

## The Role of the Internal Audit Function in Moderating the Effect of Audit Committee Gender Diversity on Audit Quality

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### ABSTRACT

This study examines how gender diversity on the audit committee board affects audit quality, with the internal audit function serving as a moderating factor. The study analyzed 321 firm-year observations based on the annual reports of manufacturing firm listed on Indonesia Stock Exchange listed between 2019 and 2023. This study uses PLS-SEM to examine a research hypothesis. Our findings provide new insights to describe that the presence of women makes the audit committee more diverse and able to have a higher impact on audit quality. They have high performance standards to demonstrate the importance of the audit committee's responsibility in the financial reporting and management monitoring process. The internal audit function has strengthened the effect of a gender diversity on audit quality. Theoretically, this study contributes to the development of literature related to agency theory. For potential investors, as a strategy, invest in companies that have quality audits due to the strong encouragement from companies with more gender-diverse audit committees. For the government, strengthen the policy of women leadership on corporate boards to improve good governance.

### ARTICLE INFO

**Article history:**

Submitted: 20 June 2025

Revised: 23 August 2025

Accepted: 26 August 2025

Published: 28 August 2025

**Keyword:**Gender Diversity,  
Audit Committee,  
Internal Audit,  
Audit Quality.**To cite this article (APA Style):**Kurniawansyah, D., and Iswajuni (2025). The Role of the Internal Audit Function in Moderating the Effect of Audit Committee Gender Diversity on Audit Quality. *JASa: Jurnal Akuntansi, Audit dan Sistem Informasi Akuntansi*. Vol 9 (2), p.313-327.<https://doi.org/10.36555/jasa.v9i2.2867>

## INTRODUCTION

The phenomenon of corporate accounting scandals that have rocked developed countries has led to the collapse of large companies and charges against them. In Indonesia, a recently uncovered accounting scandal involving Wanaartha Life and the accounting firm KAP Kosasih, Nurdiyaman, Mulyadi Tjahjo, and Partners (KNMT) failed to find evidence of financial statement manipulation, particularly regarding the inflated production of high-risk insurance products similar to savings plans. This case has led to a loss of public trust, as it is perceived that companies have failed to comply with governance regulations and that the audit quality is insufficient to detect material misstatements and fraud (Kalia et al., 2023, and ElGammal, and Gharzeddine, 2020).

Audit quality is defined as the ability of independent auditors to detect and report deviations in their clients' accounting systems (Alhababsah and Yekini, 2021). Audit quality is essential to ensure the reliability and credibility of a company's financial statements. Audit quality affects how stakeholders assess good corporate governance and the long-term sustainability of a company (Fernández-Méndez and Pathan, 2023). As one of the corporate governance mechanisms, the audit committee plays a significant role in improving company performance and economic profits (Dey, 2008) and ensuring the quality of financial reporting (Klein, 2002). Additionally, the audit committee oversees internal controls and risk management processes (Zhang et al., 2007) and enhances the independence of external auditors and audit quality (Jusoh et al., 2023; Sultana et al.,



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2015).

Most studies on audit committees related to audit quality are based on issues concerning the characteristics of audit committees, such as committee size, meeting frequency, and the financial expertise of committee members (DeFond and Zhang, 2014; Guan et al., 2016; He et al., 2017; Salehi and Shirazi, 2016; Jusoh et al., 2023). Often, gender diversity issues, including the proportion of males and females on the company's board of directors, are overlooked (Hashim et al., 2019; Alkebsee et al., 2021; Sellami and Cherif, 2020; Kurniawansyah and Mahendrawati, 2024). This issue aligns with the 2030 SDGs goal of achieving gender equality and empowering women. The presence of women on audit committee creates diversity in perspectives and thoroughness in decision-making. Women have a disciplined and conservative nature in control and supervisory functions, which can reduce adverse impacts on companies. They often request that auditors improve their audits' quality to minimize auditor failures in detecting errors. These efforts are a form of fulfilling their responsibility for the financial reporting process and management monitoring (Luh, 2023; Zalata et al., 2017; Lai et al., 2017; Miglani and Ahmed, 2019; Aldamen et al., 2018; Mustafa et al., 2018).

