FACTORS AFFECTING THE INTEGRITY OF FINANCIAL STATEMENTS

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Abstract

Financial statements can be a powerful way to disseminate information about a company's finances or operations. Alchian's (1950) evolutionary theory of economic change posits that market forces will naturally regulate businesses. This compiles and analyzes the empirical evidence to empirically explore, from an Indonesian perspective, how corporate governance, internal audit quality, and external pressures interact to affect the integrity of financial statements. Quantitative methods were used for this investigation. This information comes from a secondary source. The researchers here used a systematic sampling strategy called purposive sampling. This study used data from 96 samples collected over the course of three years. In this study, the researchers employed the panel data analysis technique with the help of the EViews software. Corporate governance is examined through the lenses of institutional ownership, managerial ownership, audit committees, and the proportion of independent commissioners. Financial statement integrity was found to be significantly affected by independent commissioners but not by institutional ownership, managerial ownership, or audit committees. The consistency of the financial statements is unaffected by either the quality of the internal audit or any external pressures. Managers are careful not to artificially inflate company profits in order to keep institutional investors happy, as they own a disproportionately large share of the company's stock. This means that the stability of financial statements improves as institutional and managerial ownership grows.

Keywords: Financial Statements, Integrity, Corporate Governance, Institutional Ownership, Managerial Ownership, Audit Committees, Independent Commissioners

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1. INTRODUCTION

Accounting processes make financial statements, which are a way to share a company's financial information with all the people who are interested. Gorety (2017) states financial statements are to obtain financial information about the company that is used by various parties that will help the company in making decisions. Solikhah (2017) states that financial statements can be called a description of the financial condition of a company, therefore financial statements must be presented honestly and correctly. Kieso et al. (2017) see financial statements as a form of accountability and understandability, relevance, and reliability, and can be compared. Financial reports must also be easy to understand so that information is conveyed to the readers. Financial statements must also be relevant so that the information can be useful for evaluating past events. The information contained within financial statements must also be accurate and truthful, without any potential for misinterpretation or material error. Financial statements must also be able to be compared between existing periods to identify the performance of the company. Fitrawansyah and Syahnifah (2018) claim that the integrity of financial statements is a measure of whether the financial statements presented can provide honest and correct information.

So that the results reported at the end of the financial year give the impression that the company is doing well as a whole, management is expected to get as much as possible out of the information in financial reports to improve operational activities. The honesty and truthfulness of accounting data presented in financial statements are very important because they can affect decision-making for users of financial statements (Gorety, 2017). However, many managements also commit fraud, which is where management manipulates financial statements. This causes the financial statements to be less reliable because the information presented does not reflect the actual condition of the company and is definitely irrelevant for parties who have an interest in making decisions because of inaccurate information. Based on research conducted by Permatasari et al. (2019), it was found that companies in Indonesia indicated that they were manipulating financial statements that could be measured using earnings management. Compared to other ASEAN countries, Indonesia is considered to be the largest country by the level of earnings management. Solikhah's (2017) research also shows the results that companies in Indonesia still manipulate financial data a lot in order to avoid reporting annual losses.

The existence of cases of manipulation of accounting data occurred in several large companies such as the phenomenon that occurred recently, namely PT Tiga Pilar Sejahtera Food manipulated the company's financial statements in 2017 with the aim of increasing the company's share price at that time. Manipulation of financial statements was carried out by increasing the receivables of six distributors from Rp. 200 billion to Rp. 1.6 trillion. Another case is from the Enron corporation, where the company soared the company's profit value of US$74 billion. The American company also hides losses and debts by using the off-balance sheet method in preparing financial statements. In the end, Enron was declared bankrupt in 2001. Next happened to the Toshiba company in 2015, where the company overstated a total of US$2.22 billion, this is because Toshiba executives set unrealistic targets. Not only that, PT Garuda Indonesia, after doing research, it turns out that this case involves many parties. The disclosure of cases like this reduces public trust in the company. It can be seen from the decline in the share price of the company. The Securities and Exchange Commission appointed three former executives of Power Solution Inc. Over the alleged overstating of the company's revenues of nearly US$25 million. In order to meet analyst expectations and keep information from the company's auditors, these three people helped the company wrongly record revenue for unfinished sales.

In cases of manipulated accounting data, it is proven that there is a lack of integrity of financial statements in presenting information to users of financial statements. According to Nurdiniah and Pradika (2017), many companies do window dressing or what can be called "beautifying financial statements" due to pressure from investors who want to get large returns because of the investment risks. This problem that arises raises many questions for various parties, especially regarding the company management system and the ownership system which is known as "corporate governance". The application of poor corporate governance can be a reason to encourage accounting manipulation in which the management presents information that has a positive impact and encourages companies to manipulate it to avoid falling stock prices (Gorety, 2017). From this case of manipulation of financial statements, it will be detrimental to the public as users of the information, because the public does not get the actual information.

The practice of good corporate governance, or what is referred to as good corporate governance, seeks to highlight the significance of shareholders' rights to accurate and truthful information. According to Herawaty and Susiana (2007), the implementation of excellent corporate governance mechanisms in a corporation might lead to information being provided by the company or management that is at odds with the current reality. These cases of financial data manipulation are actually not only parties from within the company who are responsible but many external auditors are involved. Many external auditors are involved in cases of manipulation of accounting data. The position of public accountants who are considered third parties, who will provide fairness opinions on financial statements, and the public accounting profession is a profession that is trusted by the public as users of financial statements. The accounting profession itself has an important role in presenting reliable financial statement information for various parties such as the government, investors, creditors, shareholders, debtors, and other parties who have an interest in the financial statements. Of the many cases of manipulation of accounting data involving auditors who provide an assessment of the financial statements raises questions to the public about the quality of the audit provided. In addition, external pressure can also affect financial integrity.

According to Ijudien (2018), external pressure can be interpreted as excessive pressure for management to meet the requirements or expectations of third parties. The author's reason for choosing a manufacturing company is because of the recent outstanding cases, namely from PT Tiga Pilar, where PT Tiga Pilar itself is a manufacturing company in the consumption sector. Therefore, the author is interested in choosing a manufacturing company in the consumption sector.

The results of the study by Tussiana and Lastanti (2016) show that audit quality has a positive effect on the reliability of financial statements. Hardiningsih (2010) shows that the quality of the audit does not have a big effect on how honest the financial statements are. Users of financial statements are more likely to trust financial statements that have been audited by a public accounting firm with a good reputation. The goal of this study is to add to what Qonitin and Yudowati (2019) found about how corporate governance practices and audit quality affect the integrity of financial statements in mining companies listed on the Indonesia Stock Exchange.

