ANALYSIS OF THE EFFECT OF CORPORATE GOVERNANCE, LEVERAGE, AND AUDIT QUALITY ON PROFIT MANAGEMENT WITH COMPANY SIZE AS A MODERATING VARIABLE ON THE GOODS CONSUMER COMPANY REGISTERED IN INDONESIA STOCK EXCHANGE (IDX)

Rizka Nurjannah¹, Murni Daulay²
Universitas Sumatera Utara
91131428rizka@gmail.com

Abstract
The objective of this research was to analyse the influence of Corporate Governance consisted of institutional ownership, size of board of commissioners, board of independent commissioners’ composition; leverage, and audit quality on earnings management with firm size as moderating variable in consumer goods companies listed in the Indonesia Stock Exchange. The research used associative causal method. The population was 14 companies, and all of them were used as the samples, taken by using census technique so that there were 98 observations all together. The data were gathered by conducting documentary study and analysed by using panel data regression analysis. The result of the research showed that, simultaneously, Corporate Governance consisted of institutional ownership, size of board of commissioners, board of independent commissioners’ composition; leverage, and audit quality had the significant influence on earnings management. Partially, the size of board of commissioners and leverage had the positive and significant influence on earnings management, besides institutional ownership, board of independent commissioners’ composition, audit quality had influence not significant on earnings management. The result of residual test on moderating variable showed that firm size could moderate the correlation of Corporate Governance consisted of institutional ownership, size of board of commissioners, board of independent commissioners’ composition; leverage, and audit quality with earnings management in consumer goods companies listed in the Indonesia Stock Exchange.

Keyword: Corporate Governance, Institutional Ownership, Size of Board of Commissioners, Board of Independent Commissioners’ Composition, Leverage, Audit Quality.

I. Introduction
Profit is an indicator to measure the performance of a company, where the greater the profit generated by the company, the better the performance of management. Earnings information can be found in the company’s financial statements. Financial statements serve as a means of communicating financial information to interested parties in making decisions. Management is fully aware that this earnings information becomes the focal point of attention of decision makers so that it motivates the emergence of deviant behavior from management, one of which is earnings management (Prasetya and Gayatri, 2016).

Earnings management in practice is still controversial because some researchers say that earnings management is a natural and ethical thing to do as long as in practice it does not conflict with applicable accounting standards (Fischer and Rosenzweig, 1995). On the other hand, earnings management is considered as a management action
that carries a negative influence and tends to mislead users of information in financial reporting, where there are interventions by managers with the aim of maximizing the manager's personal profit (Schipper, 1989). Earnings management arises as a result of agency conflict, where there are differences in interests between the owner of the company (principal) and company management (agent).

The recent case of earnings management is a scandal by a Toshiba company. According to an independent committee, the company inflated operating profits by ¥ 151.8 billion ($ 1.2 billion) over seven years. As a result of the accounting scandal that rocked the company, Toshiba's shares have dropped by around 20% since early April when these accounting issues were revealed. The market value of the company lost around 1.673 trillion yen ($ 13.4 billion) and analysts expect Toshiba's shares to continue to decline. Toshiba, which is one of the most recognized electronic brands in the world and has a good reputation, is now falling apart due to the accounting scandal that carried out the company.

Consumer goods companies are among the publicly listed companies that register their shares on the Indonesia Stock Exchange. This sector is one of the favorite sectors of investors' choice, as evidenced in 2017 the sector's market capitalization reached IDR 1,575.75 trillion or 22.62% of the total market capitalization in the Indonesia Stock Exchange, making it the sector with the second largest market capitalization in Indonesia after the financial sector. This sector is relatively stable from economic fluctuations, because the products produced by companies in this sector are always needed in any economic conditions, so the demand for the products of this sector is relatively constant (Sukamulja, 2017). From the explanation above, the researcher is interested in conducting a research entitled "Analysis of the Effect of Corporate Governance, Leverage, and Audit Quality on Profit Management with Company Size as Moderating Variables in Consumer Goods Companies Listed on the Indonesia Stock Exchange".

II. Literature Review

Agency Theory

Agency theory describes the meeting point between the owner of the company (principal) and management (agent) within a company. Jensen and Meckling (1976: 308) state "agency relationship as contract under which one or more persons (the principal (s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. While Scott (2009) defines agency theory "Agency theory is a branch of game theory that studies the design of contracts to motivate rational agents on behalf of the agents of interest would otherwise conflict with those of the principal".

The Principal employs agents to carry out duties in the interests of the principal, including delegating authorization to decision making from the principal to the agent. The principal enters into a contract to maximize his well-being with increasing profitability while the agent is motivated to maximize fulfillment of his economic and psychological needs so that opportunistic behaviour from the agent, namely behaviour to maximize his own welfare which is contrary to the interests of the principal, will emerge. Opportunistic behaviour is based on more information knowledge about the company than the principal as an impact of the transfer of company management to the agent. This gives the agent the flexibility to choose and apply accounting methods that can show good performance for the purpose of getting bonuses from the principal.
Mastery of information by agents is often misused to take actions in accordance with the wishes and interests of maximizing its utility by presenting information that is not true to the principal, especially if the information is related to measuring the performance of the agent. The imbalance in mastering information that is known between principals and agents is called information asymmetry.

**Signalling Theory**
Signalling theory emphasizes the importance of information issued by companies on investment decisions of parties outside the company. Information is an important element for investors and business people because information essentially presents information, notes or descriptions for both past, present and future conditions for the survival of a company and how the market effects. Complete, relevant, accurate and timely information is needed by investors in the capital market as an analytical tool for making investment decisions.

