

FACTORS AFFECTING THE INTEGRITY OF FINANCIAL STATEMENTS : BEFORE AND DURING THE PANDEMIC

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ABSTRACT

The target of this research is to establish the effect from auditor switching, audit tenure, and financial distress on the integrity of economic statements before and through the pandemic. The subject of this research are the financial sectors registered on the Indonesia Stock Exchange between years of 2019 and 2020. This research method uses a quantitative method. The population that been used are companies in the financial sector between years of 2019 and 2020. The sample of the population that been used were taken using a purposive sampling technique, counted as 106 samples. Data were analyzed using the Statistical Program for Social Software (SPSS) version 24.0 using descriptive statistics and multiple linear regression. The financial statements integrity in this study is measured using conservatism. The results of the study partially show that auditor switching and audit tenure have no significant effect on the financial statements integrity before the pandemic and through the pandemic, while financial distress has no effect on the integrity of financial statements pre-pandemic financial statements but has a significant negative effect on the financial statements significant at the time of the pandemic. There was a significant difference between the financial statements significant before and through the COVID-19 pandemic.

Keywords : Auditor Switching; Audit Tenure; Financial Distress; Integrity of Financial Statements; Pandemic Covid-19

INTRODUCTION

The annual financial statements are the primary for management's decision making. Financial statements are notation records that represent the company's financial situation and formed in a structured way (PSAK 1, 2015). The main terms of creating financial statements are to maintain financial data, changes in the financial position of an entity for internal and external parties. The requirement for making financial statements is that financial statements must be presented in accordance with the actual condition of the entity or in other words, the entity is required to present financial statements with integrity. Integrity means that the information presented is fair, honest and unbiased.

In 2020, the world is experiencing a COVID-19 pandemic and it is having a huge impact on its economy, including Indonesia. 88% of companies were severely affected, causing sales to decline and the sectors affected by COVID-19 were the

tourism sector and the financial sector. Association Certified of Fraud Examiner (ACFE) research showed the first level of fraud in financial statement manipulation is in the financial and banking sectors with a value of 41.4% or in other words, financial statements in the financial sector still do not have integrity. The COVID-19 pandemic can cause rapid modification to the financial statements integrity. This has led the research to use the balance shift theory.

Several well-known financial sectors are also involved in the financial statements manipulation in Indonesia, thereby making the public less trustful of the statements presented in the financial statements. In 2020, BPK conducted an inspection on PT. Jiwasraya and it was found that in the 2006 financial statements, Jiwasraya had modified the financial statements by recognizing the company's condition as profit while the actual condition was a loss. In addition, in 2017 Bank Bukopin manipulated credit card data for five years and caused commission income to increase unnaturally. As the case of financial statements manipulation, it usually involves internal parties such as: CEO (Chief Executive Officer), corporate governance (audit committee and commissioners) as well as auditors, both internal auditors and external auditors.

A major factor affecting the financial statements integrity is auditor switching. Weak supervision by the company is one of the causes for KAP to lose its independence. Therefore, there are regulations to improve the company's supervisory structure by changing auditors. Auditor switching is a transformation in the use of KAP services carried out by the company as the result of the auditor switching which can improve the aspect of the information (Fauziah & Panggabean, 2019). According to the results of previous research, by Totong & Majidah (2020) resulted in auditor switching variable having a significant negative outcome in the financial statements integrity. The differences of the results from two previous studies, the research conducted by Selviana & Wenny (2021) told that the auditor switching variable show no effect either simultaneously or partially on the financial statements integrity.

The second factor that influence the financial statements integrity is the audit tenure. Audit tenure is the involvement of an auditor in auditing a client. The tenure of an auditor can conduct to a close connection between the management and the auditor resulted the independence of the auditor will be reduced and his objectivity will also be reduced in evaluating the financial statements as the result of the adjustment on the

wishes of the management and then can influence the auditor while giving an opinion.(Prena & Cahyani, 2020). Research by Arista et al. (2019) prove that the audit tenure variable shows a significant negative outcome in the financial statements integrity. Research by Prena & Cahyani (2020) results where audit tenure has no effect on the financial statements integrity.