Manufacturing companies are large-scale businesses compared to other businesses, researchers picked manufacturing companies listed on the Indonesia Stock Exchange as their research subjects and samples for this reason. There are quite a number of manufacturing companies, having various types of operating sectors, and a large scale of activity compared to other types of companies so it is expected to be able to make this research obtain accurate and reliable results. Stocks of manufacturing companies can withstand downturns in the economy. This is because there is very little risk of loss because most manufactured goods are still needed.

The difference between this study and previous research is that, first, it adds an independent variable for the proxy for corporate governance mechanisms, namely managerial ownership, and is based on suggestions from previous research. The reason is that the management of companies that have a percentage of share ownership will tend to have greater responsibility in running the company. Management reports financial statements with true and honest information so that they have high integrity of financial statements (Saksakotama & Cahyonowati, 2014). Second, previous studies used the mining sector while this study used manufacturing companies in the consumption sector. The reason for choosing the manufacturing sector is that manufacturing companies have the highest percentage that gets a special notation from the Indonesian Stock Exchange. Companies that get a special notation indicate that the financial statements are less relevant so the integrity of the financial statements will be reduced. This research is expected to be used as a reference to increase insight and knowledge in the field of accounting, as well as useful for providing consideration for investors or capital analysts in assessing a company related to investment decision-making.

The goal of this study is to show how corporate governance mechanisms, audit quality, and pressure from the outside affect the integrity of financial statements. The contribution of this research is expected to increase the knowledge of corporate management to improve the implementation of good corporate governance in the corporate environment so that good corporate governance is implemented. This research is also expected to enrich the knowledge and insight of users of financial statements regarding the factors that affect the integrity of financial statements so that users can use financial statements as a consideration in making decisions. Based on the description above, the researchers are interested in conducting a study on matters that affect the integrity of financial statements. This study aims to analyze the effect of corporate governance mechanisms, audit quality, and external pressure on the integrity of financial statements.

The remainder of this paper is structured as follows. Section 2 is the pertinent literature review. The approach utilized to conduct an empirical study on the impact of corporate governance, audit quality, and outside pressure on the integrity of financial statements is analyzed in Section 3. Section 4 presents a study of the data, findings, and discussion. The conclusion, key findings, research implications, and limitations are included in Section 5.

2. THEORETICAL FRAMEWORK

2.1. Agency theory

In the 1970s, Jensen and Meckling (1976) developed the agency theory. According to Jensen and Meckling (1976), a trust relationship is a contract in which one or more persons (the principals) hire another person (the agent) to run their business and give them the authority to choose the best course of action. The core of agency theory is the creation of proper contracts to align the interests of management and owners in the event of a conflict of interest. According to Gorety (2017), agency theory helps to understand how a company's owner and management interact (principal). The chosen management must give the business's owner an account of the outcomes of their efforts. A mutually advantageous employment agreement outlines the rights and obligations of the business's owner and management. According to Jensen and Meckling (1976), there are two issues with agency: 1) moral hazard, where issues will arise if the agent does not carry out what has been mutually agreed upon in the employment contract, and 2) adverse selection, where the owner of the business is unable to determine whether a decision made by the management is correct based on the information obtained or occurs as a result of an omission in performing his duties.

Managers can mislead company researchers by giving them financial statements that do not match what really happened. This is possible because management and the company do not always have the same information. When the owner's financial information is not consistent with the business's economic performance, the management will appear to be carrying out their duties well, but in fact, the performance of the management is very poor. Therefore, this agency theory aims to explain where corporate governance has direct involvement with company owners.

2.2. Hypotheses development

This research is based on previous studies that state that corporate governance mechanisms and audit quality affect the integrity of a company's financial statements.

2.2.1. The effect of corporate governance mechanisms on the integrity of financial statements

Solikhah (2017) states that institutional ownership can be measured by the percentage of the shares owned by an institution divided by the outstanding shares. Institutional ownership is the percentage of voting rights owned by an institution. According to Wulandari and Budiartha (2014), the process of compiling financial statements might be impacted by the percentage of specific shares held by institutions, which does not preclude the potential for accrual in line with management objectives. Institutional investors' ownership over the company may urge managers to pay more attention to the business's performance, which will help to curb opportunistic or selfish behavior.

Jama'an's (2008) research shows that institutional ownership has a big effect on how accurate financial statements are. Managerial ownership is the division of ownership between those who are employees of the company and those who are not. If a corporation has a large number of shareholders, a huge number of people cannot actively participate in the management of the company. Widyaningsih (2017) defines managerial ownership as the proportion of a company's stock that is owned by the board of directors.

Institutional ownership and managerial ownership are related to agency theory because share ownership owned by institutions and management is expected to be able to reduce agency problems by aligning the interests of those who have interests with those of company managers, as there is a sense of shared ownership, managers are expected to act in the best interests of the owners. This allows them to be more careful and reduces the chance of financial information reporting fraud while also making the financial statements more accurate. The results of Widodo's (2016) study show that managerial ownership has a big effect on how accurate financial statements are. Solikhah's (2017) research shows different results. The author comes to the conclusion that managerial ownership has little to no effect on the integrity of financial statements. The board of directors sets up the audit committee as a body or committee whose job is to keep an eye on the external audit and financial reporting processes without being involved in them. The audit committee collaborates with the board of commissioners in a professional and independent manner to strengthen and support the board of commissioners in performing the audit supervisory function (Parinduri et al., 2019). The audit committee's purpose and duty in financial reporting is to oversee and monitor the financial statements' auditing process to make sure that it adheres to the requirements.

The audit committee also has a relationship with agency theory because the supervision of the audit committee will provide oversight and monitoring to the management in reporting financial statements honestly. Solikhah (2017) shows the audit committee should keep a closer eye on management actions that make it possible to change financial statements and hurt the reliability of financial statements. Audit committees in companies can be a way to reduce the chance of fraud in the way financial statements are presented. The integrity of financial statements is not significantly impacted by the audit committee. In contrast, according to a study by Jama'an (2008), the audit committee significantly affects the integrity of financial statements.

