

The effect of auditing quality and internal control on financial resilience in public sector organizations: Information quality as the mediating factor

Pius Lustrilanang^{a,b*}, Suwarno^{a,c}, Bahtiar Arif^{a,c} and Hery Subowo^{a,c}

^aState Audit Board of Republic of Indonesia, Jakarta, Indonesia

^bUniversitas Jenderal Soedirman, Purwokerto, Indonesia

^cInstitut Bisnis dan Informatika Kesatuan, Bogor, Indonesia

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ABSTRACT

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In dynamic socio-economic environments, public sector organizations and companies with strong financial resilience are better equipped to adapt to economic changes, socio-economic fluctuations, and shifts in the business landscape with greater flexibility. Financial resilience also has implications for an organization's liquidity. One of the critical factors influencing financial resilience in public sector organizations is the quality of its audit. Ensuring high-quality audits is vital for assessing the accuracy and reliability of an organization's financial statements. This study aims to investigate the impact of audit quality and internal control on financial security, with information quality serving as a mediating factor. Quantitative research methods were employed to collect and statistically analyze the data. The study gathered information through questionnaires distributed to the Auditors of the Supreme Audit Board, with a sample size of 321 participants. The data was then processed using SmartPLS software. The research findings demonstrate a significant relationship between audit quality and internal control, positively influencing the organization's financial resilience. Furthermore, the study reveals that information quality acts as a crucial mediator, linking audit quality and internal control to financial security. The analysis shows that audit quality significantly affects information quality. However, the direct impact of audit quality on financial resilience is not significant. On the other hand, internal control significantly influences both information quality and the organization's financial resilience. Additionally, the quality of information also has a significant effect on the organization's financial resilience.

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1. Introduction

In the ever-changing socio-economic landscape, the financial resilience of public sector organizations and companies plays a vital role in ensuring their long-term sustainability (Tien et al., 2020). Financial resilience refers to the ability of an organization to withstand economic challenges and pressures, enabling it to continue operating effectively in the long run (Barbera et al., 2017). Amidst evolving conditions, organizations with strong financial resilience are better equipped to navigate economic changes, market fluctuations, and shifts in the business environment with greater adaptability. Additionally, financial resilience also impacts the liquidity of the organization. According to Ahrens and Ferry (2020), organizations with robust financial resilience can maintain sufficient cash flow to meet daily obligations, such as debt payments, operational expenses, and investments in growth. In a dynamic business environment, unexpected fluctuations in income and costs can affect the liquidity of an organization. Therefore, having sound financial resilience is crucial in ensuring smooth operations and maintaining the financial stability of the organization or company (Zimon, 2018). Moreover, financial resilience plays a significant role in enhancing the ability of organizations and companies to withstand crises (Barbera et al., 2020). Economic crises and

* Corresponding author.

E-mail address: plustrilanang.unsoed@gmail.com (P. Lustrilanang)

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unexpected events often test the resilience of businesses, and having strong financial resilience enables them to endure and recover more rapidly. Through maintaining adequate reserves, financial flexibility, and a robust risk management strategy, organizations and companies can better navigate the challenges posed by crises and mitigate their adverse impact on financial stability (Belayeth Hussain et al., 2019). Possessing sufficient financial strength empowers organizations and companies to capitalize on emerging opportunities and compete effectively in a dynamic market. A solid foundation of financial resilience supports long-term growth and ensures sustainability (Tien et al., 2020; Klapper & Lusardi).