The next factor is financial distress. External parties or investors if they want to invest must see the financial condition of the company, as the result the level of financial distress is an important factor. Financial distress usually begins with difficulty paying short-term obligations by the company. Manipulation of financial statements made by management when experiencing financial difficulties because they do not want the company's performance to look bad in the eyes of investors. According to the previous result from the studies, research by Liliyani & Arisman (2021) resulted the financial distress variable has a significant positive outcome in the financial statements integrity. The differences found in the results by Halim (2021) where the variable financial distress or financial difficulty shows a significant negative effect on the financial statements integrity.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Theory of Balance Shifting

Theory of Balance Shifting is a theory put forward by Sewall Wright in 1932. This theory explains how a population or a state is at a suboptimal peak and explains that evolution can take place rapidly due to shifts. The COVID-19 pandemic in 2020 is known as the natural selection shift, which can cause rapid changes to the financial statements integrity.

Financial Statements Integrity

Financial statements prepared by management must have an integrity. Financial statements integrity is the quality of financial statements while presenting real, honest and accurate information based on the actual situation or changes in the company's financial point without any intentional changes because the financial statements will be accountable to the principal or shareholders (Selviana & Wenny, 2021). According to Nurbaiti et al. (2021) Financial statements integrity is the main of financial statements, they must be neutral or has no sideward of any, no lies and explain the actual condition of the company.

Hypothesis

Auditor Switching

Auditor switching is a change in a public accountant carried out by a company where the change can be done voluntarily or mandatory, namely company regulations. Compulsory replacement of auditors is regulated according to the Minister of Finance Regulation No. 17/PMK.01/2008 issued on February 5, 2018 which requires companies to limit the tenure of public accountants to three years and KAP to six years (Selviana & Wenny, 2021). Auditor switching which is bring out the mandatory or in accordance with applicable policies aims to maintain the independence of an auditor in carrying out audits.

The pandemic causes many companies to have small profits or even suffer losses and can cause the company's financial condition to decline, this condition causes if the company performs auditor switching it can make it possible for auditors to take a long time to understand company regulations as to improve the financial statements integrity. Thus, the more often companies perform mandatory auditor switching (based on policy), financial statements integrity should increase. The research by Kartika & Nurhayati (2018) shows that the auditor switching variable shows a significant positive outcome on financial statements integrity.

H1: Auditor switching has a positive effect on the financial statements integrity.

Audit Tenure

Audit tenure is the dimension of the audit engagement period at the Public Accounting Firm (KAP) in maintaining audit services to customers. According to the Government Regulation No. 20 of 2015 in article 11 explains that audit services in the arrangement of services on the company's annual financial statements performed by the Public Accounting Firms are a maximum of five years period (Saad & Abdillah, 2019). If an auditor has a long enough audit term, he can have a close relationship with the management, so that it can affect the opinion produced and provide results as expected by investors (Arista et al., 2019).

The COVID-19 pandemic has acquired the company's financial condition to down sufficiently so that it can affect the condition of the financial statements submitted by the company. If the audit firm's tenure has been long or more than 3 years which made a closer auditor-client relationship, the client can request the KAP to issue an

opinion based on the wishes of management. This condition causes changes from pre-pandemic financial statements and during the pandemic. The longer the tenure of an audit, the more data manipulation will occur and the financial statements integrity will decrease. The hypothesis in this research is supported by several previous research results. Research by Manuari & Devi (2021) results that the auditor tenure variable show a significant negative outcome on financial statements with integrity.

H2: The term of office of the audit has a negative effect on the financial statements integrity.

Financial Distress

According to Altman (1968), Financial Distress is the failure of a companies experiencing in a financial position that is difficult to predict (Malau & Murwaningsari, 2018). A failed company tends to be able to do fraudulent things such as engineering financial statements of the the company and causing a decrease in the integrity of the financial statements. Companies that experience financial distress will have a concussion on the use of the principle of conservatism in their companies and can cause management to act fraudulently so that it can affect the financial statements integrity of the company.