According to agency theory, gender diversity on audit committees can reduce information asymmetry and moral hazard behavior by demanding high-quality audits (Reguera-Alvarado et al., 2017; Alkebsee et al., 2021; Abatecola dan Cristofa, 2018; Gull et al., 2021; Gordini, and Racanti, 2017). See et al (2020) prove that increasing audit committee gender diversity affect audit quality, because women more sensitive to business and legal risks, ethical issues, and prioritize stakeholders' interests in improving corporate governance, which includes improving supervisory, control, and monitoring functions. In line with Sellami and Cherif (2020), The more gender diversity there is on the audit committee, the more cautious companies tend to be in their decision-making. Women will recommend public accounting firms or professional auditors who have a strong incentive to protect the company's reputation. An, (2023) demonstrated that gender diversity with women members in board has positively affect audit quality, because women is considered to provide a different perspective compared to men. She is more democratic in presenting their analysis and more conservative in decision-making (An, 2023). In contrast, Alhababsah and Yekini (2021) stated that gender diversity as measured by the proportion of women members, did not affect the audit quality of Jordanian family businesses, because women on audit committee with family relationships will hesitate to supervise effectively and tend not to contradict managers. Gresia and Itan (2022) prove that gender diversity in directors do not affect audit quality. The minimize women representation on boards of directors makes them unable to exert influence or participatory intervention in decision-making regarding the selection of external auditors.

The internal audit function is considered a governance mechanism that mitigates agency problems by providing primary assurance to the audit committee regarding the financial statements produced (Dzikrullah et al., 2020, and Abhilash et al., 2023). The internal audit function assures the misuse of company assets and contributes to the credibility of financial reporting. According to the International Standard on Auditing 610. External auditors may rely on the work of internal auditors related to audit procedures that have implications for the nature, timing, or extent of the audit procedures to be performed.

The audit committee gender diversity has increased their demands on audit quality to strengthen their reputation as vigilant supervisors in the face of agency conflicts between principals and agents. They rely on the internal audit function's work to enhance internal audit activities, monitor the financial reporting process, and improve the efficiency of the internal audit function in the company for risk management (Arena and Azzone, 2009, and Harymawan, and Putri, 2023). In practice, external auditors often use the work performed by internal auditors, considering the objectivity of the internal audit quality, the competence, and the results of the work performed by the internal audit function before relying on the work of internal auditors. External auditors can add insights about the company, and

internal auditors can bring accounting and audit issues identified during internal audits to the attention of external auditors based on their knowledge and expertise (Leung, 2013). External auditors examine financial records and issue opinions on the company's financial statements. Using internal auditors' work results and expertise improves the quality of auditing and reporting by external auditors. Therefore, the internal audit function is believed to moderate the relationship between the audit committee gender diversity and audit quality.

García et al., (2019) and Gras Gil et al., (2012) found that internal and external audits act as complementary mechanisms to encourage the presentation of high-quality financial statements and minimize fraudulent practices. Alzoubi (2019) shows that the internal audit function successfully strengthens the influence of audit committee gender diversity on earnings management. When a company has an effective audit committee and establishes an adequate internal audit function, the company can prevent earnings management practices, thereby improving the quality of financial statement presentation and audit results. In contrast, See et al., (2020) proved that the internal audit function did not succeed in moderating the influence of gender in the audit committee on audit quality in public companies in Malaysia. The audit quality produced by external auditors is not directly affected by the work of the internal audit function because the work of the internal audit function is related to risk management and the company's internal control system, while the work of external auditors is to provide independent assurance on audit opinions based on the financial statements presented by the company. Hasyim et al. (2019) explains that the internal audit function does not successfully moderate the effect of gender diversity on the level of earnings management. This finding is because there is no difference between the results of work carried out by in-house or outsourced internal audit functions, so there is no significant impact on the level of audit quality.

This study aims to empirically prove the function of internal audit in moderating the effects of gender diversity in audit committees on audit quality in manufacturing companies listed on the Indonesia Stock Exchange from 2019 to 2023. The manufacturing sector is one of the backbones of the national economy and the most significant contributor to Indonesia's Gross Domestic Product (GDP), enabling it to maintain national economic growth. 2019-2023, the manufacturing industry faced severe challenges, as evidenced by its fluctuating performance. At the end of 2019, manufacturing performance declined due to the trade war between the United States and China, which affected exports. From 2020 to 2023, the manufacturing sector faced its toughest challenges due to the COVID-19 pandemic and the Russia-Ukraine war, which led to limited supplies of raw materials for the manufacturing industry. Therefore, this study is motivated to conduct an in-depth analysis during the research period from 2019 to 2023 to determine whether company management will remain consistent in presenting financial information following actual conditions and accounting standards during periods of financial instability.