The quality of audit in public sector organizations is a significant determinant of its financial resilience. High-quality audits are essential for accurately evaluating the reliability of financial statements (Nkundabanyanga et al., 2020). These audits inspire confidence in investors and stakeholders, assuring them that the financial statements present an authentic representation of the financial position (Amahalu, 2020; Wang et al., 2017). Conversely, low-quality audits create doubts and uncertainties regarding the credibility of the financial information disclosed (Kuntari et al., 2017). Another crucial factor contributing to strong financial resilience is the implementation of effective internal control measures. Akhmetshin et al. (2018) define internal control as a collection of procedures, policies, and actions employed by public sector organizations to safeguard its assets, manage risks, and ensure compliance with internal regulations and policies. A robust internal control system helps mitigate the risks of fraud, errors, and misuses of assets, thereby instilling stakeholders with confidence in the reliability of financial information (Setyorini et al., 2021; Mexmonov, 2020). In a study conducted by Pandapotan et al. (2023), it was shown that high-quality audits and effective internal controls have a positive impact on stakeholder confidence, reducing the risks of errors and fraud, and enhancing transparency and accountability within an organization. However, to obtain a more comprehensive understanding of this relationship, further research is needed. Additionally, it is crucial to consider mediating factors that may play a significant role in this context. One such mediating factor is the accuracy, reliability, and relevance of the information presented in the financial statements. When financial information is of good quality, it improves stakeholders' comprehension and confidence in the financial statements, thereby influencing their perception of the organization's financial resilience. Thus, the primary objective of this research is to investigate the effects of audit quality and internal control on financial resilience, while also considering the mediating factor of information quality (Pandapotan et al., 2023).

2. Literature Review

2.1 *The Effect of Auditing Quality on Information Quality and Financial Resilience*

Audit quality refers to evaluating or gauging the standard of audit work performed by auditors (Ismail et al., 2020). It entails assessing the extent to which auditors adhere to relevant audit standards and conduct audits diligently, comprehensively, and objectively. The level of audit quality can significantly impact the reliability of audited financial statements and the confidence that investors and stakeholders have in the organization's financial information (Amahalu, 2020). Several critical aspects contribute to audit quality. Firstly, professionalism is a key element. High-quality auditors possess expertise, competence, and independence (Hai & Quy, 2019; Trotman & Duncan, 2018). They conduct thorough risk assessments of the audited entity (Wang et al., 2017) and collect and evaluate audit evidence that is relevant, sufficient, and precise. Adherence to applicable audit standards is also essential for audit quality, as high-quality auditors comply with established guidelines. Lastly, effective communication and reporting are vital components of audit quality, with high-quality auditors presenting clear, transparent, and accurate audit reports (Svårdsten, 2019).

Regarding information quality, audit quality plays a vital role in ensuring the reliability and accuracy of the information presented in financial statements. High-quality auditors meticulously examine and verify the organization's transactions, accounting records, and disclosures (Nwanyanwu, 2017; Kaawaase et al., 2021). Furthermore, audit quality contributes to verifying the organization's compliance with relevant accounting standards and regulations. High-quality auditors assess the organization's adherence to accounting principles, appropriate disclosures, and legal and regulatory requirements (Hai & Quy, 2019). Additionally, audit quality aids in detecting errors and fraud in the financial reporting process. High-quality auditors conduct thorough analyses of the organization's internal control system, test its sufficiency and effectiveness, and provide recommendations to address any identified weaknesses (Mexmonov, 2020). Moreover, audit quality encompasses the assessment of the organization's internal control system. High-quality auditors conduct evaluations to ensure robust internal controls, safeguard assets, mitigate fraud risks, improve financial reporting accuracy, and optimize resource utilization (Boskou et al., 2019). Additionally, good audit quality enhances the financial transparency of the public sector organizations. High-quality auditors also offer valuable advice and recommendations to the organization's management (Abdullah et al., 2018; Trotman & Duncan, 2018). These recommendations may cover process improvements, internal controls, resource efficiency, or enhanced financial policies. By implementing such suggestions, the organizations can enhance its efficiency, reduce costs, and strengthen its financial resilience. High-quality auditors play a crucial role in ensuring the organization's compliance with relevant financial regulations (Nwanyanwu, 2017; Pandapotan et al., 2023). Improved compliance with regulations minimizes the risk of sanctions or legal claims that could potentially disrupt financial stability. Consequently, the hypotheses in this research can be summarized as follows:

