

-RESEARCH ARTICLE-

THE EFFECT OF AUDIT COMMITTEE, INTERNAL AUDITOR AND AUDIT QUALITY ON FIRM VALUE ON HOTEL INDUSTRY IN INDONESIA

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—Abstract—

Firm value is a crucial element for organizational success, necessitating emphasis from contemporary researchers. This study examines the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on the firm value within Indonesia's hotel industry. Primary data were collected through survey questionnaires administered to the audit departments of hotels. Smart-PLS was employed to assess data reliability and the relationships among variables. The findings reveal a positive relationship between audit committee effectiveness, audit quality, internal auditor effectiveness, and firm value in the hotel industry in Indonesia. This article provides guidance for regulators on enhancing firm value through the implementation of effective audit committees, comprehensive audit quality, and efficient internal auditing practices.

Keywords: Audit Committee Effectiveness, Audit Quality, Internal Auditor Effectiveness, Firm Value, Hotel Industry in Indonesia.

INTRODUCTION

This study examines the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on firm value within Indonesia's hotel industry. As a significant subsector contributing to tourism, employment, and GDP, the hotel industry faces challenges in maintaining profitability in a competitive environment. Effective corporate governance is essential for organizational financial stability and enhancing firm value. Recent academic and professional literature has increasingly focused on the roles of audit committees, internal auditors, and audit quality. This research aims to evaluate how these governance components influence firm value in the Indonesian hotel industry, thereby elucidating the importance of robust audit practices for improving financial performance and stakeholder confidence. Corporate governance is crucial for effective management and operational efficiency (Al-Ahdal et al., 2020). An audit committee, typically composed of independent directors, oversees the financial reporting process, internal controls, and auditing activities. This oversight ensures that the company's financial statements accurately represent its financial condition and serves as a legal safeguard against fraudulent activities. A competent audit committee is therefore a significant asset for Indonesian hotel firms, as it helps manage the complex operational and financial relationships inherent in the industry. This, in turn,

can enhance managerial decision-making and increase firm value (Malik et al., 2021). In assessing the effectiveness of audit committees, factors such as independence, expertise, and the activities conducted by the committee in fulfilling its oversight responsibilities are critical metrics for evaluation (Oussii & Boulila, 2021). Notably, research indicates that a higher frequency of audit committee meetings and the presence of directors with substantial financial expertise enhance the likelihood of identifying and preventing improper financial reporting. This, in turn, is associated with increased firm value.

Internal auditors occupy a pivotal role within organizations by assessing the efficiency of business activities, managing risks, and overseeing governance systems. They conduct evaluations and identify weaknesses, threats, and opportunities for improvement (Nedyalkova, 2020). This role is particularly significant in the hotel industry, where effective operational management and risk mitigation are essential for sustained profitability. Chen et al. (2020) assert that robust internal auditing contributes to better decision-making, efficient resource utilization, and enhanced firm value. Internal auditors ensure that risk management, governance, and internal controls are appropriately managed, offering an impartial perspective and recommending necessary changes. This function is crucial in the hotel sector due to frequent cash transactions, complex operational procedures, and extensive customer interactions. Audit quality also significantly impacts firm value. High-quality audits ensure that financial statements accurately reflect the company's financial position, thereby boosting investor confidence and supporting informed decision-making (Atrizka & Pratama, 2022; Gold et al., 2020; Ruslan et al., 2023; Tambunan et al., 2023). Key attributes influencing audit quality include auditor competence, independence, and adherence to standards. Variations in audit quality within the Indonesian hotel industry have affected the credibility of reported financial information (Astuty et al., 2022; Pratama et al., 2019; Siregar et al., 2023; Syofyan et al., 2021). This study aims to evaluate the impact of audit quality on firm value within this sector, considering relevant regulations and market conditions. Evidence suggests that high audit quality mitigates information asymmetry between the company and stakeholders, reducing the cost of capital and enhancing firm value. Thus, higher audit quality is typically associated with large audit firms possessing adequate resources and expertise to deliver effective audits.