This study found many inconsistencies in the results of previous studies, such as that audit committee gender diversity have a positive effect on audit quality (An, 2023; See et al., 2020; Sellami and Cherif, 2020) and that it is insignificant, as found by Alhababsah and Yekini (2021) and Gresia and Itan (2022) using the role of women on the board of directors. In addition, there is a gap in previous studies, which have rarely used internal audit functions to moderate the effects of gender diversity in audit committees on audit quality. Most of the issues of gender diversity in boards have been studied in developed countries such as Anglo-Saxon countries that adopt a one-tier system, which is different from Indonesia, which uses a two-tier system, and internal audit functions are widely used as direct predictors of audit quality. The inconsistency of research results and the lack of gender diversity issues in audit committees and corporate governance in developing countries such as Indonesia motivated researchers to explore using an agency theory approach further. To capture the complexity of audit quality, this study employs control variables such as audit size (Kuan Pei See et al., 2020), audit complexity (Alhababsah and

Yekini, 2021), and audit risk (Abdollahi et al., 2020).

The results of this study are expected to contribute empirical evidence that strengthens agency theory. Public companies must have an audit committee gender diversity and a good internal audit function to improve corporate governance standards. Women on audit committees perform a stricter supervisory role and behave ethically to reduce information asymmetry between principals and agents. The role of women on audit committees will require external auditors to be more extensive and severe in testing material misstatement risks and fraud risks to protect the reputation and future losses from lawsuits. In addition, the internal audit function can assure the management team and board of directors on the effectiveness of risk management, governance, and control processes. The results of this study can be used to enrich scientific literature, especially in the field of auditing. The results of this study are expected to provide practical contributions to prospective investors in the form of appropriate strategies for assessing the risk situation of companies that affect investment decisions, especially in manufacturing companies in Indonesia. The large number of irregularities in financial statements indicates that auditors provide good audit quality. The contribution of this study practice to the government is expected to become the basis for the formulation of policies or regulations on gender diversity in the leadership of companies in Indonesia to support SDG 5, namely gender equality and women's empowerment. Gender diversity, especially women on the audit committee, is the basis for the formation of quality human development to create good corporate governance and sustainable economic development.

### **The Agency Theory**

The agency theory assumes that everyone will always act in their best interests (See et al., 2020). Differences in interests between principals and agents give rise to the risk of information asymmetry, which affects the quality of financial reports. The economic consequence of minimizing the risk of information asymmetry is agency costs. Agency costs are the costs incurred to monitor agency performance using independent auditors. The audit committee is the board responsible for promoting adequate internal control, improving transparency in financial reporting, and reviewing the scope and appropriateness of external auditor assignments, including but not limited to the reasonableness of audit fees, experience, independence, and objectivity. Therefore, the audit committee may request independent auditors to provide high-quality audits to enhance the credibility of the company's financial statements (Panda, et al., 2017). One characteristic of people who are risk-averse, cautious, and conservative is female gender. Audit committee gender diversity improves the decision-making process. The more diverse the gender representation, the more gender diversity there is, the better the company's reputation will be. They demand higher guarantees from external auditors for better audit quality (Luh, 2023). The characteristic of women being more concerned with ethics causes them to be more reluctant to take risks, so gender diversity in the audit committee has an impact on higher audit quality results (Luh, 2023).

The audit committee and internal audit function are jointly responsible for ensuring that internal controls within the company are functioning properly. The Audit Committee's responsibilities in this regard can be carried out through the use of reports and discussions with management, internal auditors, and external auditors. Gender diversity makes the audit Committee more active in evaluating the implementation and improvement of internal controls by management, which can foster a good control environment (Abdel-Meguid et al., 2023). The higher the quality of the internal audit, the stronger the influence of gender diversity in the audit committee to improve audit quality. Internal audit will collaborate with external auditors appointed by the audit committee to maintain the integrity and quality of the company's financial reporting. External auditors are highly dependent on effective internal controls, and, conversely, internal controls require support from external auditors to help improve their effectiveness.