H₁: *Audit quality positively influences information quality.*

H₂: *Audit quality positively influences financial resilience.*

2.2 The Effect of Internal Control on Information Quality and Financial Resilience

Internal control refers to a set of measures, policies, and procedures put in place by an organization's management to ensure that its business operations align with the organization's objectives, established policies, relevant regulations, and ethical standards (Napitupulu, 2023). The primary goal of internal control is to protect an organization's assets, maintain the integrity of financial data, ensure the reliability of financial reporting, and enhance operational efficiency and effectiveness (Kuntadi et al., 2023; Tien et al., 2020). Internal control is a crucial component in preserving the integrity, reliability, and sustainability of an organization's operations. It plays a significant role in preventing and detecting errors, misappropriation, fraud, and safeguarding assets from losses and misuse. Moreover, as noted by Erasmus & Coetzee (2018), internal control also inspires confidence in external stakeholders, such as investors, creditors, and government entities, regarding the quality of the organization's financial information.

Internal control has a significant impact on the quality of information produced by an organization. According to Al-Waeli et al. (2020), well-executed internal control measures enhance the reliability, accuracy, error and fraud detection, compliance, and security of information. By implementing appropriate procedures and controls, internal control ensures the integrity and dependability of information presented in financial statements and other documents. Effective controls also reduce the risk of errors and fraud, ensuring adherence to relevant standards and regulations (Turedi & Celayir, 2018; Lartey et al., 2020). Furthermore, internal control plays a vital role in information security through measures such as access controls and data protection. By implementing robust controls, companies can identify and manage financial risks, safeguard their assets, optimize cash management, establish consistent financial policies and procedures, and conduct regular financial monitoring and evaluation (Vovchenko et al., 2017). Strong internal control empowers companies to fortify their financial resilience in the face of unforeseen circumstances and maintain long-term financial stability. The third and fourth hypotheses in this research can be summarized as follows:

H₃: *Internal control has a positive influence on information quality.*

H₄: *Internal control has a positive influence on financial resilience.*

2.3 The Mediating Effect of Information Quality

Information quality refers to the degree of trustworthiness, accuracy, relevance, usefulness, and clarity of information presented within a specific context (Napitupulu, 2023). Information that is reliable, free from errors and biases, and meets the needs of users, facilitating informed decision-making, is considered high-quality (Napitupulu, 2023). High-quality information fosters trust, supports effective decision-making, and contributes to overall organizational performance (Dewi et al., 2019; Abubakar et al., 2019). The quality of information significantly influences an organization's financial resilience. High-quality information enables efficient decision-making, effective risk management, accurate financial reporting, robust performance evaluation, and financial planning, thereby instilling confidence among stakeholders (Kuntadi et al., 2023; Barbera et al., 2020). By providing accurate, reliable, and relevant information, companies can enhance their stability and financial resilience in the face of business challenges. According to Amahalu (2020), high-quality audits ensure reliability, accuracy, and adherence to audit standards, while effective internal control manages financial risks, safeguards assets, and ensures compliance. However, the mediating role of information quality is crucial in this context, as it hinges on the quality of information generated through the audit and internal control processes. High-quality information influences informed decision-making, guides appropriate management actions, strengthens financial resilience, and provides a comprehensive understanding of the organization's financial condition (Vovchenko et al., 2017; Dewi et al., 2019; Nwanyanwu, 2017). Information quality acts as a critical link between audit quality, internal control, and financial resilience. Robust audit processes and effective internal control that produce accurate, reliable, and relevant information establish a solid foundation for financial resilience (Sumaryati et al., 2020). By identifying financial risks, addressing internal control weaknesses, and presenting high-quality financial information, companies can undertake appropriate measures to manage risks, strengthen internal control, and ensure long-term financial stability. Therefore, the subsequent hypotheses in this research can be summarized as follows:

H₅: *Information quality has a positive influence on financial resilience.*

H₆: *Information quality can mediate the relationship between auditing quality and financial resilience.*

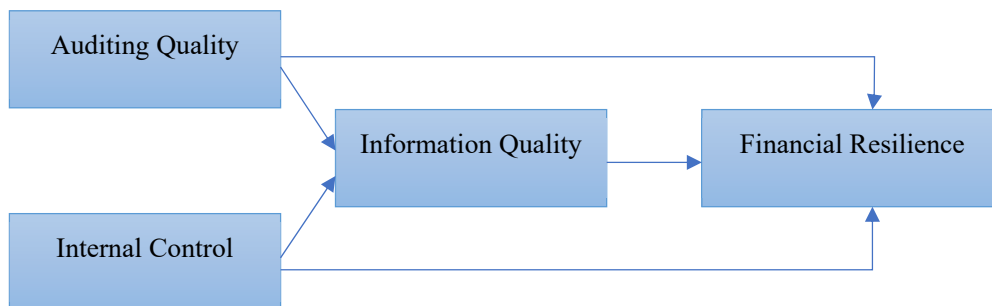


Fig. 1. Conceptual Framework

3. Method

The research method employed in this study was quantitative in nature, aiming to collect and analyze data through statistical means. Data for the study were gathered using a questionnaire that was distributed to auditors of the Audit Board of the Republic of Indonesia. The questionnaire utilized a Likert scale ranging from 1 to 7 points, allowing respondents to express their level of agreement or disagreement with the statements provided. Initially, there were 370 respondents involved in the study. However, 33 questionnaires were not returned, and 16 questionnaires were incomplete, rendering them unsuitable for analysis. As a result, the final sample size available for further analysis consisted of 321 respondents.

The collected data were subjected to analysis using SmartPLS software, which is a tool commonly used for partial least squares (PLS) analysis in quantitative research. In summary, this research followed a quantitative approach, collecting data through a questionnaire distributed to auditors of the Audit Board of the Republic of Indonesia. The Likert scale provided a range for respondents to indicate their agreement or disagreement with the questionnaire statements. After receiving and filtering the responses, a final sample size of 321 respondents was considered for analysis. SmartPLS software was used to conduct the statistical analysis, employing partial least squares (PLS) analysis as the chosen method for data evaluation. The analysis conducted in this study utilized the SmartPLS software to examine the extent of influence that independent variables have on the dependent variable. Initially, the analysis involved testing the reliability of the constructs used to measure the latent variables. There were 5 constructs employed to measure auditing quality, 4 for internal control, 4 for information quality, and 5 for financial resilience. The analysis test model in this study sought to elucidate the relationships between the latent variables and the constructs. This was demonstrated through the loading factor values, which were found to be above 0.6, indicating a strong relationship between the variables. SmartPLS software was employed to analyze the data, evaluating how the independent variables influenced the dependent variable. The study also assessed the reliability of the constructs used to measure the latent variables.

4. Result

The test results indicate that all five constructs used to measure auditing quality have loading factor values ranging from 0.770 to 0.878, which demonstrates their reliability. Similarly, the four constructs assessing internal control variables have loading factor values ranging from 0.866 to 0.908, indicating their reliability as well. In the case of information quality variables, all four constructs show loading factor values between 0.867 and 0.905, and for financial resilience variables, all five constructs have loading factor values ranging from 0.832 to 0.958, affirming the reliability of these constructs. Additionally, validity and reliability analyses were conducted to further establish the validity and reliability of the constructs used in this study. The validity test assessed whether the constructs effectively measured the intended latent variables. This was confirmed by observing the Average Variance Extracted (AVE) value, which was higher than 0.6 for all constructs. Moreover, the reliability test evaluated the consistency of the constructs in measuring latent variables. This was determined through the Cronbach Alpha value, which was higher than 0.7, and the Composite Reliability (C.R.) value, which also exceeded 0.7 for all constructs. In summary, the study employed both loading factor analysis and validity and reliability tests to verify the reliability and validity of the constructs used in measuring the various latent variables. The results demonstrated that all constructs were reliable and effectively captured the intended latent variables. The results presented in Table 1 and Fig. 2 provide insights into the relationships between the variables under investigation.