The primary research question for this study is to establish the significance of audit committee effectiveness, internal audit functions, and audit quality on the value of Indonesian hotel firms. Specifically, the research objectives are to determine how these mechanisms enhance financial transparency, operational efficiency, and stakeholders' trust. This study aims to operationalize a comprehensive measure of auditing practices in relation to various quantitative measures of firm value among publicly listed hotel companies in Indonesia. The major objective is to provide critical recommendations for improving corporate governance in the hotel industry. This research contributes to the

literature on corporate governance by addressing the scarcity of studies focused on the Indonesian hotel sector. While extensive research exists on the relationship between corporate governance mechanisms and firm value across various industries, the fast-growing, compliance-challenged, and diverse operational environment of the Indonesian hotel industry remains underexplored. By presenting findings on audit committee effectiveness, internal audit functions, and audit quality, this study fills a significant gap in the literature and offers systematic insights that can strengthen governance initiatives and organizational performance in this crucial sector. In the next section of this study, we will review the relevant literature, outline the research methodology, and conduct a comprehensive empirical analysis to test the proposed hypotheses.

LITERATURE REVIEW

Firm value is a critical factor for organizational success, warranting renewed focus from researchers. This study investigates the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on the firm value within the Indonesian hotel industry (Cahyadi et al., 2023; Danilwan & Pratama, 2020; Pratama et al., 2019; Sibuea et al., 2020). The audit committee plays a pivotal role in enhancing firm value, especially in the hotel sector, by ensuring robust financial management, which is essential for maintaining investor confidence and organizational integrity. Composed of non-executive directors and focusing on financial oversight, the audit committee is tasked with monitoring the company's financial reporting, management, internal controls, and audit activities (Pratama et al., 2019; Raimo et al., 2021; Saragih et al., 2020; Tambunan et al., 2022). This omission mitigates risks associated with financial statement errors and fraud, thereby enhancing the credibility of financial reports. In the context of the hotel industry, characterized by significant cash flows and a complex functional structure, Almaqoushi and Powell (2021) indicate that the effectiveness of the audit committee is markedly improved due to the large volume of financial data involved. Chen et al. (2023) demonstrate that hotels with robust audit committees exhibit increased firm value, superior stock price performance, and higher valuation multiples. This positive effect is largely attributed to the audit committee's role in ensuring accurate financial disclosures, which are crucial for investment decisions (Heikal et al., 2019; Lubis et al., 2015; Pratama et al., 2019; Simanjuntak et al., 2024; Utami et al., 2019).

Additionally, Al Farooque et al. (2020) highlight that effective audit committees contribute to good governance by reducing agency costs and aligning management with shareholder interests. The presence of frequent audit committee meetings and the inclusion of at least one non-executive director and one financially experienced member are particularly effective in enhancing the audit committee's ability to identify and address potential financial misconduct (Biswas et al., 2023; Tambunan et al., 2022;

Tanjung et al., 2022). This active and knowledgeable oversight not only protects the firm from recurring fraudulent incidents but also enhances its market reputation. Consequently, investors are more confident in investing in firms with efficient audit committees, thereby bolstering firm value. Therefore, we propose that,

H1: *Audit committee has a positive effect on firm value on hotel industry.*

Internal auditors significantly enhance stakeholder firm value in the hotel industry by improving operational efficiency, managing risks effectively, and maintaining robust internal controls (Busru et al., 2020). They are crucial in environments characterized by extensive cash transactions and complex procedures. According to Nedyalkova and Nedyalkova (2020), internal auditors systematically examine and evaluate organizational processes, identifying inherent weaknesses, risks, and flaws in business procedures. These proactive measures enable hotels to allocate resources efficiently, prevent potential negative events, and sustain profitability. Kabuye et al. (2019) further highlight that well-developed internal audit functions contribute to higher firm value by providing valuable guidance that supports improved decision-making and strategic planning. Internal auditors offer objective input to management, addressing issues that could negatively impact performance and minimizing costly errors. An effective internal audit team also projects a positive image to investors and stakeholders by demonstrating adherence to governance and accountability standards (Mashayekhi et al., 2022). This, in turn, enhances investor confidence, increases investment, and boosts firm value. The positive impact of internal auditors is evident through better reporting standards and heightened compliance with regulations, which bolster the company's market reputation and credibility. As change agents, organizational internal auditors play a critical role in maintaining effectiveness and accountability, thereby significantly contributing to firm value (Roussy et al., 2020). Therefore, we propose that,