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### **The Role of the Internal Audit Function in Moderating the Effect of Audit Committee Gender Diversity on Audit Quality**

Deddy Kurniawansyah<sup>\*1</sup>, Iswajuni<sup>1</sup>



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### **The Influence of audit committee gender diversity on Audit Quality**

Psychologically, females are considered to have a different perspective from males, which leads to differences in communication style, management style, leadership style, and decision-making processes (An, 2022). They are considered to be more thorough, cautious, and risk-averse, which affects their leadership style and decision-making, making them more conservative, such as improving the company's control environment (Alhababsah and Yekini, 2021). A good control environment can mitigate fraud and manipulation that can harm the company. Based on agency theory, gender diversity as demonstrated by the proportion of women on the audit committee are cautious, honest, conservative, risk-averse, and democratic, and their ability to ensure participatory decision-making makes them bold in recommending reputable public accounting firms or external auditors to obtain high assurance (Luh, 2023). These capabilities can minimize information asymmetry between management (agents) and shareholders (principals).

See et al. (2020) explain that females are essential in audit committees as supervisors of company activities related to preparing financial statements and audit activities carried out by external auditors. Women who are meticulous and cautious are considered bold in making decisions by demanding highly reputable external auditors or more comprehensive audit efforts so that companies will obtain more assured audit results (Sellami and Cherif, 2022). Gender diversity in audit committees is considered to provide different perspectives and enrich references in decision-making. A higher proportion of women on audit committees is considered to be more independent and democratic in analyzing uncertain situations. Audit committee gender diversity can assist the board of commissioners in its supervisory function related to determining a qualified public accounting firm or external auditor (An, 2022). Based on the previous discussion, the research hypothesis is stated as follows:

H1: The audit committee gender diversity affects audit quality.

### **The effect of internal audit moderation on the relationship between the audit committee gender diversity and audit quality**

Internal audit is an interactive component of corporate governance and is classified as a corporate competency that can affect audit quality (DeFond and Zhang, 2014). Research on the internal audit function related to audit quality is limited (See et al., 2021). In line with agency theory, as the complexity of a company increases, the internal audit function is expected to provide added value to improve good corporate governance (Alzoubi, 2019). The internal audit function assures the effectiveness of internal controls and internal risk management systems concerning the audit committee and the board of directors (Dzikrullah et al., 2020, and Pious et al., 2022). García et al. (2019) and Gras Gil et al. (2012) explain that internal and external audits act as complementary mechanisms to encourage the presentation of quality financial statements and minimize fraudulent practices. Alzoubi (2019) proves that the internal audit function successfully strengthens the influence of audit committee gender diversity on earnings management. When a company has an effective audit committee and establishes an adequate internal audit function, earnings management practices can be prevented, thereby improving the quality of financial reporting and audit results. Based on the above description, the research hypothesis is stated as follows:

H2: The internal audit function strengthens the relationship between the audit committee gender diversity and audit quality.

## **METHODS**

### **Samples and Data Collection Methods**

This research is explanatory research that explains the causality between variables and a particular phenomenon and proves the relationship or influence between variables

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### **The Role of the Internal Audit Function in Moderating the Effect of Audit Committee Gender Diversity on Audit Quality**

Deddy Kurniawansyah<sup>\*1</sup>, Iswajuni<sup>1</sup>

through hypothesis testing (Hair et al., 2021). This study uses secondary data sources. The secondary data for this study are annual reports of manufacturing companies listed on the Indonesia Stock Exchange (IDX) from 2019 to 2023, obtained from the IDX website ([www.idx.co.id](http://www.idx.co.id)) and the websites of each company. The data collection method used in this study is content analysis, which systematically and objectively analyzes the meaning of a phenomenon to formulate the best conclusions to represent, describe, and measure a particular phenomenon (Hair et al., 2021).

The population of this study consists of manufacturing companies listed on the Indonesia Stock Exchange (BEI) from 2019 to 2023. Table 1 provides the population criteria.

**Table 1. Research Population Criteria**

| Criteria                                                                                | Total      |           |           |           |           |
|-----------------------------------------------------------------------------------------|------------|-----------|-----------|-----------|-----------|
|                                                                                         | 2019       | 2020      | 2021      | 2022      | 2023      |
| Manufacturing companies listed on the Indonesia Stock Exchange (IDX) for 2019-2023.     | 167        | 193       | 212       | 224       | 236       |
| Companies that do not publish audited financial statements and complete annual reports. | (-)        | (-)       | (-)       | (-)       | (17)      |
| Companies that did not provide the data and information required for this study.        | (124)      | (147)     | (166)     | (176)     | (171)     |
| <b>Total</b>                                                                            | <b>43</b>  | <b>46</b> | <b>46</b> | <b>48</b> | <b>48</b> |
| <b>Total Observations</b>                                                               | <b>231</b> |           |           |           |           |

Source: processed secondary data (2023)

Based on the population criteria in Table 1, there were 231 annual reports from manufacturing companies. Furthermore, this study used the census method for sampling. All observations became the sample for this study.

