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### 3 SELF-EFFICACY MEDIATES THE RELATIONSHIP BETWEEN INDIVIDUALISM CULTURE AND AUDIT QUALITY: EVIDENCE FROM INDONESIA

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#### ABSTRACT:

This study investigates the effects of individualism culture on audit quality. Specifically, it examines the mediating effects of self-efficacy on the relationship between individualism culture and audit quality. Social cognitive theory is employed as a theoretical framework. Using the purposive sampling method, 69 auditors of the Indonesian Supreme Audit were selected as the sample. Structural Equation Modeling with WarpPLS Program 4.0 was used to test the hypotheses. The results of this study show that individualism culture has a significant impact on audit quality. This study also finds that self-efficacy acts as a mediator variable.

**Keywords:** self-efficacy, government auditor, social cognitive theory, audit quality, Indonesia

#### 1. INTRODUCTION

DeAngelo (1981, p. 186) defines audit quality as “the market assessed joint probability that a given auditor will both discover a breach in a client’s accounting system, and report the breach”. A high-quality auditor will detect errors and enhance the reliability of the financial statements (D. Chan and Wong, 2002; Gul et al, 2002; Chang et al, 2009). Carcello et al (2002) find that audit quality is directly linked to the amount of audit work. Many factors affect the quality of the audit, and these factors come not only from within the auditor but also from the outside. In this study, individualism culture and self-efficacy variables are expected to influence audit quality.

The importance of the cultural characteristics of individual auditors in the audit process has been widely documented. For example, studies by Agacer and Douppnik (1991), Bernardi et al (1997), Cohen et al (1996), Douppnik and Salter (1995), Lampe and Sutton (1994) suggest that cultural differences significantly affect the audit process. Self-efficacy is derived from social cognitive theory (Bandura, 1986). It suggests that most of the knowledge and behaviour of members of an organization is derived from the environment, and thought processes in response to information received are continuous. It affects the motivation, attitudes, and behavior of individuals. Some research suggests that self-efficacy contributes significantly on an individual destination level, i.e., achievement of goals and performance (Lock and Latham, 1990).

Although prior studies have investigated the determinants of audit quality, few studies in the organizational behavior and auditing literature have tested the mediating effects of self-efficacy. The first objective of this study is to examine the effect of individualism culture on audit investigative quality. The second is to investigate whether self-efficacy mediates the relationship between individualism culture and audit investigative quality. This study was carried out because of the importance of audit quality in the decision-making process of stakeholders. By understanding the factors that affect the quality of an audit, auditors can increase their capabilities and thus minimise the occurrence of fraud.

#### 2. LITERATURE REVIEW AND HYPOTHESES

“Social cognitive theory was used by Bandura in response to dissatisfaction with the principles of behaviorism and psychoanalysis. According to the theory, the role of cognition in motivation and the role of motivation are mostly ignored” (Bandura, 1977). The term “cognitive” comes from the word cognition,

which means understanding or understand. The wider definition of cognition is the acquisition, structuring, and use of knowledge. In subsequent developments, this cognitive term, then, became popular as one of the areas of human psychology/a general concept that includes all forms of recognition, which includes any mental behavior related to the problem of understanding or paying attention.

Hofstede (1991) and Hofstede (2001) "identified five dimensions along which national cultures could be compared and contrasted: individualism versus collectivism, large versus small power distance, strong versus weak uncertainty avoidance, masculinity versus femininity, and short-term versus long-term orientation. One cultural dimension (individualism) is identified as a dimension that is closely related to factors affecting errors detected in auditing. Members of an individualist culture are expected to act according to their own interest, and they champion individual achievement. Management in an individualist organization is management of individuals, and the relationship between employer and employee is conceived as a business transaction based on mutual benefit. From a control perspective, this cultural dimension relates to the behavioral aspects of the internal control system and the inherent risks." There is a growing recognition of the importance of personnel policies and practices in implementing effective controls to prevent and detect errors or irregularities in financial statements (Glover and Aono, 1995). K. H. Chan et al (2003) argue that "based on cultural characteristics, individualist companies have more reliance on accounting numbers for individual performance evaluation".