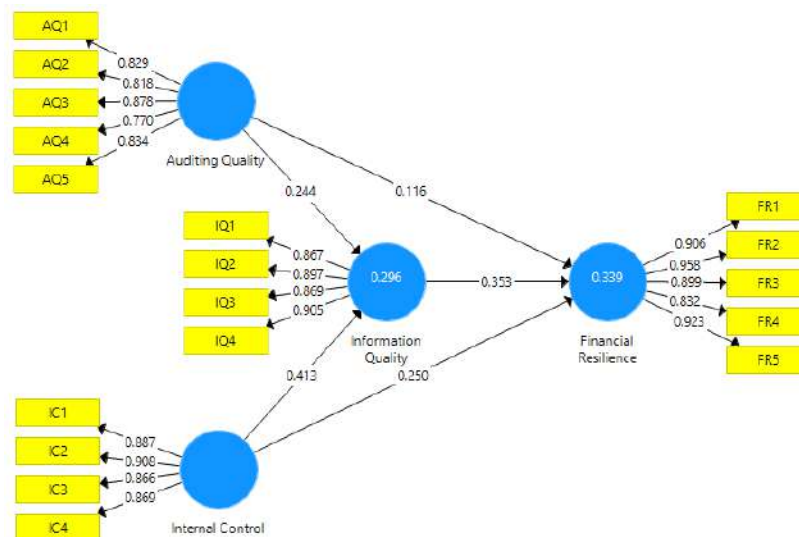


Fig. 2. Measurement Model

Table 1
Std. Loading Factor Value

Variable	Construct	Std. Loading Factor
Auditing Quality	AQ1	0.829
	AQ2	0.818
	AQ3	0.878
	AQ4	0.770
	AQ5	0.834
Internal Control	IC1	0.887
	IC2	0.908
	IC3	0.866
	IC4	0.869
Information Quality	IQ1	0.867
	IQ2	0.897
	IQ3	0.869
	IQ4	0.905
Financial Resilience	FR1	0.906
	FR2	0.958
	FR3	0.899
	FR4	0.832
	FR5	0.923

The results presented in Table 2 indicate that the auditing quality variable achieved an Average Variance Extracted (AVE) value of 0.683 (> 0.6), a Cronbach's Alpha value of 0.885 (> 0.07), and a Composite Reliability (C.R.) value of 0.915 (> 0.7). This confirms that the construct used to measure auditing quality is both valid and reliable. Similarly, for the internal control variable, the AVE value obtained was 0.779, with a Cronbach's Alpha of 0.906 and a C.R. of 0.934, signifying the validity and reliability of the constructs used to measure internal control. Moreover, the information quality variable achieved an AVE value of 0.782, a Cronbach's Alpha of 0.907, and a C.R. of 0.935, while the financial resilience variable obtained an AVE value of 0.817, a Cronbach's Alpha of 0.944, and a C.R. of 0.957. These results demonstrate that the constructs used to assess information quality and financial resilience are also valid and reliable.

Table 2
Validity and Reliability

Variable	Average Variance Extracted (AVE)	Cronbach's Alpha	Composite Reliability (C.R.)
Auditing Quality	0.683	0.885	0.915
Internal Control	0.779	0.906	0.934
Information Quality	0.782	0.907	0.935
Financial Resilience	0.817	0.944	0.957

The subsequent analysis conducted is the model fit test, an essential step in statistical analysis that assesses how well the model employed in the study aligns with the observed data. The purpose of the model fit test is to ensure that the model accurately captures the patterns present in the data and aligns with the proposed hypotheses. This test holds significant importance in validating the model utilized for the research.

