annual report. A total of 610 observations representing 122 companies became the sample of this study.

3.3 Empirical Model

Multiple regression analysis is used for hypotheses testing. The regression equation is as follows:

$$\text{AUFEE} = \beta_0 + \beta_1\text{SOCIALCAPITAL} + \beta_2\text{SIZE} + \beta_3\text{DEBT} + \beta_4\text{ROA} + \beta_5\text{BIG4} + \beta_6\text{LOSS} + \beta_7\text{DAYS TO SIGN} + \beta_8\text{PUBLIC EXCHANGE} + \beta_9\text{UNQUALIFIED OPINION} + \beta_{10}\text{GOING CONCERN} + \beta_{11}\text{INHERENT RISK} + \beta_{12}\text{AUDITOR CHANGE} + \beta_{13}\text{COST OF LIVING} + \beta_{14}\text{RURAL} + \beta_{15}\text{LN POP} + \beta_{16}\text{POPG} + \varepsilon$$

Notes:

AUFEE	: Audit Fee
SOCIAL CAPITAL	: Social Capital
SIZE	: Size
DEBT	: Leverage
ROA	: Return on Asset
BIG4	: Big4 or non-Big4 Public Accounting Firm
LOSS	: Loss
DAYS TO SIGN	: Lag between the signing date of the audit report and the end of the fiscal year
PUBLIC EXCHANGE	: Main or Development Stocks
UNQUALIFIED OPINION	: Unqualified Opinion
GOING CONCERN	: going concern modification report
INHERENT RISK	: Inherent Risk
AUDITOR CHANGE	: Auditor Change
COST LIVING	: regional minimum wage
RURAL	: Population density is less than the median
POPULATION	: Population density at a certain area
POP G	: Population density growth

IV. Result and Discussion

4.1 Descriptive Statistic Test

The following are the results of descriptive statistical test from 610 observations obtained from 122 companies listed on the Indonesia Stock Exchange (IDX) in 2015-2019. Table 1 shows descriptive statistical tests. The mean value for Social Capital is 43.9442, meaning that the average social capital index in Indonesia is in the low category and the values of Quartile1, Quartile3 for Social Capital are the same, namely 42,5800 which indicate that 75% of companies in Indonesia are in the category of low Social Capital index. The LN audit fees variable has a mean value of 20.0463. Some control variables have the same Q₁, Q₂ and Q₃ values, namely the Loss variable which is at 0.000 meaning that 75% of companies in Indonesia do not have a negative Return on Assets value, while the unqualified opinion variable has the same Q₁, Q₂ and Q₃ values, which is equal to 1, meaning that 75% of the financial statements of companies in Indonesia have an unqualified opinion while the going concern variable has a value of 0.000 for Q₁, Q₂ and Q₃, meaning that 75% of companies in Indonesia have auditors who provide a modified going concern report, while the auditor variable exchange has a value of 0.000 for Q₁, Q₂ and Q₃, meaning that 75% of companies in Indonesia do not change auditors and the Rural variable has a value of 1,000 for Q₁, Q₂ and Q₃, meaning that 75% of companies in Indonesia are in areas with a population density smaller than the median.

4.2 Hypotheses Test

The following are the results of descriptive statistical test from 610 observations obtained from 122 companies listed on the Indonesia Stock Exchange (IDX) in 2015-2019. Hypothesis test is conducted on two groups of data based on the social capital index, namely the low social capital index and the high social capital index. Companies that are included in areas with a low social capital index (38.00-46.81) are companies located in the provinces of DKI Jakarta and Riau, with a total of 95 companies and 475 observations. Companies that are in the areas with a high social capital index (46.82-55.62) are companies located in the provinces of West Java, North Sumatra, Banten, South Sumatra, Central Kalimantan, East Java, and Central Java, with a total of 27 companies and 135 observations.

This study conducts hypothesis testing twice with significant level 5%, which are hypothesis testing for companies in low social capital areas and hypothesis testing for companies in high social capital areas.