During COVID-19 pandemic, many companies experienced operational difficulties which would have an impact on financial conditions, which in turn would have an impact on financial distress for the company. Of course, the level of financial distress in 2020 or during a pandemic will be high due to a shift in balance. The increasement on the value of financial distress from the company, the lower the financial statements integrity. The hypothesis in this research is supported by previous research. Research by Halim (2021) shows that the financial distress variable show a positive effect on the financial statements integrity.

H3: Financial distress has a negative effect on the financial statements integrity.

RESEARCH METHODOLOGY

Method is a method of work that can be used to obtain something. While the research method can be interpreted as a work procedure in the research process, both in searching for data or disclosing existing phenomena (Zulkarnaen, W., et al., 2020). This research uses secondary data, used with purposive sampling method for sample selection. The data comes from financial sector companies registered on the Indonesia

Stock Exchange (IDX) for the years of 2019 and 2020 and did not conduct delisting during the analysis period. Then, financial sector companies that fall into the 'main' listing category. The total research sample in 2019 and 2020 is 106 financial sector companies.

This research uses multiple linear regression data for techniques of analysis and is refined using Statistical Program for Social (SPSS) software version 24.0 which purposed to identify the effect from the the dependent variable and independent variable.

Financial Statements Integrity

There are two ways to measure the financial statements integrity, namely by calculating earnings management or by conservatism (Arista et al., 2019). In this study, the researcher uses conservatism, because the main characteristics of conservatism can be used as a prediction of future conditions and in accordance with the objectives from financial statements. As if the results of the conservatism measurement are negative, then the company is indicated to apply conservatism as the result if financial statements of the company have integrity. The results on the report integrity variable in 2019 will be compared with the results on the financial statement integrity completeness variables in 2020 through a table, so that the impact in the covid period can be seen.

Auditor Switching

Measurement of the auditor switching variable used is based on research by Kartika & Nurhayati (2018). The auditor turnover variable in this research was measured by a measurement using a dummy variables, where if the client or the company changes auditors it will be given as the value of 1, whereas if the client or the company does not change auditors it will be given as the value of 0. The results on the auditor switching variable in 2019 will be compared with the results on the auditor variable. switching in 2020 through the table, so you can see the effect in the covid period.

Audit Tenure

The audit tenure variable was measured by a measurement using a dummy variable because the regression results were easier to interpret. If the audit tenure firm or auditor is less than three years, code 0, otherwise, if the audit tenure firm or auditor is more than three years, code 1 is assigned (Nicolin & Sabeni, 2013). The results on the

audit tenure variable in 2019 will be compared with the results on the audit tenure variable in 2020 through the table, so that the impact in the covid period can be seen.

Financial Distress

The deterioration of the company's financial position as owned by the debt of equity ratio, known as the large portion of debt in a company's capital. The results from the financial distress variable in 2019 will be compared with the results on the financial distress variable in 2020 through the table, so that the impact in the covid period can be seen. If $DER > 1$, the company is not experiencing financial distress because the level of financial distress is low, while if $DER < 1$, the company is experiencing financial distress because the company's level of financial distress is considered high (Halim, 2021).

RESULT AND DISCUSSION

The results of descriptive statistics are the minimum value, maximum value, mean value and standard deviation of respectively independent variable and dependent variable (provided in table 1). According to table 1, it's showed that descriptive statistics results on the financial sector with a total sample of 106 research samples. The financial statements integrity variable shows the minimum value of -0.921 and the maximum value of 0.250 with the mean of -0.01895 and a standard deviation of 0.145114. The standard deviation of the financial statements integrity is higher than the mean, indicating that the data from the financial statements integrity is heterogeneous or that the distribution of the integrity data on the financial statements fluctuates between one company and another.