According to Widyaningsih (2017), an independent commissioner is a member of the board of commissioners who is not connected to management, other commissioners, or shareholders. They also have no business ties or other connections that would make it hard for them to be fair. Meanwhile, Gorety (2017) defines the independent commissioner as the party in charge of assessing the company's overall performance. With the supervision of an independent commissioner, it is hoped that the management will not have the freedom to determine the accounting principles used so that the management can apply conservative accounting principles in the preparation of financial statements.

According to Gorety's (2017) research, independent commissioners have a big impact on financial statements' credibility. Meanwhile, in a study conducted by Yasmeen and Hermawati (2015), independent commissioners do not have a significant influence on the integrity of financial statements. The agency theory holds that there is a separation between management and shareholders which can cause different interests and have an impact on the presentation of the company's financial statements (Kusumo & Meiranto, 2014). So, it is necessary to implement a mechanism that can minimize differences in interests between management and company owners or investors. Board independent commissioner is a party who is not related or related to any relationship with the board of directors or member of the board of commissioners in the company which could interfere with an independent commissioner. As is oversight by the council's independent commissioner expected shareholder interests can be maintained.

Abor and Biekpe (2007) and Kyereboah-Coleman and Biekpe (2006) discovered a link between board independence and business profitability. Independent boards of commissioners have a detrimental impact on return on assets (ROA), according to a study by Christensen (2011). The study demonstrates that a large number of independent commissioners can lower profitability. The ownership structure is a tool that can help make sure that shareholders' and managers' interests do not clash too much. The ownership structure mechanism that is seen as a technique to lessen information asymmetry between insiders and outsiders through information disclosure in the capital market under the information imbalance approach. The concentration of ownership is one corporate governance strategy that can be utilized to balance the interests of principals and agents. Demsetz and Lehn (1985) concentrated ownership,

so the principal has a way to monitor the agent so that the agent acts in accordance with the interests of the principal. The percentage of share ownership in a company will determine the level of control over company management. According to Shleifer and Vishny (1997), company owners with a large percentage of ownership can carry out supervision because they can obtain information and have voting rights that can control management.

Corporate governance companies in this study use the existence of independent commissioners and boards of directors are expected to be able to balance the decision-making process, especially in the integrity of information in financial reports. In July 2001, the Indonesian government passed a law that set up an independent board of commissioners and an audit committee. This was done to protect shareholders and increase public trust (Perwitasari & Septiani, 2014). Beasley (1996) and Evans et al. (2002) showed that independent commissioners or businesses do not have much of an effect on performance. The integrity of financial statement information is the condition that the information in the financial statements is presented fairly and cannot honestly portray what is meant to be represented, according to Statement of Financial Accounting Concept No. 2 (Financial Accounting Standards Board [FASB], 1980). According to Jama'an (2008), the accounting data must be reliable, objective, and relevant. Many small and large-scale businesses present financial data with a low level of integrity, where the data is skewed and unsuitable for some financial statement readers (Astria & Ardiyanto, 2011).

In the corporate governance system, the board of directors and independent commissioners are very important. They set the company's policies and protect investors over the short and long term (Ajija et al., 2011). The results of Yermarck's (1996) empirical study showed that the board of directors usually has no effect on how well a company does and does not change the integrity of financial statements. The board of commissioners' function in a firm is more of a monitoring one than it is one of carrying out the policies of the directors. In order for the board of commissioners to be able to check how well the directors are looking out for the interests of shareholders (Krisnauli & Hadiprajitno, 2014), the company's financial statements need to be accurate (Augustine, 2012). Institutional ownership is the number of shares that outside organizations, businesses, insurance companies, banks, or other institutions own at the end of the accounting period (Bukhori & Rahardja, 2012).

Managerial conduct in control and decision-making can be restricted by keeping an eye on the acts taken by a firm and other institutional shareholders (Tehranian et al., 2006). Beiner et al. (2004) assert that to improve corporate governance by ensuring that the company has one or more large shareholders. Solomon and Solomon (2004) state that aligning the interests of management with those of shareholders by using institutional shareholders' power over management can be very helpful.

Jensen and Meckling (1976) stated that share ownership by management can help unite the interests of internal companies and investors. The better the performance of the company, the more the proportion of management share ownership will be. Contrary to Hermalin and Weisbach's (1991) research, the greater the percentage of management ownership, the lower the integrity of financial reports. Riduwan and Sari (2014) explain that "managerial ownership" means that the people who run a company own shares in it. Setia et al. (2020) say that managers care much more about the interests of shareholders in a company with strong managerial ownership and that stock options are a way to get the company to help. Benefits for the organization will result from managerial ownership. Nabor and Suardana (2013) state the value of ownership management below 10% is a low percentage of share ownership so that management is not able to influence company policy, especially in the integrity of a financial report. Shares with small percentages are vulnerable to agency problems so it will improve financial reports conservatively (LaFond & Roychowdhury, 2007). Transparency and openness are expected to be achieved if there is managerial ownership in the company. With more managers owning shares, it is anticipated that they will behave in accordance with the principal's desires because they will be incentivized to enhance performance. This is because they have control over making company policies. The percentage of shareholders from management that actively engage in company decisions made by directors and commissioners is known as management ownership (Sudiyanto & Husaini, 2016). The management will tend to endeavor to improve company performance, and the quality of financial reporting reported by managers will be better the more ownership the management has in the company (Oktaviani et al., 2015). This is consistent with a study by Khafid and Arief (2017) that found managerial ownership had a favorable impact on firm earnings. Based on the above description, the researchers hypothesize that managerial ownership has an effect on earning quality.

The need for more information will increase supervision carried out by institutions so that management opportunities to manipulate financial information are minimal and the profits presented are of higher quality (Octaviani, 2018). Anggraini (2010) says that institutional ownership is one of the things that can lessen agency conflict. For the agency costs that occur within the firm to reduce and the value of the company to also increase, the stronger the amount of control exercised by outside parties over the company, the higher the institutional ownership level. The size of the commissioners greatly influences the effectiveness of the communication and coordination processes among the members of the commissioners, so that the supervisory process that is played becomes more optimal (Mustaqomah, 2011). The board of commissioners is appointed by the majority shareholder at the general meeting of shareholders so that it represents the owner's decision. As a result, the board of commissioners has a sizable membership in practice. The board of commissioners' role in performing the oversight function of the company's operations by management has effectively contributed to the outcomes of the process of preparing quality financial reports or the possibility of avoiding fraudulent financial statements in order to limit and suppress earnings

management by the company (Sari, 2017). The board of commissioners has a favorable impact on the earning quality, according to studies by Pratama and Sunarto (2019), Oktaviani et al. (2015), Arniati et al. (2019), and Khafid and Arief (2017). Corporate governance in this study uses board independence and ownership structure, the hypothesis is as follows:

H1: There is an effect of board independence and ownership structure on the integrity of financial statements.