H2: *Internal auditor has a positive effect on firm value on hotel industry.*

According to Mbir et al. (2020), audit quality significantly enhances firm value within the hotel industry by improving the accuracy of financial information and bolstering investor confidence and corporate governance. To achieve high-quality audits, it is essential to engage competent auditors who perform thorough independent checks of the accuracy of internal financial statements (Shivaram et al., 2021). Accurate financial reporting is crucial for enhancing investor credibility, as it aids investors in making informed investment decisions. Hotels with high-quality audits are found to have greater firm value, as these audits help prevent fraud and financial misstatements (Agyemang et al., 2023). The market reputation of reputable audit firms also enhances the market credibility of the hotel, attracting more investors. Additionally, Thottoli (2021) notes that high-quality audits protect firms from legal non-compliance penalties and contribute to organizational stability by ensuring all regulatory requirements are met. This is particularly important in the hotel industry, which is subject to numerous

laws and operational challenges. Furthermore, [Shahzad et al. \(2019\)](#) demonstrate that audit quality positively affects the reduction of the cost of capital, as investors prefer firms that offer quality assurance and accurate financial statements. Lower capital costs, resulting from high audit quality, can lead to increased firm value. Effective audits also enhance internal controls and risk management practices, thereby improving hotel operations and reducing long-term costs ([Kabuye et al., 2019](#)). Thus, audit quality positively influences firm value, underscoring the importance of high audit standards and the careful selection of auditors. Improvements and advancements in accredited audits are crucial for enhancing firms' worth and sustainability in the hotel industry by ensuring financial soundness and regulatory compliance. Therefore, we propose the hypothesis that,

H3: *Audit Quality has a positive effect on firm value on hotel industry.*

RESEARCH METHODS

The study examines the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on the firm value within the hotel industry in Indonesia. Primary data was collected through survey questionnaires distributed to the audit departments of hotels in Indonesia. The constructs were measured using specific items: audit committee effectiveness was assessed with seven items based on ([Krishnamoorthy et al., 2002](#)) audit quality was evaluated using seven items adapted from ([Masood & Afzal, 2016](#)) internal auditor effectiveness was measured with five questions derived from ([Khan et al., 2020](#)) and firm value was gauged with three questions sourced from ([Karman et al., 2024](#)). [Table 1](#) presents these measurement items.

The study targeted employees from the audit departments of hotels in Indonesia as respondents. Participants were selected using purposive sampling, and surveys were distributed through personal visits to the hotels. Out of 534 surveys sent, 290 were completed and returned, yielding a response rate of 54.31%. Additionally, Smart-PLS was employed to assess data reliability and examine associations among variables. Smart-PLS is a preferred data analysis tool for large datasets due to its robustness ([Hair Jr et al., 2020](#)). The study analysed three independent variables: audit committee (AC), internal auditor (IA), and audit quality (AQ), and one dependent variable: firm value (FV). [Figure 1](#) illustrates these variables.