### Definition and Measurement of Variables

The dependent variable in this study is Audit Quality. Audit Quality is the ability of auditors to assure the possibility of material errors, manipulation, or bias in the financial statements presented that affect the accuracy of information so that it reflects the economic condition of the company (Adeniyi and Aderobaki, 2023; Alhababsah and Yekini, 2021). This variable is measured using audit fees adopted from An (2023) and Owolabi and Ayobami (2020). The measurement scale for this research variable is a ratio scale.

The independent variable in this study is the audit committee gender diversity. audit committee gender diversity is the presence of women members of the audit committee in carrying out their duties and functions as a form of difference in managerial style, strategic decision-making, and communication processes in strengthening a better corporate governance system (Alhababsah and Yekini, 2021; Kuan Pei See et al., 2020). This variable is measured by the proportion of women on the audit committee board, adopted from Alhababsah and Yekini (2021). The measurement scale for this research variable is a ratio scale.

The moderating variable in this study is the Internal Audit Function. The Internal Audit Function is an independent and objective assurance and consulting activity designed to add value to the company (Ghaleb et al., 2020, and See et al., 2021). This research variable is measured by 1) the size of the internal audit function, as seen through the number of internal audit members in the company, 2) the number of internal audit certifications using a dummy scale, scored (1) if there is at least one member with an internal audit certification and (0) if there are no members with certifications, 3) the existence of internal audit using

### The Role of the Internal Audit Function in Moderating the Effect of Audit Committee Gender Diversity on Audit Quality

Deddy Kurniawansyah<sup>\*1</sup>, Iswajuni<sup>1</sup>

a dummy scale, scored (1) if there is an internal audit department and (0) if the company does not have an internal audit department, adopted from See et al. (2021). The measurement scale for the research variables is a ratio scale.

The control variable in this study is audit size. Audit size refers to the extent of the auditor's efforts based on the client's revenue in one accounting period (Kuan Pei See et al., 2020; Abdollahi et al., 2020). This variable is measured using the natural logarithm of the annual revenue of the public accounting firm, adopted by Kuan Pei See et al. (2020). The measurement scale for this research variable is a ratio scale. Audit complexity is the extent to which auditors analyze the volume of a client company's business (Alhababsah and Yekini, 2021). This variable is measured using the natural logarithm of the number of subsidiaries adopted from Alhababsah and Yekini (2021). The measurement scale for this research variable is a ratio scale. Audit risk is the extent to which auditors determine the level of audit risk based on an audit risk model (Abdollahi et al., 2020). This variable is measured using the natural logarithm of the sum of accounts receivable and inventory held by the company during the accounting period, adopted from Abdollahi et al., (2020). The measurement scale for this research variable is a ratio scale.

### **Data Analysis Techniques and Model Specifications**

The data analysis technique used in this study is Partial Least Square Structural Equation Modeling (PLS-SEM), a multivariate technique combining elements of factor analysis, regression analysis, and path analysis. This analysis technique allows testing the relationships between variables in a construct, whether between indicators and their construct or between constructs (Hair et al., 2021). SEM is used because it has several advantages, one of which is the ability to measure using multiple variables with different indicator measurement scales in a single model (Hair et al., 2021). The steps in PLS-SEM testing are the measurement model test (outer model) and the structural model test (inner model). The measurement model test (outer model) evaluates the relationship between indicators and their latent variables. The evaluation of the outer model with reflective indicators is done by looking at indicator loadings, internal consistency reliability, convergent reliability, and discriminant validity. The structural model test (inner model) evaluates the model that connects latent variables. The evaluation of the inner model can be seen from path analysis, adjusted R<sup>2</sup>, and predictive relevance. The regression equation of this study's model is:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_1 \times X_2 + \beta_4 X_3 + \beta_5 X_4 + \beta_6 X_5 + \varepsilon$$

Information:

|                     |                                         |
|---------------------|-----------------------------------------|
| $Y$                 | : Audit Quality                         |
| $\alpha$            | : Intercept                             |
| $\beta_1 - \beta_6$ | : Independent Variable Path Coefficient |
| $X_1$               | : Audit Committee Gender Diversity      |
| $X_2$               | : Internal Audit Function               |
| $X_3$               | : Audit Size                            |
| $X_4$               | : Audit Complexity                      |
| $X_5$               | : Audit Risk                            |
| $\varepsilon$       | : Error                                 |

## **RESULTS AND DISCUSSION**

### Descriptive Statistics

Descriptive statistical testing aims to describe the variables being studied. The measures used in this test are the minimum, maximum, average, and standard deviation values. The results of this test can be seen in Table 2.