2.2.2. The effect of audit quality on the integrity of financial statements

According to Hardiningsih (2010), an auditor's ability to find irregularities in the client's accounting system and disclose them in the audited financial statements depends on the auditor's ability to do his tasks. A large public accounting firm with excellent auditors has a very good reputation. Auditors will undoubtedly conduct themselves professionally so that they can personally attest to the integrity of the financial statements. As an auditor, apart from having to take formal education, you also have to undergo sufficient technical training to cover technical aspects, as well as general education. In the principal and agent relationship, a mediator is needed as a specialist auditor who provides good audit quality. In contrast to research by Widodo (2016) and Solikhah (2017), which claim that audit quality has no significant impact on the integrity of financial statements, Hasanudin (2018, as cited in Srikandhi and Suryandari, 2020) finds that it has a significant impact on the integrity of the financial statements.

Internal auditing is the process through which a company's internal audit division examines its financial statements and accounting records, as well as whether specified top management policies, governmental rules, and provisions from relevant professional associations are being followed (Agoes, 2013). Companies will employ internal audits as objective, independent assurance and consulting work to enhance organizational operations and help disciplines and organizations assess and enhance the efficacy of risk management, control, and governance procedures (Amin, 2016). The company's success is measured by its financial performance, which is a reflection of the numerous operations that have been undertaken. Assessment of financial performance in a company requires an internal audit in order to find out the actual condition of the company. Internal audit in a company is useful to help oversee the course of company activities, especially in financial performance, this is done to avoid a decrease in financial performance. Sidik (2014) shows that an internal audit in a company has an effect on financial performance where there is a strong correlation with financial performance. Also, Rajagukguk's (2017) research shows that internal auditing and preventing fraud have a big effect on how well a business does financially.

To enhance the quality of financial reporting, which was hitherto entirely management's duty, the role of the internal audit function has increased. Using the internal audit function as a source of information about how different parts of an organization work helps people make decisions that are fair and responsible. Internal audit, according to Messier et al. (2005), is activity-independent objective assurance and consulting designed to add value and improve organizational operations. The better the role of internal audit in the company, the higher the quality of the financial reports that will be produced by the company. Because internal auditors have extensive knowledge about various aspects of the company or also known as the company's internal controls so that they can detect fraudulent financial reporting effectively. The involvement of the internal audit function in the financial reporting process results in greater transparency in the company's operations. Susanto (2003) explains that internal audit plays a role in compliance management, especially in order the company's internal control, where false one objective of the control process of internal audit is so that reports can be trusted finance. Another research, conducted by Widyaningsih (2017), obtained results that internal audit has an effect on the effectiveness of internal control of production costs.

Meanwhile, other previous studies are in line with the research conducted by Sundayani (2013). This research obtained the result that the internal audit influences the implementation of good corporate governance (GCG), where one of the components of GCG is the company's internal control related to financial reporting quality so that the financial statements are presented reliably. Therefore, the hypothesis that can be taken is as follows:

H2: There is an effect of internal audits on the integrity of financial statements.

2.2.3. The effect of external pressure on the integrity of financial statements

According to SAS No. 99, external pressure is the pressure placed on management to satisfy the demands or expectations of outside parties. Causes of external pressure include obligations to pay debts, adhere to debt agreements, or satisfy listing requirements (Skousen et al., 2009). This pressure will trigger management to manipulate financial statements. Management will use all reasonable efforts to get loans and make every effort to publish accurate financial reports so that their performance is also regarded as accurate (Sari & Nugroho, 2020). External pressure is also closely related to agency theory, because agency theory explains the relationship between the principal as the owner of capital and the agent as the one who runs the company, with this external pressure, companies whose capital is mostly held by third parties, of course, the company management always want good company reports so that third parties will continue to invest in the company. Previous research conducted by Ozcelik (2020), Agusputri and Sofie (2019), Bayagub et al. (2018), Akbar (2017), Pusphita and Yasa (2018), and Putriasih et al. (2016) showed that the results of external pressure have a significant effect on the integrity of financial statements. Listyaningrum et al.'s (2017) research shows that external pressure does not have a big and positive effect on fraudulent financial reporting.

External pressure is pressure that comes from outside the regional apparatus organization such as regulations, executives, society, and so on. The existence of external pressure can result in the practices of regional apparatus organizations which are only a formality to gain legitimacy. This study talks about how to apply transparency in financial reporting (Basuki & Ridha, 2012). External pressure to adopt a structure or system is known as coercive power and is used by the government, rules, or other institutions (Ashworth, 2009, as cited in Arsyad, 2012). The coercive power of a regulation, on the other hand, can cause an organizational tendency to gain or improve legitimacy (legitimate coercion) (Scott, 2008, as cited in Arsyad, 2012), thus only emphasizing the positive aspects (Hess, 2007, as cited in Arsyad, 2012), so that organization looks good to parties outside the organization. According to Arsyad (2012), one of the elements influencing the adoption of financial reporting transparency is external pressure. According to Frumkin and Galaskiewicz (2004), external influences, particularly those connected to the implementation of a policy or procedure, might diminish the degree of governmental competence. Frumkin and Galaskiewicz (2004) explain that a low level of government capability could be caused by pressure from the outside, especially when it comes to putting a policy or procedure into place. Studies on the impact of external pressure on financial reporting transparency by Basuki and Ridha (2012), Satriawan and Sihaloho (2014), and Hadi and Hastuti (2015) demonstrate that external pressure, in the form of regulations and policies that prompt the implementation of financial reporting transparency, has a positive impact. The same variable was explored by Julita and Belian (2015) and Yusrawati and Dewi (2015), with the findings that external pressure had no impact on the implementation of financial reporting transparency. Based on this description, the following hypothesis can be formulated:

H3: There is an effect of external pressure on the integrity of the financial statements.