H1: Individualism culture is related to audit quality.

Social cognitive theory suggests that self-efficacy is a dynamic judgment that changes with organizational context, and it can be affected by individuals' forethought of the trade-offs between effort and payoff (He and Freeman, 2010). Organizational culture is one type of environmental influence that impacts the way people (employees) think, perform tasks, and communicate/interact with each other. The culture of an organization provides a corporate framework, which provides guidance on issues like how work is done, the use of technology, how people think, and standards for interaction and communication. It then impacts and can be influenced by people's behavior with respect to various things, such as how to solve problems, how to perform a job, and how to communicate. These, in turn, affect an individual's job performance and satisfaction, impacting firm performance.

H2: Individualism culture is related to self-efficacy.

Self-efficacy refers to the belief in one's capabilities to successfully perform a specific task (Bandura, 1986). Perceived self-efficacy is concerned with judgments of how well one can execute courses of action that are required to deal with prospective situations (Bandura, 1986, p. 122), and 'beliefs in one's capabilities to mobilize the motivation, cognitive resources, and courses of action needed to meet given situational demands' (Wood et al, 2000). Self-efficacy is concerned with whether a person believes he can use his skills in specific circumstances (Stajkovic and Luthans, 1998; Snyder and Lopez, 2009). Self-efficacy has been regarded as a version of self-esteem (Lunenburg, 2011). The basic principle of self-efficacy is assessment, which is generally measured by three basic scales: scale, strength, and general. (Bandura, 1997) contend that performance and motivation are partly determined by the degree to which people believe.

Cybinski and Windsor (2005) found that the relationship between self-efficacy and independent auditor's work may offer a different insight into the domain of the internal auditor and audit quality. (Shih et al, 2009) concluded that there was a significant and positive relationship between the self-efficacy of the auditor and the performance of internal auditors. "Previous studies demonstrate that high self-efficacy improves performance in a wide range of work settings, including education, training, sports and management" (Shea and Howell, 2000). "An individual's belief that he or she has the ability to execute certain tasks contributes to better performance. Individuals with high self-efficacy tend to perform well on a variety of tasks" (Bandura, 1997; Stajkovic and Luthans, 1998) " In contrast, low self-efficacy individuals tend to avoid tasks and situations that they believe exceed their capabilities. Highly motivated auditors only demonstrate a better audit judgment performance when the audit tasks are simple."

H3: Self-efficacy is related to audit quality

Many studies have demonstrated that level of self-efficacy can predict work attitude, job training, work performance, job satisfaction, educational development, and knowledge sharing ((Randhawa, 2004; Cabrera et al, 2006). "Therefore, self-efficacy is widely perceived as one critical factor in determining how much effort and resources a person invests when confronting challenges. Auditors with higher self-efficacy are more likely to continue investing in goal achievement behavior. Therefore, self-efficacy influences behavior by affecting the motivation and confidence to overcome difficulties and improve performance "(Shue-Ching Lee, Jau-Ming Su, Sang-Bing TsaiEmail author, Tzu-Li Lu and Weiwei Dong).

H4: Self-efficacy mediates the relationship between individualism culture and audit quality

### 3. RESEARCH METHODS

The purposive sampling method is used to select the sample. The sample in this study consists of 69 investigative auditors from Indonesian Supreme Audit. The sample selection is presented in Table 1. In 2015, the total number of auditors at Indonesian Audit Supreme was 288. Of the respondents, 198 are not investigative auditors. Of the 90 investigative auditors who sent the questionnaire, 21 were not responsive. Thus, the final sample was 69.