Table 3
Model fit test

Indexes	Saturated Model	Estimated Model
SRMR	0.061	0.061
d_ULS	0.628	0.628
d_G	0.343	0.343
Chi-Square	320.739	320.739
NFI	0.867	0.867

To assess the appropriateness of the model in capturing the relationships between variables in the study, various statistics in the summary of model fit can be examined. One such statistic is the Standardized Root Mean Squared Residual (SRMR), where a value below 0.10 indicates a good fit of the model. Another important indicator is the Normal Fit Index (NFI) value, which should be close to 1.0, signifying a better fit of the model to the data. As shown in Table 5, the results of the fit model test reveal an SRMR value of 0.061 (less than 0.10) and an NFI value of 0.867 (very close to 1.0). Therefore, it can be concluded that the model used in this study is well-aligned with the observed data, indicating its suitability in describing the relationships between the variables.

Regarding the influence of the independent variable on the information quality variable, the R-Square value was found to be 0.296 (Adjusted R Square of 0.288). On the other hand, the financial resilience variable showed an R-Square value of 0.339 (Adjusted R Square of 0.326). These values suggest that while the impact of the independent variables on the information

quality variable is relatively low, they have a moderate level of influence on the financial resilience variable (Table 3).

Table 4

R-Square

Variable	R Square	Adjusted R Square
Information Quality	0.296	0.288
Financial Resilience	0.339	0.326

In this study, two types of hypothesis testing were employed: direct hypothesis testing and indirect hypothesis testing, also known as mediation. Direct hypothesis testing aimed to evaluate the direct impact of the independent variables on the dependent variable. On the other hand, hypothesis testing using mediating factors sought to examine whether the relationship between the independent variables and the dependent variable could be influenced by the mediating variables incorporated in the analysis. The significance of these hypothesis tests was determined based on the obtained statistical T value and P value. A T value greater than 1.96 and a P value less than 0.05 indicated that the hypotheses had a significant effect and were thus accepted.

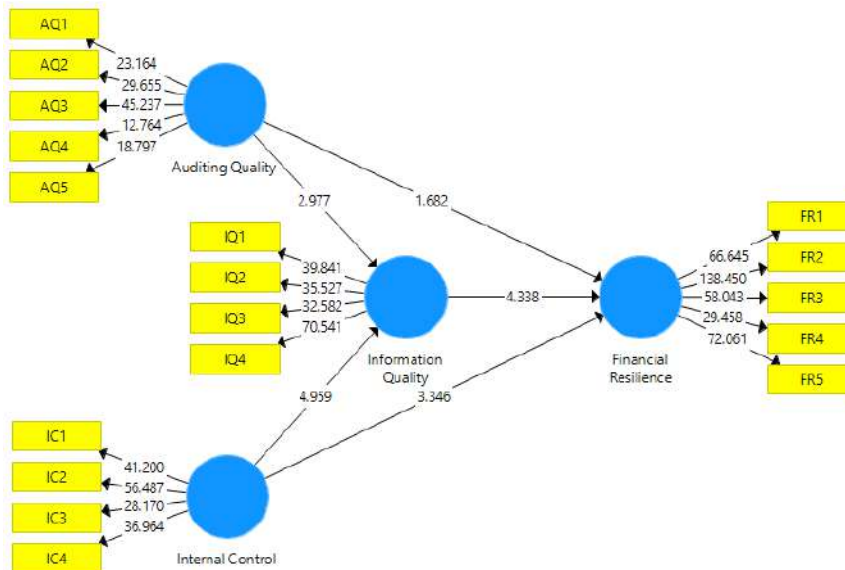


Fig. 3. Path Coefficient

Table 5

Hypothesis testing

Hypothesis	T Statistics	P Values	Information
H1 Auditing Quality → Information Quality	2.977	0.003	Accepted
H2 Auditing Quality → Financial Resilience	1.682	0.095	Rejected
H3 Internal Control → Information Quality	4.959	0.000	Accepted
H4 Internal Control → Financial Resilience	3.346	0.001	Accepted
H5 Information Quality → Financial Resilience	4.338	0.000	Accepted
H6 Auditing Quality → Information Quality → Financial Resilience	2.551	0.012	Accepted
H7 Internal Control → Information Quality → Financial Resilience	3.126	0.002	Accepted