3. RESEARCH METHODOLOGY

3.1. Sample and data collection

According to Sugiyono (2017), the aim of the study is the scientific objective to gather data about something with certain goals and uses. The authors of this study collected samples from manufacturing firms in the consumer sector that were listed on the Indonesia Stock Exchange (IDX) in 2018–2020. Researchers chose to obtain it through the IDX because it has complete, accurate, and organized data. This study has a dependent variable and independent variables. The independent variables in this study include corporate governance mechanisms (*X1*), audit quality (*X2*), and external pressure (*X3*), while the dependent variable taken in this study is financial statement integrity. All manufacturing businesses that were listed on the IDX in 2018–2020 were considered in this study. The non-probability sampling methodology combined with the purposeful sampling method was the choice for data sampling in this study. According to Sekaran and Bougie (2016), non-probability sampling is a strategy in which the components of a population have no chance of being chosen as sample subjects. Purposive sampling, on the other hand, is a method for carrying out deliberate sampling based on particular criteria picked by the authors. The criteria set are:

1. Manufacturing companies in the consumption sector listed on the IDX in the 2018–2020 period and publishing annual reports.
2. Financial statements are presented in rupiah (Rp).
3. Companies that are not newly listed during the 2018–2020 period.
4. Annual reports of manufacturing companies that have complete financial data related to research variables.

From the criteria above, the number of samples used in this study was 96 of 138 companies obtained with 3 years of observation.

The sample collection methods used in this study are:

1. *Literature study:* Library research is a study that is used to collect information and data obtained through existing books, scientific journals, and official websites. According to Santosa (2020), library research is an activity to collect information that is relevant to a topic or problem that is the object of a study.
2. *Documentation:* Santosa (2020) explains that the documentation method is a way to get information from transcripts, newspapers, books, and other materials that already exist or have been saved. Some data will be gathered for this study from the financial reports of manufacturing businesses that were audited and released by the IDX between 2017 and 2019. The information collected, gathered, and compiled will be studied by the authors.

3.2. Variable operations

3.2.1. Independent variables

According to Fajaryani's (2015) research, the conservative index is used to gauge the integrity of a financial statement. The use of the conservatism index is a result of conservatism, which shows understated financial statements when understated financial statements carry less risk. Beaver and Ryan (2000) and Fajaryanti (2015) employed a number of measurement models, one of which was the adoption of a market-to-book ratio, which reflects the relative market value of the company's book value. Because the corporation records a company value that is lower than its market value, a ratio greater than 1 denotes the practice of conservative accounting. The measurement model to be used is as follows:

$$ILK_{it} = \frac{Stock\ market\ price}{Stock\ book\ value} \quad (1)$$

where, ILK_{it} is the integrity of the company's financial statements in year *t*.

3.2.2. Corporate governance mechanism

Sulistyanto and Prapti (2003) view the corporate governance mechanism as a system that controls and regulates a company in order to provide added value. This variable is measured using four variable dimensions, namely:

1. *Institutional ownership:* The percentage of shares owned by externals or persons outside of an institution at the end of an accounting period is known as "institutional ownership". Institutional ownership has a part to play in regulating how management behaves so that the integrity of financial statements is appropriately upheld. A formula utilized in the studies by Fajaryani (2015) and Gorety (2017) is used to calculate this institutional variable, namely:

$$INST = \frac{Number\ of\ shares\ owned\ by\ the\ institution}{Total\ shares} \times 100 \quad (2)$$

2. *Managerial ownership:* Managerial ownership is the number of a company's shares that are owned by management or other people inside the company who help make decisions. Managerial ownership seeks to restrict managerial actions that might be harmful to the organization. The ratio of the manager's ownership of shares to the total number of outstanding shares is used to determine managerial ownership. Research by Fajaryani (2015) and Gorety (2017) employs the following formula:

$$MAN = \frac{Number\ of\ shares\ owned\ by\ management}{Total\ shares} \times 100 \quad (3)$$

3. *Audit committee:* Grotery (2017) explains that the audit committee is a part of corporate governance that helps the board of commissioners by improving how well internal and external audits work and how good financial reports are:

$$KMA = Number\ of\ all\ audit\ committee\ members \quad (4)$$

4. *Independent commissioner:* The independent commissioner is in charge of making sure that the organization uses corporate governance principles. He or she does this by paying the board of commissioners so that they can supervise, advise, and add value to the business in an effective way. Gorety (2017) explains that having a board of commissioners can make financial reporting better and reduce the amount of management engineering. The independent commissioner variable in this study was calculated using the same formula as in Fajaryani's (2015) and Gorety's (2017) research:

$$KI = \frac{Number\ of\ independent\ commissioners}{The\ total\ number\ of\ members\ of\ the\ board\ of\ commissioners} \quad (5)$$

5. *Audit quality:* According to Widodo (2016), the auditors of the four major public accounting firms have access to a variety of research methods, techniques, and audit tools that are thought to be more accurate than those used by smaller companies, these firms are also regarded as having more qualified auditors. Seen from the public accounting firm where they work. In Guna and Herawaty (2010), Gorety (2017), and Widodo (2016), audit quality can be measured using a dummy variable where public accounting firms (*kantor akuntan publik* — KAPs) will be divided into two, namely Big Four KAPs and non-Big Four KAPs. Large KAPs, such as the Big Four are considered to maintain their independent auditor attitude compared to non-Big Four KAPs. This variable is measured by the Big Four KAP proxy using a nominal scale with a dummy variable as in previous studies. Where the number 1 will be given if the auditor conducting the audit is an auditor from the Big Four KAP and 0 if it is from a non-Big Four KAP.

The Big Four KAPs used in this study are:

1. PricewaterhouseCoopers (PwC) with partners in Indonesia.
2. Deloitte Touche Tohmatsu with partners in Indonesia.
3. Klynevld Peat Marwick Goerdeler (KPMG) International, with partners in Indonesia.
4. Ernst & Young (EY) with partners in Indonesia.
5. External pressure.

Third-party pressure or external pressure is the pressure felt by the management to obtain sources of funds such as debt and capital from parties outside the company. According to Yesriani and Rahayu (2017), external pressure is excessive pressure for management to meet the requirements or expectations of third parties. In this study, the external pressure variable was measured using the formula used in Agusputri and Sofie's (2019) research as follows:

$$Lev = \frac{Total\ liability}{Total\ assets} \quad (6)$$

4. RESULTS AND DISCUSSION

In this study, the method that will be used to analyze the data is the panel regression analysis technique. According to Ahmaddien and Susanto (2020), this panel data regression analysis technique is an analytical technique that combines time series and cross-section data, which is supported by available quantitative data. Regression analysis of panel data is used to describe the variables that might affect the integrity of financial statements, namely corporate governance mechanisms, audit quality, and external pressures.