Table 1 – Sample Selection

Description	N
Total auditors	288
Auditor who doesn't include as investigative auditor	(198)
Available sample	90
Respondents didn't respon the questionnaire	(21)
Final sample	69

In this study, the variable of individualism culture is proxied as local culture. The dimensions consist of attitudes, behavior, and symbols. The normative approach views local culture as habits that are common or normatively agreed upon by a particular group. The second independent variable is self-efficacy, which is measured by five dimensions: loyalty to profession, social obligations, independence, confidence, relationship. The instrument was adapted from (Bandura, 1977). The dependent variable of this study is audit quality. It is measured by six indicators: accuracy, skepticism, recommendation, audit benefits, and audit follow-up. Using a 1-5 Likert scale, the respondents are asked to answer the questions. Data analysis was based on variance or the component approach of Structural Equation Modeling SEM-PLS with WarpPLS Program 4.0. The model of this study is as follows:

$$Y = \beta_1 X + \beta_2 Z + \beta_{3M} + \varepsilon$$

$$Z = \beta_1 X + \varepsilon$$

Notation :

Y	= audit quality
Z	= self-efficacy
X	= individualism culture
$\beta_{1, 2}$	= coefficient
$\varepsilon$	= error

### 4. RESULTS

Table 2 presents the result of the correlation test. Based on the table, it can be seen that individualism culture is negatively correlated with self-efficacy and positively related with audit quality. This result also shows that self-efficacy is positively correlated with audit quality.

Table – 2 Correlation of variables

Variables	Individualism culture	Self-efficacy	Audit quality
Individualism culture	1.000	-0.219	0.141
Self-efficacy	-0.219	1.000	0.372
Audit quality	0.141	0.372	1.000

Table 3 exhibits the result of reliability testing of variables. The result shows that all variables have a Cronbach's alpha score higher than 0.60. It suggests that all variables can be reliably analysed.

Table 3 – Coefficient and reliability test of latent variable

Indicator	Individualism culture (X)	Self-efficacy (Z)	Audit quality (Y)
R-squared		0.167	0.288
Adj.R-squared		0.154	0.267
Composite reliable.	1.000	1.000	1.000
Cronbach's alpha	1.000	1.000	1.000
Avg.var.extrac.	1.000	1.000	1.000
Full collin. VIF	1.118	1.272	1.235
Q-squared		0.152	0.290

Table 4 presents the result of WarpPLS for full model testing. Based on the table, it can be shown that all indicators fulfilled the criteria of a fit model. The score for Average Path Coefficient is 0.373 with p-value less than 0.001. The Average R-Squared is 0.228, and the p-value is 0.003.

Table 4 also shows the regression results. The path coefficient of individualism culture  $\longrightarrow$  audit quality is 0.379, and the p-value is less than 0.001. It can be concluded that individualism positively affects audit quality. Thus, H1 is accepted.

The second hypothesis (H2) stated that individualism culture is related to self-efficacy. The regression result shows that the coefficient of individualism culture  $\longrightarrow$  self-efficacy is -0.408 with a p-value less than 0.001. Therefore, the H2 is also accepted. The positive relationship between self-efficacy and audit quality is also supported. The path coefficient self-efficacy  $\longrightarrow$  audit quality is 0.331 (p-value = <0.001).

Finally, the mediation effect of self-efficacy in the relationship between individualism culture and audit quality is shown by the fact that the path coefficient of the indirect effect is positively significant. Thus, H4 is accepted.

Table 4 – Model Fit and Quality Indices, Path Coefficients and p-Values, Indirect, Total Effects, Effect Size - Full Model

Model Fit and Quality Indices		
Average Path Coefficient:	0.373, p < 0.001	
Average R-Squared:	0.228, p = 0.003	
Average Adjusted R-Squared:	0.211, p = 0.004	
Average Block VIF:	1.020, acceptable if <= 5, ideally <= 3.3	
Average Full VIF:	1.208, acceptable if <= 5, ideally <= 3.3	
Tenenhaus GoF:	0.477, small >= 0.1, medium >= 0.25, large >= 0.36	
Path	Coefficient	P-Value
Self-efficacy → Individualism culture	-0.408	<0.001
Audit quality → Individualism culture	0.379	<0.001
Audit quality → Self-efficacy	0.331	<0.001
Indirect Effect		
Audit quality → Individualism culture	-0.135	0.016
Total Effect		
Self-efficacy → Individualism culture	0.408	< 0.001
Audit quality → Individualism culture	0.244	0.003
Audit quality → Self-efficacy	0.331	< 0.001
Effect Size		
Audit quality → Self-efficacy	Coefficient	
Individualism culture → Audit quality	0.167	
Self-efficacy → Audit quality	0.104	
	0.127	