The financial distress variable shows a minimum value of 0.01 which is owned by the STAR company (Buana Artha Anugerah Tbk) which means the company is experiencing financial difficulties and the maximum value is 16.08 which is owned by the BBTN company (Bank Tabungan Negara Tbk) which means the company is in a healthy financial condition. The average financial distress variable is 4.0861 where the standard deviation is 2.90919, these results means the financial distress data in the financial sector is homogeneous as the result from the standard deviation is smaller than the mean.

$$ILK = 0.059 - 0.072 US - 0.048 MJA + 0.006 FD + e$$

The result of the t-test table before the 2019 pandemic provided on table 2, which explained below:

1. The significance value of the auditor switching variable on the financial statements integrity shows a value of 0.089 or higher than 0.05. As the result, H1 is declined. T table for auditor switching variable is $1.736 < 1.98350$ (Tcount). Hypothesis 1 in this research shows that the auditor switching shows a positive effect on the financial statements integrity. It is concluded that auditor switching shows no effect on the financial statements integrity.
2. The significance value from the audit tenure variable on the financial statements integrity shows a value of 0.279 which is greater than 0.0. As the result H2 is rejected. The T table for the audit tenure variable is 1.094 or smaller than T count, which is 1.98350. Hypothesis 2 in this research shows that the audit tenure shows a negative effect on the financial statements integrity. It is concluded that the audit tenure shows no effect on the financial statements integrity.
3. The significance value from the financial distress variable on the financial statements integrity shows a value of 0.450 or higher than 0.05. As the result, H3 is rejected. T table for financial distress variable is $0.762 < 1.98350$ (Tcount). Hypothesis 3 in this research shows that the financial distress shows a negative effect on the financial statements integrity. It is concluded if financial distress shows no significant effect on the financial statements integrity.

$$ILK = -2.350 + 0.387 US + 0.048 MJA - 0.098 FD + e$$

According to the t-test table during the pandemic (2020) above, the results are explained below:

1. The significance value of the auditor switching variable on the financial statements integrity shows a value of 0.249 or greater than 0.05 which means H1 is rejected. T table for auditor switching variable is $1.202 < 1.98350$ (Tcount). Hypothesis 1 in this research shows that auditor switching shows a positive outcome on the financial statements integrity. It is concluded if auditor switching shows no outcome on the financial statements integrity.
2. The significance value of the audit tenure variable on the financial statements integrity shows a value of 0.870 which is greater than 0.05 which means H2 is rejected. The T table for the audit tenure variable is 1.094 or smaller than T count,

which is 1.98350. Hypothesis 2 in this research shows that audit tenure shows a negative outcome on the financial statements integrity. It is concluded if the audit tenure shows no outcome on the financial statements integrity.

3. The significance value of the financial distress variable on the financial statements integrity shows a value of 0.041 or less than 0.05 which means H1 is accepted. T table for financial distress variable is $2.253 > 1.98350$ (Tcount). Hypothesis 3 in this research shows that financial distress shows a negative outcome on the financial statements integrity. It is concluded that financial distress shows a significant negative outcome on the financial statements integrity

According to the results of the multiple regression test before the pandemic and during the covid-19 pandemic, it can be concluded that there are differences starting from constants with positive values before the pandemic and negative through the COVID-19. Then on pre-pandemic financial statements, if auditor switching was carried out, it would reduce the financial statements integrity, while during the pandemic, if the auditor switching was carried out, it would increase the financial statements integrity. The audit tenure variable, if the audit tenure of an auditor is more than 3 years, it will reduce the financial statements integrity, while during a pandemic, if the position of an auditor is more than three years, it will increase the financial statements integrity. financial distress variable, if the company experienced financial distress before the pandemic, the financial statements integrity would increase, whereas if the company experienced financial distress during the pandemic, the financial statements integrity would decrease. it can be concluded that there are disparity in the results of the financial distress variable. Preceding to the COVID-19, financial distress had no effect on the financial statements integrity, while during the COVID-19, financial distress shows a significant negative outcome on the financial statements integrity. And it can also be concluded that there are disparity in the results of the financial distress variable. According to the COVID-19 pandemic, financial distress shows no outcome on the financial statements integrity rather than on the COVID-19.