4.1. Classic assumption test

Before continuing the research, the classical assumption test is carried out first to ensure that the regression equation used is correct. In this case,

there are four forms of classical assumption testing, namely: normality test, multicollinearity test, heteroscedasticity test, and autocorrelation test.

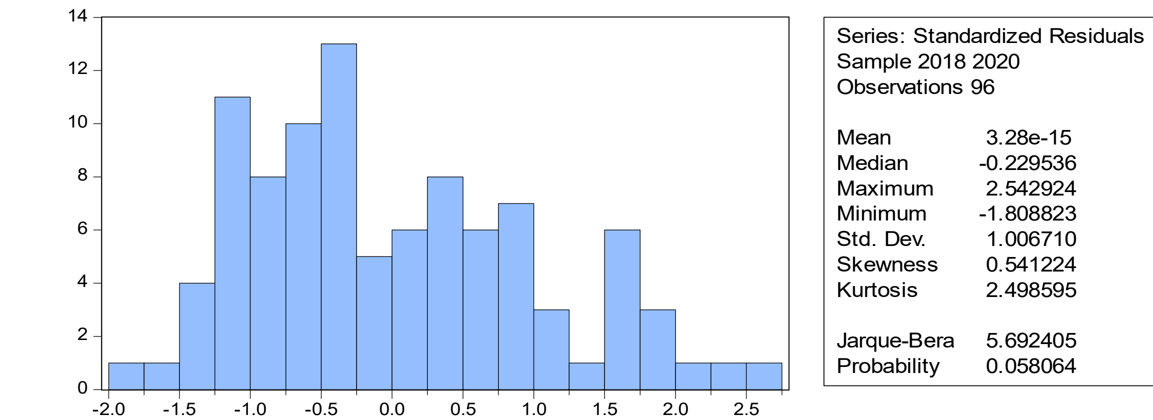
4.1.1. Normality test

The purpose of the normality test is to look at how the regression model is spread out. In this study, the normality test was done by looking at the probability, with the rule that it was normally distributed if the probability value was greater than 0.05. While this is going on, if the probability value is less than 0.05, the distribution is not normal.

4.1.2. Data analysis and findings

A significant probability level of 0.058064 is shown by the normality result in Figure 1. It is clear that the probability value is regularly distributed because it is larger than 0.05. In other words, the regression model utilized is consistent with the normality assumption.

Figure 1. Classic assumption test



Source: EViews 9 processed data, 2021.

Table 1. Multicollinearity test results

Sample: 96 Included observations: 96			
Variable	**Coefficient Variance**	**Uncentered VIF**	**Centered VIF**
C	0.287618	25.87975	NA
X1	1.01E-06	1.731265	1.133970
X2	2.03E-05	1.532576	1.208509
X3	0.008511	5.504404	1.184643
X4	1.181848	16.99448	1.176407
X5	0.087579	1.559656	1.250974
X6	0.013070	1.444106	1.073890

Source: EViews 9 processed data, 2021.

Since each of the independent variables has a variance inflation factor (VIF) value of less than 10, the results of the multicollinearity test shown in the table above show that there is no multicollinearity problem between the independent variables.

Table 2. Heteroscedasticity test results

Variable	*Coefficient*	*Std. error*	*t-statistic*	*Prob.*
C	2.155558	0.642676	3.354034	0.0012
X1	-0.002258	0.001206	-1.872630	0.0644
X2	-0.004533	0.005394	-0.840373	0.4030
X3	-0.063523	0.110555	-0.574583	0.5670
X4	-1.765993	1.302762	-1.355576	0.1787
X5	-0.391309	0.354638	-1.103404	0.2728
X6	-0.024519	0.137001	-0.178968	0.8584

Source: EViews 9 processed data, 2021.

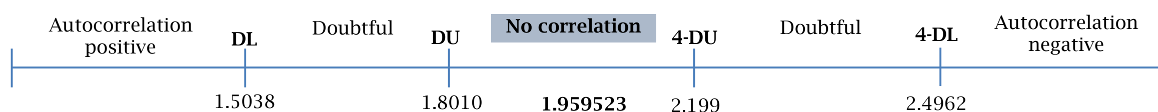
Based on the table above, the results of the heteroscedasticity test can be seen that the overall probability value of the variable is greater than the previously determined alpha level of 0.05. So, it can be concluded that the probability value exceeds the alpha value and the data is free from heteroscedasticity problems.

Table 3. Autocorrelation test results

Autocorrelation test			
R-squared	0.147027	Mean dependent variable	0.649944
Adjusted R-squared	0.089523	S.D. dependent variable	0.720477
S.E. of regression	0.687472	Residual sum of squares	42.06292
F-statistic	2.556825	Durbin-Watson statistic	1.959523
Prob. (F-statistic)	0.024852		

Source: EViews 9 processed data, 2021.

Figure 2. Durbin-Watson test results



The Durbin–Watson (DW) null, which is displayed in the table above, is 1.959523. The value ranges from DU (Durbin–Watson upper limit) to 4-DU, so there is no autocorrelation in this model.

4.1.3. Estimation model selection

The Chow test aims to determine the best model between the common effect model (CEM) and the fixed-effects model (FEM) in estimating panel data. The Chow test is a test to compare the common effects model with the fixed effects (Widarjono, 2009). The Chow test in this study used the EViews program. The Chow test aims to determine the best model between the common effects approach and the fixed effects approach to be used to perform panel data regression.

Table 4. Chow test results

Redundant fixed-effect tests Equation: MODEL_FEM Test cross-section fixed effects			
Effects test	***Statistic***	***d.f.***	***Prob.***
Cross-section F	4.791717	31.58	0.0000
Cross-section Chi²	121.926399	31	0.0000

Source: EViews 9 processed data, 2021.

$H1_0$: Common effect (Probability value > 0.05).

H1: Fixed effect (Probability value < 0.05).

The basis for making decisions on the above hypothesis are:

1. *H1* is accepted, if the probability value is < 0.05, so the model used is the fixed-effect model.
2. *H1* is accepted, if the probability value is > 0.05, so the model used is a common effect.

The Chow test results have a probability of 0.000, which is less than 0.05, according to the above table, hence *H1* is approved. These results back up the idea that the fixed-effect model is better than the common-effect model.

Table 5. Hausman test results

Correlated random effects — Hausman test Equation: MODEL_REM Test cross-section random effects			
Test summary	***Chi² statistic***	***Chi² d.f.***	***Prob.***
Cross-section random	8.494173	6	0.2041

Source: EViews 9 processed data, 2021.