**Table 2. Descriptive Statistics Results**

|                                  | N   | Min   | Max   | Mean  | Std. Deviation |
|----------------------------------|-----|-------|-------|-------|----------------|
| Audit Quality                    | 231 | 18,11 | 22,90 | 20,61 | 0,93           |
| Gender Diversity                 | 231 | 0,00  | 1,00  | 0,21  | 0,24           |
| Audit Committee Gender Diversity | 231 | 0,67  | 11,33 | 2,78  | 2,42           |
| Audit Size                       | 231 | 20,40 | 32,09 | 28,63 | 1,75           |
| Audit Complexity                 | 231 | 0,69  | 2,94  | 1,60  | 0,65           |
| Audit Risk                       | 231 | 20,99 | 30,45 | 27,32 | 1,73           |

Source: processed secondary data (2023)

Based on Table 2 the average value of the audit quality variable is 22.90. This finding that the financial statements of manufacturing companies in Indonesia have been audited with high quality by independent auditors. Audit committee gender diversity measured by proportion of women on the audit committee board is 0.21 or 21%. This finding that manufacturing companies in Indonesia support and care about gender diversity on the company board. Internal audit function value of 2.78, this finding that the internal audit function of manufacturing companies in Indonesia is good because they have professional internal audit certification, an adequate number of internal audit members, and an internal audit department. Audit size value of 28.62, this finding that the high level of income of manufacturing companies requires independent auditors to conduct more extensive audits. Audit complexity value of 1.60, this finding that independent auditors face high audit complexity when conducting audits on manufacturing companies in Indonesia. Audit risk value of 27.32, this finding that the high audit risk of independent auditors who audit manufacturing companies in Indonesia. Accounts receivable and inventory are hazardous accounts prone to manipulation by management, necessitating auditors to conduct detailed examinations of these accounts.

### Outer Model Test (Indicator Test)

The outer model test tests indicators against latent variables or, in other words, measures how far the indicators can explain the latent variables. For reflective indicators such as those used in this study, the test was conducted by looking at the results of indicator loadings, internal consistency reliability, convergent validity, and discriminant validity.

**Table 3. Indicator loadings**

|                                               | Loading factor |
|-----------------------------------------------|----------------|
| Proportion of Woman in Audit Committee ← ACGD | 1,00           |
| IAF Ratio ← Internal Audit Function           | 1,00           |
| AQ_FEE ← Audit Quality                        | 1,00           |
| Log Annual Income ← Audit Quality             | 1,00           |
| Log Number of Subsidiaries ← Audit Complexity | 1,00           |

Source: processed secondary data (2023)



**Table 4. Internal Consistency Reliability**

|                                         | AVE  | CR   |
|-----------------------------------------|------|------|
| Audit Committee Gender Diversity (ACGD) | 1,00 | 1,00 |
| Internal Audit Function (IAF)           | 1,00 | 1,00 |
| Audit Quality (AQ)                      | 1,00 | 1,00 |
| Audit Size (AS)                         | 1,00 | 1,00 |
| Audit Complexity (ACo)                  | 1,00 | 1,00 |
| Audit Risk (AR)                         | 1,00 | 1,00 |
| Moderasi FAC*IAF                        | 1,00 | 1,00 |

Source: processed secondary data (2023)

**Table 5. HTMT**

|          | ACGD | ACGD * IAF | ACo  | AQ   | AR   | AS   | IAF  |
|----------|------|------------|------|------|------|------|------|
| ACGD     | 0,00 | 0,00       | 0,00 | 0,00 | 0,00 | 0,00 | 0,00 |
| ACGD*IAF | 0,02 | 0,00       | 0,00 | 0,00 | 0,00 | 0,00 | 0,00 |
| ACo      | 0,18 | 0,06       | 0,00 | 0,00 | 0,00 | 0,00 | 0,00 |
| AQ       | 0,33 | 0,08       | 0,59 | 0,00 | 0,00 | 0,00 | 0,00 |
| AR       | 0,15 | 0,04       | 0,33 | 0,56 | 0,00 | 0,00 | 0,00 |
| AS       | 0,19 | 0,08       | 0,43 | 0,62 | 0,86 | 0,00 | 0,00 |
| IAF      | 0,15 | 0,22       | 0,41 | 0,46 | 0,32 | 0,38 | 0,00 |