Table 2 shows that social capital has a positive effect on audit fees (coefficient 0.006; p-value < 0.000). These results indicate that both the direction and strength of the coefficient for the relationship between audit fees and social capital support the hypothesis. Companies located in areas with a low social capital index pay higher audit fees. This means that companies located in areas with a low social capital index will be charged a higher audit fee. These results support (Jha & Chen, 2015) and the statement of (Jha, 2019) namely that auditors' trust will decrease in companies located in areas with low social capital. Companies located in areas with low social capital tend to manipulate financial statements and auditors would take more time to sign the clients' audit reports, and therefore auditors will increase the audit fees. Table 2 also shows several control variables that have a positive and significant effect on audit fees, namely the Big Four category (coefficient 4.285; p-value < 0.000), Going Concern Assumption (coefficient 5.527; p-value < 0.000). If one company is audited by one of the Big4 PAFs which are qualified in conducting a good audit process, the amount of audit fees will be greater than if the company uses a Non-Big4 PAFs. Table 3 shows the results of multiple regression in companies located in areas with high social capital index. The findings show that social capital has a negative effect on audit fees (coefficient -1.864; p-value 0.044). These results indicate that both the direction and strength of the coefficient for the relationship between audit fees and social capital of companies located in areas of high social capital index support the hypothesis. Companies located in areas with high social capital index pay lower audit fees. These results support Jha, 2013; Jha & Chen, 2015; Yue, 2010; Chen et al. 2021; Sánchez-Ballesta & Yagüe, 2021 who state that managers of companies located in high social capital areas tend to be more honest in financial statements and auditors will have more trust in clients and would eventually make decisions to reduce auditor efforts. In addition to the quality of financial statements, the ease of obtaining objective evidence from stakeholders is also believed to occur in companies that are in the area of a higher social capital. Therefore, the required audit effort is less and audit fees are lower. In addition to Social Capital, other factors that negatively affect audit fees for companies located in areas of high social capital index are Size (Coef -10.550; P-value <0.000) and Debt (Coef -2.878; P-value 0.005).

4.3 Analysis of Covariance (ANCOVA)

To increase the accuracy of the experiment, covariance analysis techniques (ANCOVA) can be used. The analysis of covariance is a method of adjusting for the effects of an uncontrollable nuisance variable and the procedure is a combination of analysis of variance and regression analysis (Montgomery, 2013). The finding shows in Table 4, from the output, it can be seen that the significance figures for the control variables Size, Debt, Big 4, ROA, Going Concern, & Auditor exchange are below the Sig value of 5%, and because the Sig value is <0.05 , then H_0 is rejected. This means that at the 95% confidence level it can be said that there is a linear relationship between Size, Debt, Big 4, ROA, Going Concern, & Auditor exchange with audit fees. This statement indicates that the ANCOVA assumption has been met.

V. Conclusion and Implication

This study motivated by the existing literature, which show that managerial decision and business practices are driven by the social environment. This study analyzes whether the social environment can affect the audit fees. The social environment reflects the company's culture and influences the behavior of managers. Therefore, the social environment will form a trust between the auditor and the managers, and provide an overview to the auditor about the auditor's effort in conducting the audit and the magnitude of audit risk, which leads to the determination of audit fees.

The finding show that social capital has a positive effect on audit fees in companies located in area with low social capital index (coefficient 0.006; p-value < 0.000) that means companies located in areas with a low social capital index pay higher audit fees. And the second findings show that social capital has a negative effect on audit fees in companies located in areas with high social capital index (coefficient -1.864; p-value 0.044) that means companies located in areas with high social capital index pay lower audit fees.