The hypothesis in decision-making on the Hausman test can be seen as follows:

$H2_0$: Random effect (Probability value > 0.05).

H2: Fixed effect (Probability value < 0.05).

The basis for decision-making on the above hypothesis, namely:

1. *H2* is accepted, if the probability value is < 0.05, so that the correct model is a fixed effect.
2. *H2* is rejected if the probability value is > 0.05, so the correct model is a random effect.

The results from the table above indicate that *$H2_0$* is accepted because the random cross-section probability value is 0.2041, which is greater than 0.05. Based on these results, it seems that the fixed-effect model should not be used but rather the random-effect model.

Table 6. Lagrange multiplier test results

Lagrange multiplier tests for random effects Null hypotheses: No effects Alternative hypotheses: Two-sided (Breusch–Pagan) and one-sided (all others) alternatives			
Effects test	***Cross-section***	***Time***	***Both***
Breusch–Pagan	25.17876	0.008806	25.18757
	(0.0000)	(0.9252)	(0.0000)

The hypothesis in the decision-making of the Lagrange multiplier test can be seen as follows:

$H3_0$: Common effect (Probability value > 0.05).

H3: Random effect (Probability value < 0.05).

The basis for making decisions on the above hypothesis, namely:

1. *H3* is accepted, if the probability value is < 0.05, so the right model is a random effect.
2. *H3* is rejected if the probability value is > 0.05, so the correct model is a common effect.

According to the aforementioned findings, *H3* is accepted because the probability value of a random cross-section of 0.000 is less than 0.05. These findings suggest that the random-effect model should be employed instead of the common-effect model. The results of the three tests led the authors to the conclusion that the random-effect model rather than the common-effect model and the fixed-effect model is the most appropriate one to apply in this study.

4.2. Empirical test result

According to Table 7, the probability for the variables institutional ownership, managerial ownership, audit committees, independent commissioners, audit quality, and external pressure on the integrity of financial statements is 0.024852, which is less likely than 0.05, and the F-value is calculated at 2.5566825, which is higher than the F-table of 2.32 so these variables are all present at the same time.

Table 7. Simultaneous test results (F-test)

F-statistic	2.556825
Prob. (F-statistic)	0.024852

Table 8. Coefficient of determination test results (R^2)

R-squared	0.147027
Adjusted R²	0.089523

The determinant coefficient is 0.089523 or 0.89523%, according to the table above. These numbers show that institutional ownership, managerial ownership, the audit committee, the independent commissioner, audit quality, and external pressure have an impact of 8.9523% each, while additional variables not studied in this study account for the remaining 91.0477%.

Table 9. Partial test (t-test)

Dependent variable: *Y* Method: Panel EGLS (Cross-section random effects) Date: 01/07/22 Time: 18:34 Sample: 2018–2020 Periods included: 3 Cross-sections included: 32 Total panel (balanced) observations: 96 Swamy and Arora estimator of component variances				
Variable	***Coefficient***	***Std. error***	***t-statistic***	***Prob.***
C	3.556234	0.688697	5.163710	0.0000
X1	-0.002582	0.001540	-1.676442	0.0972
X2	-0.005605	0.006678	-0.839316	0.4035
X3	-0.087485	0.126714	-0.690415	0.4917
X4	-3.921574	1.321907	-2.966603	0.0039
X5	0.369363	0.398831	0.926114	0.3569
X6	-0.170707	0.095974	-1.778674	0.0787

According to the table above, which analyzes how independent commissioners affect the integrity of financial statements, the probability value for the independent commissioner variable is 0.0039, larger than 0.05, and the t-count value is -2.966603, greater than the t-table value of 1.98667. The independent commissioner, then, has a negative impact on the integrity of the financial statements. Hence, it can be said that *H4* is accepted.

4.3. Discussion

4.3.1. The effect of board independence and ownership structure on the integrity of financial statements

This study's first hypothesis looks at how institutional ownership affects the integrity of financial statements. According to Table 9, the probability for the institutional ownership variable was 0.0972, which is larger than 0.05, and the value of the t-count was -1.676442, which was lower than the table's value of 1.98667. So, it can be inferred that *H1* is rejected because it reveals that institutional ownership has no appreciable impact on the integrity of financial statements. This study's findings are consistent with those of studies by Solikhah (2017) and Nurdiniah and Pradika (2017). Because the institutional owners of the company themselves do not have much role in the management of the company, it is quite difficult to monitor which can cause the implementation of the integrity of financial statements to be less influenced by institutional ownership. However, the results of this study contradict Goretry (2017). The study explains that institutional ownership has an effect because the management will reduce the tendency to present manipulated reports. This difference in results may be due to the different years of research and the use of different samples. It can be concluded that the higher or lower the institutional ownership does not have a significant impact on the integrity of the financial statements.

The purpose of this study is to determine if managerial ownership can significantly impact the integrity of financial statements. According to the results, the probability value for the managerial ownership variable is 0.4035, which is higher than 0.05, and the t-count value is -0.839316, which is lower than the t-table value of 1.98667. Furthermore, it demonstrates that managerial ownership has little to no impact on the integrity of financial statements. Hence, it can be said that *H2* is rejected. The findings of this study concur with those of studies by Gorety (2017) and Solikhah (2017), which state that managerial ownership is less influential because management generally owns the company's shares, but private ownership is not sufficient to provide opportunities for decision-making and voting rights. However, this study contradicts Widodo (2016) where the results show a significant effect. Differences in research results can be caused by the use of different regression methods, and different sample data. The results of managerial ownership do not have a big effect on the integrity of financial statements. This means that it does not matter much whether the managerial ownership of a company is high or low; the integrity of the financial statements would not change much either way.

The goal of this study is to determine whether the audit committee significantly affects the integrity of the financial statements. According to Table 9, the audit committee variable receives a probability value of 0.4917, which is larger than 0.05, and the t-count value of -0.690415 is less than the t-value of 1.98667. This demonstrates that the audit committee's influence on the integrity of the financial statements is negligible. The findings of this study are consistent with studies by Hardiningsih (2010) and Nurdiniah and Pradika (2017), and others that found no discernible impact of the audit committee on the integrity of the financial statements. The audit committee is not directly involved in the financial issues the firm is experiencing because it merely reviews the financial and accounting data generated by the company. It may be inferred that the number of audit committees, whether bigger or smaller, has no bearing on the integrity of the financial statements.