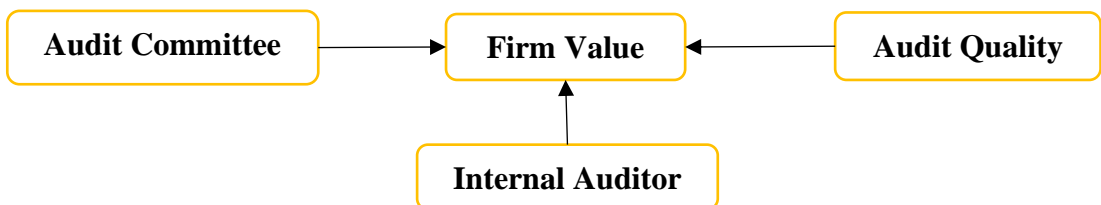


Figure 1: Research Framework

Table 1: Measurements and Variables

Items	Statements	Sources
Audit Committee		
AC1	The role of audit committee to ensure the audit quality that enhance firm value.	(Krishnamoorthy et al., 2002)
AC2	The role of audit committee to ensure the quality financial reporting that enhance firm value.	
AC3	Audit committee effectiveness reduce the fraud in the firm.	
AC4	Audit committee should have enough power to confront management.	
AC5	Audit committee should have enough time and resource to conduct audit.	
Audit Quality		
AQ1	Audit reports are free of personal biases.	(Masood & Afzal, 2016)
AQ2	Audits are transparent in nature.	
AQ3	Audits reports are timely reported to management.	
AQ4	Audit reports are effective to highlight corruption in audited body.	
AQ5	Audit reports are purely based on objectivity.	
AQ6	Top management fully discloses true audit findings to general public.	
AQ7	Frequency of audits in same firm improves the audit quality.	
Internal Auditor		
IA1	The IA system improves the operation of the business.	(Khan et al., 2020)
IA2	The staff of IA is deemed sufficient.	
IA3	IA ensures the economical, effective and efficient use of resources.	
IA4	The audit procedures and evidence collections are completed on time.	
IA5	There are disciplinary consequences to perpetrators of fraud.	
IA6	There are special control services in all departments of the business.	
IA7	The safeguards of the control system prevent illegal activities	
Firm Value		
FV1	During the last 6 months in our organization the quality of the products has increased.	(Karman et al., 2024)
FV2	During the last 6 months in our organization the production costs in the organization decreased.	
FV3	During the last 6 months in our organization the financial performance has increased.	

RESEARCH FINDINGS

The study explores the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on the firm value within the hotel industry in Indonesia. To assess convergent validity, the study analysed item correlations using Cronbach's alpha and composite reliability (CR). The results revealed values exceeding 0.70, indicating strong reliability. Additionally, factor loadings and average variance extracted (AVE) were examined, with outcomes showing values greater than 0.50.

These results demonstrate a high correlation between items and validate the convergent validity of the constructs. [Table 2](#) presents these findings.

Table 2: Convergent Validity

Constructs	Items	Loadings	Alpha	CR	AVE
Audit Committee	AC1	0.858	0.909	0.932	0.733
	AC2	0.870			
	AC3	0.864			
	AC4	0.867			
	AC5	0.822			
Audit Quality	AQ1	0.580	0.868	0.884	0.528
	AQ2	0.664			
	AQ3	0.569			
	AQ4	0.835			
	AQ5	0.856			
	AQ6	0.853			
	AQ7	0.661			
Firm Value	FV1	0.852	0.782	0.873	0.696
	FV2	0.816			
	FV3	0.834			
Internal Auditor	IA1	0.863	0.919	0.936	0.675
	IA2	0.853			
	IA3	0.833			
	IA4	0.826			
	IA5	0.778			
	IA6	0.776			
	IA7	0.818			

Table 3: Fornell Larcker

	AC	AQ	FV	IA
AC	0.856			
AQ	0.629	0.727		
FV	0.411	0.458	0.834	
IA	0.429	0.502	0.544	0.821

The study assesses discriminant validity by examining the correlations between variables. This was done using the Fornell-Larcker criterion and cross-loadings. The results showed that the correlations between constructs were higher than the correlations between constructs and other variables, indicating that each construct is distinct and does not overlap excessively with others. These findings confirm the discriminant validity of the variables. [Tables 3](#) and [4](#) present these results.