Result of this study consistent with the hypothesis and prove that the company's social capital has an effect on audit fees. For companies located in areas with a high social capital index tend to pay lower audit fees (accountants charge a cheaper audit fee) and vice versa, companies in areas with a low social capital index pay higher audit fees. Companies located in areas with a low social capital index pay higher audit fees. This means that companies located in areas with a low social capital index will be charged a higher audit fee. These results support (Jha & Chen, 2015) and the statement of (Jha, 2019) namely that auditors' trust will decrease in companies located in areas with low social capital. Companies located in areas with low social capital tend to manipulate financial statements and auditors would take more time to sign the clients' audit reports, and therefore auditors will increase the audit fees. Companies located in areas with high social capital index pay lower audit fees. These results support Jha, 2013; Jha & Chen, 2015; Yue, 2010; Chen et al. 2021; Sánchez-Ballesta & Yagüe, 2021 who state that managers of

companies located in high social capital areas tend to be more honest in financial statements and auditors will have more trust in clients and would eventually make decisions to reduce auditor efforts

This study has several limitations, such as: first, this study assumes that the social capital index is relatively stable every year so that the 2014 index published by the Statistics Indonesia is used to analyze its effect on audit fees for 5 years (2015-2019). Although this assumption is supported by (Anheier, Gerhards, & Romo, 1995) and (Jha & Chen, 2015), this assumption might be inaccurate and might affect the results. Future studies are advised to re-test if a new social capital index has been published or conduct an independent calculation to obtain the social capital index. To gain another perspective on social capital, future research may also measure social capital by reflecting on factors of social deviance, such as crime rates (robbery, divorce, and other cases). Second, the short period of observation (5 years) and the proportion of samples that are not balanced between companies located in areas with high and low social capital, namely 22% (N = 135) and 78% (N = 475) which might reduce the power of statistical tests. Therefore, future studies may extend the years of observation. Future studies can analyze other non-financial variables that can affect audit fees, misalnya budaya lokal and also analyze the impact of social capital on dysfunctional behavior in accounting, such profits management and budget gaming. Future studies are also suggested to control for known client-specific, auditor-specific, audit-specific and country-specific assignments.

This study contributes to both theoretically and practically by showing that the social environment can form a trust between auditors and clients, and have an impact on the determination of audit fees. To our knowledge, this is the first study in Southeast Asia directly examine the relationship between social capital and audit fees. This study also complements studies that investigate how variations in socio-economics factors, such as social capital, affect managerial decision making, especially in the field of auditing.

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Acknowledgments

APPENDIX

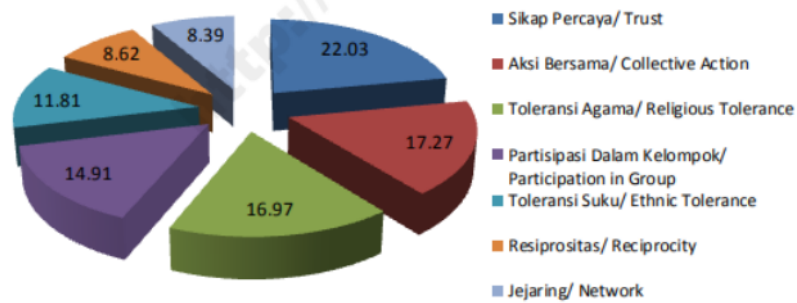


Figure 1. Contribution of Each Factor of Social Capital Index, 2014

Source: <https://www.bps.go.id/>

Table 1. Descriptive Test Results

Variables	Mean	Median	Std. Deviation	Quartile	
				1	3
Social Capital	43.9442	42.5800	3.0584	42.5800	42.5800
Ln Audit Fees	20.0463	20.3376	2.7952	19.5193	21.1631
Size	16.1933	15.2980	3.7060	14.3287	16.6464
Debt	3.2091	2.1226	3.3184	1.5852	3.3460
ROA	0.0435	0.0324	0.1567	0.0041	0.0775
Big 4	0.4311	0.0000	0.4956	0.0000	1.0000
Loss	0.1918	0.0000	0.3940	0.0000	0.0000
Days To Sign	82.9082	80.0000	51.7146	61.0000	87.0000
Public Exchange	0.6885	1.0000	0.4635	0.0000	1.0000
Unqualified Opinion	0.9885	1.0000	0.1066	1.0000	1.0000
Going Concern	0.1590	0.0000	0.3660	0.0000	0.0000
Inherent Risk	0.3043	0.2042	1.0989	0.0888	0.3567
Auditor Exchange	0.1557	0.0000	0.3629	0.0000	0.0000
Cost Of Living	300566	310000	755262	270000	364803
	5	0		0	5
Rural	0.9590	1.0000	0.1984	1.0000	1.0000
Ln Pop	16.3596	16.1548	0.5931	16.1482	16.1724
Pop G	0.0103	0.0090	0.0034	0.0086	0.0125