The purpose of this study is to determine whether the integrity of financial statements is significantly impacted by independent commissioners. According to Table 9, the probability value for the independent commissioner variable is 0.0039, which is lower than 0.05, and the t-count value is -2.966603, which is higher than the t-table, which is 1.98667. This proves that the independent commissioner has a big impact on the integrity of financial statements. The findings of this study are consistent with studies by Grotery (2017) and Verya et al. (2017), according to which independent commissioners are thought to be able to lessen agency problems from managers since they mediate when such issues arise. However, there are some differences between this study and Solikhah's (2017) that may explain why. These differences include the research methodologies, research sample data, and research years. Thus, the independent commissioner has an impact on the integrity of financial statements. It indicates that whether it is larger or smaller, it will have an impact on the integrity of financial statements.

4.3.2. The effect of internal audit on the integrity of financial statements

This study's second hypothesis is to determine whether the integrity of financial statements is impacted by the audit quality. According to the study's findings, the audit quality variable has a probability value of 0.3569, which is higher than 0.05, and a t-count value of -0.926114, which is lower than a t-table value of 1.98667. This demonstrates that the integrity of financial statements is not significantly impacted by the quality of the audit. The Big Four and non-Big Four public accounting firms are sufficiently independent and less likely to engage in fraud; hence, the findings of this study are consistent with studies by Gorety (2017) and Hardiningsih (2010). If an auditor is unable to maintain an independent attitude, so that persons who can affect the integrity of financial statements are not based on the public accounting firm where they work, the Big Four and non-Big Four will also continue to perpetrate fraud. The fact that these findings differ from those of Widodo (2016) and Jama'an (2008) may be due to the varied study methodologies, research sample data, and research years. According to one interpretation, the audit quality has no appreciable impact on the integrity of financial statements; therefore, whether the audit quality is high or low has no bearing on the integrity of financial statements.

4.3.3. The effect of external pressure on the integrity of financial statements

The third hypothesis of this study tests whether outside pressure can have a big effect on the integrity of financial statements. According to the findings, the external variable receives a probability value of 0.0787, which is higher than 0.05, and the value of -1.778674 for the t-count is lower than the value of 1.98667 for the t-table. Also, it shows that outside pressure does not have a big effect on the reliability of financial statements. Hence, it can be said that *H6* is rejected. The findings of this study are consistent with those of Sari and Nugroho (2020). According to Ulfah et al. (2017) and Martanty and Daljono (2013), there is no evidence that external pressure significantly affects the integrity of financial statements because companies frequently issue shares in return for additional working capital from investors rather than entering into new debt agreements, which could increase the burden on the business. Yet, these findings contradict Ozcelik (2020). This is possible as a result of the various study methodologies, research sample data, and research years, which indicates that the integrity of the financial statements will not be impacted by external pressure, whether it is higher or lower. According to the findings of earlier studies on the impact of external pressure on financial reporting transparency conducted by Basuki and Ridha (2012), Satriawan and Sihaloho (2014), and Hadi and Hastuti (2015), external pressure has a favorable impact on the implementation of financial reporting transparency in the form of regulations and policies that set off this process. The same variable was explored by Julita and Belian (2015) and Yusrawati and Dewi (2015), with the findings that external pressure had no impact on the implementation of financial reporting transparency.

5. CONCLUSION

The following can be deduced from the findings of the study and the hypothesis testing that was done:

1) the integrity of financial statements is not significantly impacted by institutional ownership;
2) the integrity of financial statements is not significantly impacted by managerial ownership;
3) the integrity of financial statements is not significantly impacted by the audit committee;
4) the integrity of financial statements is significantly influenced by independent commissioners;
5) the integrity of the financial statements is not materially affected by the audit quality;
6) the integrity of financial statements is not significantly affected by external pressure.

The results of this study are expected to be useful in providing some positive implications and input which are especially prioritized for parties who have the following interests:

1. *For writers*: This research is expected to be a source of insight and inspiration to future researchers in conducting research on corporate governance mechanisms, audit quality, and external pressure on the integrity of financial statements, so as to open views and develop new theories related to the integrity of financial statements.
2. *For companies*: In this study, it is expected that companies can be more transparent in their business activities. Company leaders are expected to increase monitoring of the company's internal control over the performance produced by the company so that it is better.
3. *For decision-makers*: In deciding to invest in a company, investors are expected to be more careful and ensure that the information received is valid about the condition of the company, investors are also expected to be able to analyze finances in detail to find out the actual financial condition of the company.
4. *For auditors*: In this study, it is expected that an auditor can maintain the existing code of ethics, an auditor is expected to be able to provide an honest opinion about a company so that users of financial statements are not harmed.

Companies should continue to strive to present financial reports with high integrity. Companies should increase the proportion of institutional share ownership, managerial share ownership, and internal audit supervision so that institutional investors are interested in investing in companies, companies should disclose complete information in accordance with capital market conditions. The information that can attract investors is in the form of corporate actions, such as the distribution of dividends, issuance of bonus shares, and so on, so that the integrity of financial statements can be achieved and meet the needs of investors and other users of financial statements. Users of financial statements should collect all information related to the condition of the company, not limited to financial reports so that they can make decisions

that have the right economic consequences. Future research should conduct the same research for other types of industries in order to obtain more samples in order to strengthen the results of previous studies. Subsequent research in testing the integrity of financial statements can add other independent variables, such as auditor reputation, external auditors, external pressure on audit tenure and so on.

This research has limitations, namely, the research period which only includes 2018–2020; the independent variables used are not uniform between internal factors and external factors. As a recommendation, further research can add other variables that may have a stronger influence on the integrity of financial statements, such as tax avoidance, International Financial Reporting Standards implementation, firm size, and so on. Future research can use other internal factors as independent variables, such as independent commissioners, board of directors, financial distress, audit committees, intellectual capital, corporate social responsibility, ratios of financial performance, investment opportunity, and variables relevant to the objectives study.

Besides internal factors, future research can also use other external factors as independent variables, such as opinions audit, tenure audit, delay audit, switching audit, and industrial auditor specialization. Suggestions that can be useful input for related parties, namely the company expected to maintain independent commissioners in accordance with the regulations apply. So that the effect of the presence of independent commissioners in the company will become an important component in good corporate governance so as to have an impact on increasing the integrity of financial reports. This research is expected to provide information about what factors affect the integrity of financial statements in financial reporting in the context of presenting financial reports with integrity and quality. For stakeholders, this research is expected to help stakeholders to assess whether the financial reporting presented by companies has integrity by analyzing the factors that influence the integrity of financial statements.

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