Table 4: Cross-Loadings

	AC	AQ	FV	IA
AC1	0.858	0.527	0.332	0.320
AC2	0.870	0.559	0.356	0.393
AC3	0.864	0.521	0.331	0.364
AC4	0.867	0.551	0.397	0.410
AC5	0.822	0.532	0.338	0.342
AQ1	0.639	0.580	0.181	0.264
AQ2	0.670	0.664	0.206	0.244
AQ3	0.616	0.569	0.177	0.256
AQ4	0.387	0.835	0.419	0.469
AQ5	0.399	0.856	0.440	0.460
AQ6	0.358	0.853	0.462	0.457
AQ7	0.673	0.661	0.211	0.245
FV1	0.327	0.397	0.852	0.452
FV2	0.354	0.343	0.816	0.423
FV3	0.350	0.404	0.834	0.483
IA1	0.345	0.414	0.493	0.863
IA2	0.367	0.434	0.466	0.853
IA3	0.344	0.436	0.458	0.833
IA4	0.355	0.443	0.436	0.826
IA5	0.354	0.414	0.401	0.778
IA6	0.336	0.392	0.441	0.776
IA7	0.372	0.355	0.421	0.818

Discriminant validity was further assessed using the Heterotrait-Monotrait (HTMT) ratio. The results revealed that the HTMT values were below 0.85, indicating a low correlation between variables and supporting the validity of discriminant validity. [Table 5](#) presents these results.