According to the table below, it is known if the t table in part of before the pandemic and during the pandemic is 2,392, degrees of freedom is 52, and the significance value is 0.020. A significance value of $0.02 < 0.05$, it can be summarized that there is a difference between the financial statements integrity before the pandemic

and through the covid-19 pandemic. In accordance with the balance shifting theory which explains that a situation or condition is as the result from an unexpected phenomenon such as COVID-19 pandemic. The condition in question is the difference in the usage of the main conservatism in financial statements in the financial sector. These results are supported by the balance shifting theory which states that the phenomenon causes the current and previous period conditions to differ or change.

Hypotheses Discussion

Effect of Auditor Switching on the Financial Statements Integrity

This research has not been able to prove if there is a positive outcome of auditor switching from the financial statements integrity. The impacts from this research shows if auditor switching has no effect on the financial statements integrity both before the pandemic (2019) and during the pandemic (2020), and the results from this research is consistent with the research by Hartono & Wenny (2017) which declares that auditor switching shows no effect on the financial statements integrity. Auditor switching is carried out by the company only to fulfill the provisions stipulated in PP Number 20 of 2015 which requires companies to change auditors after five consecutive years so that it has no affection to the use of the company's conservatism principle so that even though the company changes auditors, the financial statements remain with integrity (Selviana & Wenny, 2021).

In the financial sector, the impacts declare that auditor switching show no effect the financial statements integrity, this is because even though the company changes auditors, the information in the financial statements remains conservative. Auditor switching show no outcome on the financial statements integrity, this could also be because the management and accountants in the company have compiled the financial statements based on SAK and the stipulated provisions. This result is not in accordance with the balance shifting theory which states that the phenomenon causes different conditions in the current and previous periods. The pandemic does not cause companies to intentionally switch lid up the financial condition of the company.

The Effect of Audit Term on the Financial Statements Integrity

This research has not been able to prove that audit tenure shows a negative outcome on the financial statements integrity. The research's results show if audit tenure shows no outcome on the financial statements integrity, both before the

pandemic (2019) and during the pandemic (2020), consistent with the research from Rosalina et.al. (2019) which conducted if the audit tenure has no affect at the financial statements integrity. This shows that the length from the engagement of the Public Accounting Firm (KAP) with the client does not interrupted with the financial statements integrity from financial sector companies.

Furthermore, the level of activity of the audit tenure at the Public Accounting Firm (KAP) as an auditor does not affect the application of the principle of prudence in the annual financial statements, or in other words, the audit tenure is not a consideration for the financial statements to be conservative or not (Rosalina et al., 2019). The length of the audit term for a Public Accounting Firm (KAP) has been organized in the Regulation of the Minister of Finance of the Republic of Indonesia Number 5 of 2011 which states that the maximum period of time for KAP to audit one entity is 5 years. The longer the audit tenure allows the KAP to be more careful in issuing audit opinions.

In the sector of financial, which has been registered on the Indonesia Stock Exchange (IDX), it shows if KAP auditing financial sector companies still adheres to the principle of objectivity, so that even though the audit term of the KAP has been more than three years, it does not create closeness with the management and does not issue an opinion at the request of the public authority. This proof is not only in accordance through the balance shifting theory which is said as the phenomenon causes different conditions in the current and previous periods.

The Effect of Financial Distress on the Financial Statements Integrity

This research is able to prove that financial distress shows a negative affect on the financial statements integrity during covid-19 pandemic (2020) but financial distress shows no affect on the financial statements integrity before the covid-19 pandemic (2019). Differences on pre-pandemic financial statements and during the pandemic can be caused by shifts in natural selection so that these changes move quickly over the course of a year. As explained in balance shifting theory, a state can change and can even reach a suboptimal peak. In this case, financial distress reached a suboptimal peak, causing significant disparity in the results before COVID-19 and through COVID-19. The COVID-19 can be called a shift that causes these conditions because there were quite significant changes before and during the pandemic which can be seen from the t-

test and different tests. Both of them have very different results, especially in the results on the financial statements integrity.

These proof are in accordance with the result on the research from Halim (2021) which said if financial distress shows a negative affect on the financial statements integrity. The greater level of financial distress in the company, the more it motivates management to manipulate financial statements because management wants to present good company conditions to investors so that it has a concussion on the financial statements integrity. Companies experiencing financial distress tend to maintain a large portion of net income to cover unexpected events so that they ignore the principle of conservatism and can reduce the financial statements integrity. Companies experiencing financial distress will increase conservatism (positive value) in financial statements and can reduce the financial statements integrity.