The outcomes of the hypothesis testing presented in Table 5 reveal that the first hypothesis, which examines the impact of auditing quality on information quality, demonstrated a significant influence. The T statistics value obtained was 2.977 (> 1.96), and the P value was 0.003 (< 0.05), confirming the significance of this relationship. However, the second hypothesis, which investigated the effect of auditing quality on financial resilience, did not yield a significant result. The T statistics value obtained was only 1.682, and the P value was 0.095, indicating that the second hypothesis has no significant effect. On the other hand, the third and fourth hypotheses, which explored the influence of internal control on information quality and financial resilience, respectively, exhibited significant effects. The statistical T values obtained were 4.959 and 3.346, with corresponding P values of 0.000 and 0.001, respectively. As a result, the third and fourth hypotheses were accepted, demonstrating that internal control indeed has a significant impact on both information quality and financial resilience. Furthermore, the fifth hypothesis, investigating the effect of information quality on financial resilience, also showed a significant impact. The statistical T value obtained was 4.338, with a P value of 0.000, providing evidence of the significant relationship between information quality and financial resilience. Moreover, the results of hypothesis testing using mediating variables (information quality) in the sixth and seventh hypotheses demonstrated significant effects. The statistical T values obtained were 2.551 and

3.126, with P values of 0.012 and 0.002, respectively. Hence, the sixth and seventh hypotheses were accepted, confirming that information quality acts as a suitable mediator, bridging the effects of auditing quality and internal control on financial resilience.

5. Conclusion

In conclusion, the findings of this study highlight the significant impact of auditing quality and internal control on an organization's financial resilience. Moreover, information quality emerges as a crucial mediating factor that links audit quality and internal control to financial security. The analysis reveals that high-quality audits have a positive effect on information quality, leading to improved information generated by the organization. However, it is important to note that audit quality does not directly influence financial resilience. Instead, the effect of audit quality on financial security is primarily mediated by the quality of information. Furthermore, the study demonstrates that effective internal control significantly influences both information quality and organization's financial resilience. A robust internal control system contributes to enhancing the quality of information and financial security. This suggests that well-implemented internal control measures play a pivotal role in ensuring accurate and reliable information, as well as effectively managing financial risks. Additionally, the quality of information itself exerts a significant influence on an organization's financial resilience. High-quality information supports sound decision-making, effective risk management, and better financial performance. As a result, information quality acts as a vital mediator in the relationship between audit quality, internal control, and financial security. The presence of high-quality information, generated through a robust audit process and effective internal control, establishes a firm foundation for the organization to manage risks, strengthen internal control, and achieve sustainable financial resilience in the long run.

This research contributes significantly to our comprehension of the interconnections among audit quality, internal control, information quality, and corporate financial resilience. The findings underscore the importance for companies to prioritize and maintain high audit quality, enhance their internal control systems, and ensure the provision of reliable information to bolster strong and sustainable financial resilience. Despite the limitations of this study, it provides valuable insights for businesses in fostering their financial robustness. Given the scope of this study, it is recommended that future research be carried out to delve deeper into other potential factors that may influence the relationship between audit quality, internal control, information quality, and financial security. These factors could encompass external elements, such as governmental regulations, shifts in the business landscape, or volatile market conditions, which might have an impact on the dynamics of these variables. Expanding the investigation to include these external factors would provide a more comprehensive understanding of the overall impact on financial resilience and facilitate the development of more effective strategies for companies to weather challenges and uncertainties in their operating environments.

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