Table 5: Heterotrait Monotrait Ratio

	AC	AQ	FV	IA
AC				
AQ	0.805			
EG	0.486	0.486		
IA	0.468	0.513	0.638	

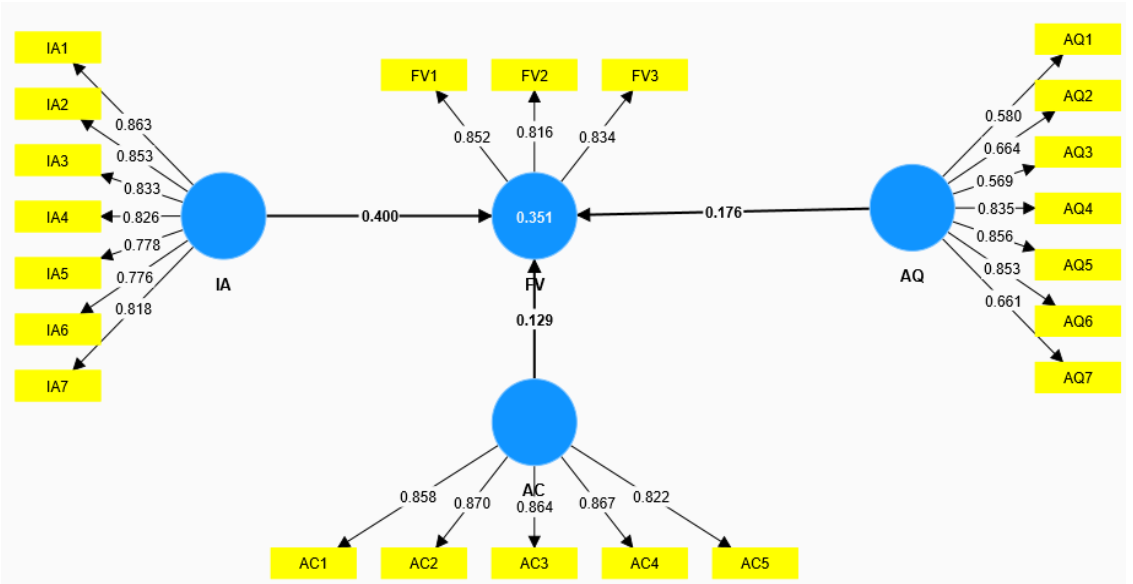


Figure 2: Measurement Assessment Model

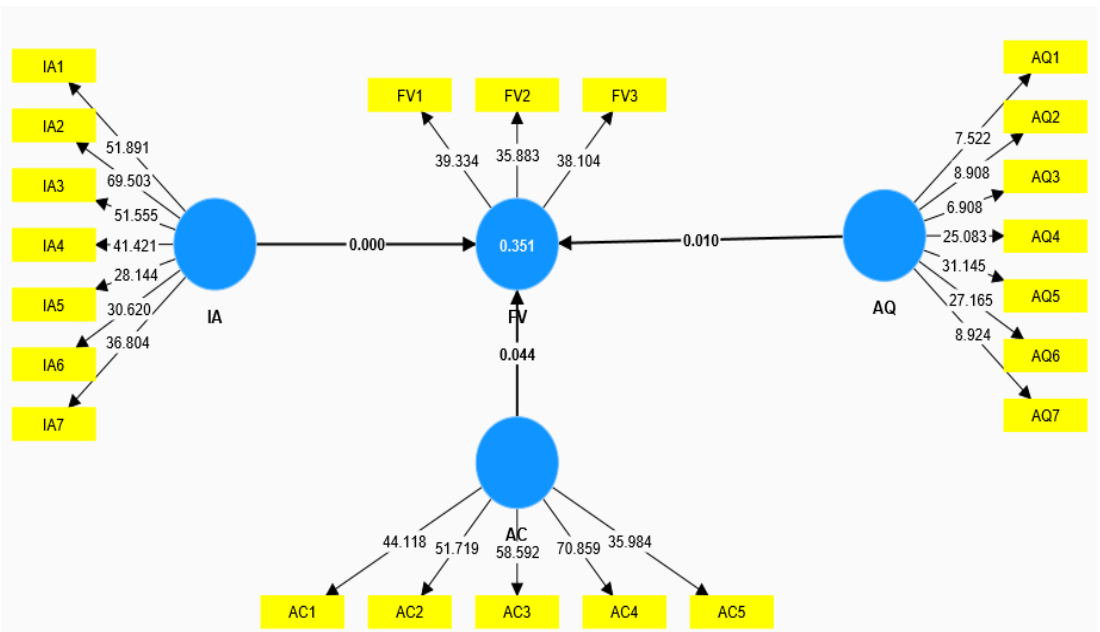


Figure 3: Structural Assessment Model

The study also utilized path analysis to examine the relationships among variables. The results demonstrated that audit committee effectiveness, audit quality, and internal auditor effectiveness each have a positive association with firm value in the hotel industry in Indonesia, leading to the acceptance of hypotheses H1, H2, and H3. Table 6 presents these associations.

Table 6: Path Analysis

Relationships	Beta	Standard Deviation	T Statistics	P Values
AC -> FV	0.129	0.063	2.039	0.044
AQ -> FV	0.176	0.067	2.627	0.010
IA -> FV	0.400	0.061	6.507	0.000

DISCUSSION

Firm value is a crucial factor for organizational success and warrants further research. This study explores the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on the firm value within the hotel industry in Indonesia. It specifically examines the interplay between these elements of corporate governance and their influence on financial performance in the context of the Indonesian hotel sector. The findings underscore the importance of these governance components in enhancing firm value, highlighting their critical role in a complex and dynamic industry.

The study highlights the critical role of an effective audit committee in enhancing firm value. Composed of independent directors with financial expertise, the audit committee is essential for rigorous oversight of financial reporting, internal controls, and audits. Neglecting this function can significantly undermine investor confidence, particularly in the hotel industry, where financial integrity is paramount. [Oncioiu et al. \(2020\)](#) demonstrate that firms with robust audit committees exhibit higher firm values, as evidenced by improved stock performance and valuation multiples. Furthermore, [Sultana et al. \(2019\)](#) find a positive correlation between the frequency of audit committee meetings, the financial expertise of its members, and firm value, underscoring the importance of diligent monitoring and informed decision-making in mitigating risks and enhancing financial operations. This aligns with existing literature, which indicates that effective audit committees significantly reduce the likelihood of accounting fraud and financial statement manipulations, thereby safeguarding investor interests and enhancing overall market capitalization. The study also emphasizes the critical role of internal auditors, who provide vital internal controls by evaluating the efficiency of organizational operations, risk management, and governance structures ([Turetken et al., 2020](#)). The study highlights the critical role of internal auditors in the hotel industry, characterized by numerous cash transactions and complex internal operations. It underscores the importance of internal auditors in identifying fail points and potential risks. The findings confirm that effective internal audit functions contribute to increased firm value by enhancing decision-making and optimizing resource management. Internal auditors, by maintaining their independence, can identify and address operational concerns, thereby improving overall business performance. This aligns with the views of [Kim et al. \(2024\)](#), who argue that the effectiveness of audit plans and review schedules significantly enhances the positive relationship between internal auditors and firm value. These findings are consistent with