The financial distress variable is in correspondence with the balance shifting theory which states that the phenomenon causes differences in conditions in the current and previous periods. This is showed in table 4.15 which viewed the mean and standard deviation increased on pre-pandemic and through pandemic financial statements. At the time of the t-test or comparison test, the standard deviation was 2.78139 before the pandemic and 3.10653 through the pandemic. Then, the mean before the pandemic was 3.9630 and 4.1191 through the pandemic, this shows that the overall value of financial distress from the entire sample increased, so it can be said that financial distress before and during the pandemic differed significantly. The pandemic caused companies to experience increased financial distress from the previous year so that it could influence the financial statements integrity. The pandemic causes a shift that causes a significant disparity between before the pandemic and through the pandemic. The shift in natural selection, namely the pandemic, also causes the operational burden on the company to continue to increase, so that it can affect cash and can cause financial difficulties for the company. This financial distress or financial difficulty can affect the financial statements integrity. This is caused from a shift in the phenomenon in accordance with the explanation of the theory of balance shifting. The shift in natural selection, namely the pandemic, also causes the operational burden on the company to continue to increase, so that it can affect cash and can cause financial difficulties for the company. This financial distress or financial difficulty can affect the integrity of financial

statements. This is caused by a shift in the phenomenon in accordance with the explanation of the theory of balance shifting. The shift in natural selection, namely the pandemic, also causes the operational burden on the company to continue to increase, so that it can affect cash and can cause financial difficulties for the company. This financial distress or financial difficulty can affect the financial statements integrity. This is caused by a shift in the phenomenon in accordance with the explanation of the theory of balance shifting.

CONCLUSION

The financial statements integrity in the financial district which has registered on the Indonesia Stock Exchange in 2019 and 2020 may occur due to financial distress and the COVID-19 pandemic. Then the researcher has not been able to find any effect of auditor switching and audit tenure on the financial statements integrity. Auditor switching performed by the company does not affect the use of the principle of conservatism so that it has no affection to the company's statements integrity. The audit tenure of three years or more and less than three years has affect to the financial statements integrity because the KAP maintains independence while producing audit opinions.

This research also concludes that there are differences in linear regression and hypothesis testing. Then, there is a significant difference in the financial statements integrity before the pandemic and through the pandemic through the t test (paired sample). This is in the same way with the balance shifting theory, which declares that the financial statements integrity in the financial sector is undergoing rapid changes caused by shifts in natural selection (the covid-19 pandemic) and financial distress reaching suboptimal conditions during the pandemic (2020).

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TABLES

Table 1. Descriptive Statistical Analysis Results

Descriptive Statistics

	N	Minimum	Maximum	mean	Std. Deviation
Switching Auditor	106	0	1	,48	,502
Audit Term	106	0	1	,67	,473
Financial Distress	106	,01	16.08	4.0861	2,90919
Financial Report Integrity	106	-,921	,250	-0.01895	,145114
Valid N (listwise)	106				

Table 2. T-Test Results Before the Covid-19 Pandemic (2019)

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.059	0.059		1.006	,320
	Switching Auditor	-,072	.042	-,242	-1,736	,089
	Audit Term	-,048	.044	-,153	-1.094	,279
	Financial Distress	,006	,007	,106	,762	,450

Table 3. T-Test Results During the Covid-19 Pandemic (2020)

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-2,350	,277		-8,480	,000
	Switching Auditor	,387	,322	,279	1,202	,249
	Audit Term	0.048	,291	,039	,166	,870
	Financial distress	-,098	.043	-,501	-2.253	.041

Table 4. Paired Samples t-test Result of Financial Statement Integrity

Paired Samples Test

	Paired Differences		T	df	Sig. (2-tailed)
	mean	Std. Deviation			
Pair 1 Before the Pandemic - During the Pandemic	.051340	.156279	2,392	52	.020