Table 5 – R-Squared, Q-Squared and Full Colinearity VIF

	R-Squared
Audit quality	0.29
Self-efficacy	0.17
Q-Squared	
Audit quality	0.290
Self-efficacy	0.152
Full Colinearity VIF	
Audit quality	1.235
Self-efficacy	1.272

The strengthening of individualism culture positively affects audit quality. This suggests that the culture of the individual auditor improved audit quality; the culture of the individual auditor is based on local wisdom. The result of this study is consistent with the characteristics of cognitive theory. Cognitive learning theory is more concerned with the learning process rather than the result of learning itself. Learning does not just involve the relationship between stimulus and response; learning involves a complex thinking process.

Learning is a change in perception and understanding. Changes in perception and understanding are not always a change in behavior that can be observed.

A change in individualism auditor culture is a learning process that changes the perception and understanding of the ethical audit process, improving the quality of the investigative audit. This study supports a previous study suggesting that the culture of individual auditors is reflected in the audit process of Indonesian Audit Supreme. It influences the quality of the audit (e.g. completion of the audit process at an early stage without improvement of audit procedures).

The culture of individualism auditor negatively affects self-efficacy. Therefore, the diverse acculturation of the individual auditor applied further lowers self-efficacy. The results of this study are not consistent with social cognitive theory. According to the theory, a person believes he/she is able to use his/her skills in specific circumstances (Snyder and Lopez, 2009). Self-efficacy has been regarded as a version of self-esteem (Lunenburg, 2011).

Self-efficacy positively and significantly impacts audit quality, meaning that self-efficacy is an individual performance that is determined by the effectiveness of the trust audited, including the state. Self-efficacy has been regarded as self-actualization (Lunenburg, 2011). Proving that self-efficacy positively and significantly impacts the quality of the audit is necessary for the the potential of science and knowledge in the field of investigative audits; an audit process can be created based on the suitability standard of good governance (transparency, accountability, responsibility, independence and fairness), producing a quality audit that stakeholders expect.

The study also provides empirical evidence that the individual culture of auditors directly influences audit quality, and self-efficacy indirectly influences it. The results of this study partially support previous research; it is possible that the self-efficacy in gathering audit evidence was inadequate, there was inaccuracies in the audit process, or certain audit measures were eliminated. The culture of individual auditors reflected in the behavior at the time of the audit process influences the quality of the investigative audit and includes the completion of the audit process at an early stage without improvement to audit procedures.

## 5. CONCLUSIONS

The individualism culture of the auditor positively affects the quality of audit. The results are consistent with the characteristics of social cognitive theory. Cognitive learning theory is concerned with the learning process rather than the results of learning. The individualism culture of the auditor negatively affects self-efficacy. The result is not consistent with social cognitive theory. Self-efficacy positively affects the quality of the audit. That is, self-efficacy is the performance and motivation of auditor and is determined by the confidence of the auditor, which will improve the quality of the audit. Self-efficacy mediates the relationship between individualism culture and audit quality. This study provides empirical evidence that culture influences audit quality directly or indirectly through self-efficacy.

Theoretically, this study contributes to the organizational behavior and accounting literature. Practically, the results of this study can be used as a reference for various parties regarding the individual culture of the auditor. Specifically, this study is for the Supreme Audit Agency, the Inspectorate, Directorate General of Taxes, government internal auditors and independent auditors and academics in the field of accounting education. Future study may consider other variables which are expected to affect audit quality, such as competence, independence, experience in auditing, integrity, quality control, client industry specialization, and audit quality benchmarks.

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