other research indicating that robust internal audit practices bolster risk management and operational efficiency, which are essential for sustaining profitability in the hotel sector.

Another key factor influencing firm value is audit quality. Independent audit firms provide relatively accurate financial statements, reflecting the true financial status of companies (Salehi et al., 2020). In Indonesia, where regulatory standards and compliance may not always be optimal, audit quality becomes crucial for ensuring the reliability of financial reports (Abdullatif & Al-Rahahleh, 2020). The study demonstrates a significant positive relationship between audit quality and firm value, highlighting that audits conducted by top-tier firms have a pronounced effect on hotel market value. This is due to the enhanced credibility associated with high-quality audits, which in turn boosts investor confidence. The evidence suggests that superior audit quality reduces information asymmetry between companies and external stakeholders, thereby improving firm value and lowering the cost of capital. These findings are consistent with previous research emphasizing the importance of auditor independence, experience, and professionalism in producing high-quality audits and maintaining investor trust (Duc et al., 2019). The discussion also explores the relationship between governance mechanisms and the Indonesian hotel industry environment. The study highlights that this sector, characterized by significant growth potential, faces dynamic challenges, including evolving regulatory landscapes and operational issues. It underscores the importance of adopting robust corporate governance principles to navigate these challenges effectively. Empirical evidence from the study confirms that hotels with effective audit committees, robust internal audit functions, and high audit quality are better positioned to address these hurdles and enhance their firm value. This is particularly relevant in the context of the Indonesian hotel industry, where external factors such as fluctuating tourist arrivals and economic conditions are beyond the control of industry players. The study suggests that sound governance mechanisms facilitate efficient fund accumulation, operational effectiveness, and reliable financial reporting. These factors are crucial for the sustained growth and profitability of hotels in Indonesia, enabling them to thrive amidst external uncertainties.

IMPLICATIONS

The study explores the impact of audit committee effectiveness, audit quality, and internal auditor effectiveness on the firm value within the Indonesian hotel industry. The findings have broad implications extending beyond academic research, offering actionable insights for policymakers, investors, and professionals engaged in corporate governance. For policymakers, the study advocates for self-regulatory measures aimed at enhancing audit quality and corporate governance. It suggests implementing stringent regulatory requirements for both the public and private sectors to improve transparency and bolster investor confidence, ultimately contributing to industry stability and growth.

For industry practitioners and business professionals, the study highlights the importance of investing in robust governance mechanisms to achieve value enhancement and competitive advantage. By adopting best practices in auditing and corporate governance, companies can significantly improve their financial performance and sustainability. The article also provides guidance for regulators in developing policies that focus on optimizing firm value through effective audit committees, high-quality audits, and efficient internal audit functions.

LIMITATIONS

The study on the impact of audit committee effectiveness, internal audit functions, and audit quality on the firm value of Indonesian hotel industries has several limitations. Firstly, the research is restricted to firms listed on the Indonesian stock exchange, thereby excluding privately held hotel companies operating within the country. Consequently, the study does not capture the full spectrum of the hotel industry. Secondly, the data collected is limited to a specific timeframe, potentially affecting the analysis of long-term trends and patterns. Thirdly, the study's methodological approach relies solely on financial data, which may not comprehensively capture the qualitative aspects and specific nuances of internal audit effectiveness and quality. Finally, the findings may be constrained by the legal and market conditions unique to Indonesia, which could limit their applicability to other countries with different regulatory and market environments.

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