Source: Output Statistic Descriptive

Table 2. Hypothesis Test Results - Low Social Capital Index

Dependent Variable: Audit Fees

Low Social Capital Index (DKI Jakarta and Riau)

Variables	Coefficient	P-value
SOCIAL CAPITAL	0.006	<0.000**
SIZE	-8.433	<0.000**
DEBT	-1.117	0.265
ROA	-0.600	0.549
BIG 4	4.285	<0.000**
LOSS	0.817	0.415
DAYS TO SIGN	-0.344	0.731
PUBLIC EXCHANGE	-0.309	0.758
UNQUALIFIED OPINION	-0.761	0.447
GOING CONCERN	5.527	<0.000**
INHERENT RISK	-1.176	0.240
AUDITOR EXCHANGE	-2.554	0.011*
COST OF LIVING	0.163	0.871
LN POP	-0.003	0.998
POP G	0.274	0.784

Source: Output Multiple Regression Analysis (**p-value<1%, *p-value<5%)

Table 3. Hypothesis Test Results - High Social Capital Index
Dependent Variable: Audit Fees
High Social Capital Index (West Java, North Sumatra, Banten,
South Sumatra, Central Kalimantan, East Java, Central Java)

Variables	Coefficient	P Value
SOCIAL CAPITAL	-1.874	0.044*
SIZE	-10.550	<0.000**
DEBT	-2.878	0.005**
ROA	4.012	<0.000**
BIG 4	0.580	0.564
LOSS	2.564	0.012*
DAYS TO SIGN	0.320	0.750
PUBLIC EXCHANGE	2.815	0.006**
GOING CONCERN	5.107	<0.000**
INHERENT RISK	-1.836	0.070
AUDITOR EXCHANGE	1.616	0.110
COST OF LIVING	-1.328	0.188
RURAL	0.343	0.732
LN POP	-1.674	0.098
POP G	-0.724	0.471

Source: Output Multiple Regression Analysis (**p-value<1%, *p-value<5%)

Table 3. Hypothesis Test Results - High Social Capital Index
Dependent Variable: Audit Fees
High Social Capital Index (West Java, North Sumatra, Banten,
South Sumatra, Central Kalimantan, East Java, Central Java)

Variables	Coefficient	P Value
SOCIAL CAPITAL	-1.874	0.044*
SIZE	-10.550	<0.000**
DEBT	-2.878	0.005**
ROA	4.012	<0.000**
BIG 4	0.580	0.564
LOSS	2.564	0.012*
DAYS TO SIGN	0.320	0.750
PUBLIC EXCHANGE	2.815	0.006**
GOING CONCERN	5.107	<0.000**
INHERENT RISK	-1.836	0.070
AUDITOR EXCHANGE	1.616	0.110
COST OF LIVING	-1.328	0.188
RURAL	0.343	0.732
LN POP	-1.674	0.098
POP G	-0.724	0.471

Source: Output Multiple Regression Analysis (**p-value<1%, *p-value<5%)

Table 4. Analysis of Covariance Result

Variables	Sig
SIZE	0.000
DEBT	0.000
ROA	0.678
BIG 4	0.000
LOSS	0.513
DAYS TO SIGN	0.437
PUBLIC EXCHANGE	0.083
GOING CONCERN	0.000
UNQUALIFIED OPINION	0.642
INHERENT RISK	0.414
AUDITOR EXCHANGE	0.009
COST OF LIVING	0.497
LN POP	0.702
POP G	0.718

Source: Output ANCOVA

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