Source: processed secondary data (2023)

All indicators were valid based on the indicator loadings shown in Table 3 because they had loading factor values above 0.708 (Hair et al., 2022). The results of Table 4 on internal consistency reliability show that the composite reliability value is above 0.70 (Hair et al., 2022), indicating that the reliability of the variable indicators is very high and meets the internal consistency reliability requirements. The AVE values for each variable also show values above 0.50 (Hair et al., 2022), so all reflective constructs are considered valid and meet the convergent validity requirements. The results in Table 5 show that the HTMT values for all latent variables are less than 0.90 (Hair et al., 2022). These results indicate that all constructs' average item correlation values relative to the average correlation are good. Therefore, the testing can proceed to the structural model stage.

### Path analysis

Path analysis shows the influence and significance of latent variables in the study. The results of path analysis are seen from the magnitude of the structural path coefficients (path coefficients) and t-values for the significance of the prediction model. The results of the path coefficients in this study can be seen in Table 6.

**Table 6. Path Coefficients Results**

|                              | Coefficient<br>Beta | T-Statistic | Significant<br>(p-value < 0,05) | Affected<br>(T-statistic > 1,96) | Hypothesis  |
|------------------------------|---------------------|-------------|---------------------------------|----------------------------------|-------------|
| FAC → AQ                     | 0,148               | 2,561       | 0,006                           | Affected                         | H1 Accepted |
| IAF → AQ                     | 0,152               | 2,706       | 0,004                           | Affected                         | -           |
| AS → AQ                      | 0,293               | 3,360       | 0,001                           | Affected                         | -           |
| ACo → AQ                     | 0,322               | 5,993       | 0,000                           | Affected                         | -           |
| AR → AQ                      | 0,116               | 0,924       | 0,178                           | Not Affected                     | -           |
| FAC * FIA → AQ               | 0,249               | 3,103       | 0,001                           | Affected                         | H2 Accepted |
| Adjusted R <sup>2</sup> → AQ | 0,593               |             |                                 |                                  |             |
| Q <sup>2</sup> → AQ          | 0,551               |             |                                 |                                  |             |

Source: processed secondary data (2023)

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## Discussion

The results of this study indicate that the audit committee gender diversity affects audit quality. The higher proportion of woman attendance in the audit committee, the more positive the impact on improving audit quality. This study's results align with agency theory, which states that women have socio-demographic characteristics that men do not. Women are considered to be more cautious, so they avoid risks and tend to prioritize ethical behavior. In addition, women are also considered conservative, so they tend to be more obedient to rules than men. This condition makes audit committee situation more diversity and strict in supervision and minimize agency conflicts between management and shareholders (Reguera-Alvarado et al., 2017; Alkebsee et al., 2021; Gull et al., 2021). Women can analyze quickly and respond to phenomena in certain conditions. Their cautious and conservative nature encourages women to be less confident, so they prefer to obtain higher professional guarantees to avoid risks, maintain their reputation, and maintain trust.

This study support Shellami and Cherif (2020) and An (2023), who state that the higher the proportion of women, the more diverse the audit committee. The high proportion of women on the audit committee tends to prioritizes ethical behavior and openness, will improve the quality of communication, thereby reducing the risk of information asymmetry between principals and managers. They are psychologically very cautious and sensitive to issues that are detrimental to the company, will encourage the role and function of the audit committee to be more effective. Concerning the audit committee as an extension of the supervisory function of the board of directors and commissioners, the presence of women is undoubtedly considered to improve supervision and control over company operations.

This study does not support the research of Gresia and Itan (2022) and Alhababsah and Yekini (2021), which showed that audit committee gender diversity did not affect audit quality. The results of this study prove that the proportion of women on audit committees in Indonesian manufacturing companies is already perfect. This proportion is above the 15% requirement of the Ministry of State-Owned Enterprises. Audit committee gender diversity demands good financial reporting quality to produce guaranteed audit quality. Therefore, audit committee gender diversity more courageous in demanding greater audit efforts to produce more assured audit quality, ultimately affecting the level of audit fees the company must pay.

This study indicate that the internal audit function strengthens the influence of audit committee gender diversity on audit quality. The better the internal audit function, the stronger the incentive for audit committee gender diversity to demand higher audit quality. Internal auditors must submit audit reports periodically to the leadership (president director) and the supervisory board through the audit committee regarding the comparison of plans and realizations, including the objectives, authority, responsibilities, and performance of the internal audit function. Audit reports serve as information for the audit committee to identify deviations or findings deemed significant by the audit committee and discuss them with the head of the internal audit division to take corrective actions. Internal auditors support the audit committee in assessing the quality of financial reporting and internal control systems. Strong support from the internal audit function to maintain transparency and trust in financial reports and ensure reliable governance within a company makes it easier for the audit committee gender diversity to consider the ethical and skeptical nature of the decision-making process. This nature makes the presence of women on the audit committee expected to be able to improve the detection of financial statement fraud by asking external auditors to improve the quality of their audits.

This study support Alzoubi (2019), García et al. (2019), and Gras Gil et al. (2012), who prove that the internal audit function is a moderating variable that strengthens the effect of audit committee gender diversity on earnings management. Practical internal audit functions can yield positive outcomes by ensuring the operation of adequate internal controls to safeguard assets, prevent the misuse of company resources, and ensure that

management performance aligns with company objectives. Companies with a good internal audit function demonstrate lower levels of earnings management and higher-quality financial information (Prawitt et al., 2009), promoting growth and prosperity within the company (Arel et al., 2012). These findings confirm the need for an internal audit function within corporate governance mechanisms with processes more focused on daily operational activities. The ability of the internal audit function to assess the effectiveness of a company's internal controls is key to supporting the audit committee's effectiveness as a supervisory function. The better the internal audit function, the greater the opportunity to reveal significant internal control weaknesses and financial fraud committed within the company. The presence of women on the audit committee brings a more thorough, neat, specific, and communicative perspective, experience, and work style in completing their tasks, thereby helping to improve discussions between the audit committee and internal audit and subsequently improving decision-making. A good internal audit function supports the audit committee gender diversity in encouraging external auditors to improve audit quality. Higher audit quality requirements naturally increase the risk and responsibility of an external auditor, which will ultimately improve the quality of the audit.

This study supports the agency theory of minimizing the risk of information asymmetry and moral hazards committed by management. The formal obligation for internal auditors to communicate and coordinate with the audit committee makes communication more open and intensive, and the supervisory function is much tighter on management. Supported by the nature of women who are more communicative than men, this creates a more harmonious relationship, making it easier to raise issues such as significant irregularities during the audit process. The support of the internal audit function will further strengthen the audit committee gender diversity by providing recommendations for improvement and communicating them to external auditors. The presence of women on the audit committee will be more stringent in supervising the performance of external auditors so that they perform their duties professionally and see the quality of services performed to realize good corporate governance.

This study does not support See et al. (2020), which proved that the internal audit function does not moderate the influence of audit committee gender diversity on audit quality in Malaysian public companies. The internal audit function is related to assessing the company's risk management and internal control systems, while external auditors are more concerned with providing independent assurance on audit opinions based on the financial statements presented by the company. External auditors conduct independent examinations of financial statements, records, and processes. They also verify that the figures in the financial statements have been presented fairly by generally accepted accounting standards. Therefore, although most external auditors utilize internal audit work, external auditors still adopt a systematic and comprehensive approach to detect potential material misstatements and fraud in financial statements. In addition, this study supports the research of Hasyim et al. (2019), which proves that the internal audit function does not succeed in moderating the influence of board gender diversity on earnings management, possibly because the results of the work carried out by the in-house or outsourced internal audit function are no different so that they do not have a significant impact on the level of audit quality.

## **CONCLUSION**

The results show that the audit committee gender diversity affect audit quality. The more women there are on the audit committee, the more diverse the decision-making process, and the greater the incentive to maintain the quality of financial reporting by demanding high-quality audits from external auditors. The results also show that the internal audit function strengthens the influence of the audit committee gender diversity on audit quality. The better the internal audit function, the stronger the incentive for the audit

committee gender diversity to request external auditors to improve their audit quality. The strong, strict, and agile character of woman in the audit committee minimizes the risk of information asymmetry and moral hazard behavior. The existence of collaboration and formal communication between the internal audit function and the audit committee makes it easier for women in the audit committee to perform their duties. They avoid risky decisions that could harm the company and the board of commissioners' reputation. Therefore, they will carry out stricter oversight of financial reporting, enhance the effectiveness of internal controls, and improve the performance of the internal audit function and the company's risk management system.

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**The Role of the Internal Audit Function in Moderating the Effect of Audit Committee Gender Diversity on Audit Quality**

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