Information published as an announcement will signal investors in making investment decisions (Jogiyanto, 2000: 392). If the announcement contains a positive value, it is expected that the market will react when the announcement is received by the market. When information is announced and all market participants have received the information, market participants first interpret and analyze the information as a good news or bad news.

**Earnings Management**
Earnings management is an act of managers to choose accounting policies or actions that affect earnings in order to achieve certain goals in reporting earnings (Scott, 2009: 403). Scott (2009) divides ways of understanding earnings management into two. First, seeing it as an opportunistic agent of managers to maximize their utility in the face of compensation contracts, debt contracts and political costs (Opportunistic Earnings Management). Second, by looking at earnings management from perspective efficient contracting (Efficient Earnings Management), where earnings management gives managers a flexibility to protect themselves and the company in anticipating unexpected events for the benefit of the parties involved in the contract. There are three ways that can be used to do earnings management, namely: utilizing opportunities to make accounting estimates, change accounting methods, and shift the period of costs or income.

**Corporate Governance**
Corporate governance is defined as a set of rules that determine the relationship between shareholders, managers, creditors, governments, employees, and other internal and external stakeholders in accordance with their rights and responsibilities. The corporate governance mechanism consists of several variable indicators. In this study the indicators used by researchers are institutional ownership, board size, and the composition of independent commissioners.

**a. Institutional Ownership**
Institutional ownership is the ownership of company shares by financial institutions such as insurance companies, banks, pension funds, and investment banking (Siregar & Utama, 2005). Institutional ownership is believed to have the ability to monitor management actions better than individual investors. Through the mechanism of institutional ownership, the effectiveness of management of
company resources by management can be seen from information generated through market reactions to earnings announcements. Institutional ownership has the ability to control management through an effective monitoring process that reduces management actions to manage earnings. The percentage of certain shares owned by the institution can affect the process of preparing financial statements that do not rule out the possibility of accrualisation according to the interests of the management (Ujiyantho and Pramuka, 2007).

b. **Board of Commissioner**
The Board of Commissioners is defined as a corporate organization that is collectively responsible and responsible for supervising and providing advice to directors and ensuring that the company implements good corporate governance. The board size of commissioners is the number of all members of the board of commissioners who come from internal and external companies who supervise the directors in running the company. The increasing number of members of the board of commissioners, it will be difficult in carrying out their roles, including difficulties in communicating and coordinating the work of each member of the board itself, difficulties in monitoring and controlling management actions and difficulties in making decisions that are useful for the company.

c. **Composition of the Independent Board of Commissioners**
Independent Commissioners have responsibility for the quality of information from financial statements. According to the National Committee on Good Corporate Governance (2004), independent commissioners are commissioners who are not affiliated with management, other members of the board of commissioners and controlling shareholders, and are free from business relationships and other relationships that can affect their ability to act independently or act solely eyes for the sake of the company.

**Leverage**
The practice of earnings management is associated with a new theory in accounting, namely positive accounting theory or positive accounting theory. Positive accounting theory is an accounting theory that seeks to reveal that certain economic factors or characteristics of a particular business unit can be associated with the behaviour of managers or financial report makers. Leverage is an agreement between a company as a debtor and a creditor. In this debt agreement, there is a company's interest to be positively valued by creditors in terms of their ability to pay their debts. The greater the leverage ratio, the higher the value of the company's debt. Thus, a company that has a high leverage ratio, means the proportion of its debt is higher than the proportion of its assets will tend to manipulate in the form of earnings management. This aims to avoid violations of debt agreements (Astuti, 2004). In addition, the existence of a debt contract agreement triggers management to increase its discretionary accrual with the aim of showing positive performance to creditors, so that they get an injection of funds or to get a debt repayment scheduling.

**Audit Quality**
Companies need to conduct audits by using outside parties to provide endorsement of financial statements in order to reduce the inconsistency in information found in managers and shareholders (Meutia, 2004). Public accountants as external auditors who are relatively more independent than management than internal auditors are expected to
minimize profit engineering cases and increase the credibility of accounting information in financial statements.

Larger public accounting offices are assumed to produce better audit quality as well. The difference in the quality of services offered by public accounting firms shows the identity of the public accounting firm. Auditor independence and quality can have an impact on the detection of earnings management. There are allegations that reputable auditors can detect the possibility of earning management earlier so that it can reduce the level of earnings management carried out by company management.

**Firm Size**
Firm size can be known from the total assets of the company, where the greater the number of company assets, the greater the size of the company (Jin and Machfoedz, 1998: 180). The results of research by Jin and Machfoedz (1998) show that firm size is a factor that encourages the practice of earnings management. The larger the size of the company, the more information available to investors in making more decisions and minimizing the possibility of information asymmetry that can lead to the practice of earnings management in the company.

**Conceptual Framework and Hypothesis**
This research is quantitative research. Based on the previous explanation, eat the conceptual framework in the research as follows:

![Conceptual Framework](image)

**Figure 1 Conceptual Framework**

Based on the introduction described, the research hypothesis can be developed as follows:


b. The size of the Board of Commissioners has a positive effect on Profit Management in consumer goods companies listed on the Indonesia Stock Exchange.
c. The composition of the Independent Board of Commissioners negatively affects Profit Management in consumer goods companies listed on the Indonesia Stock Exchange.

d. Leverage has a positive effect on Profit Management in consumer goods companies listed on the Indonesia Stock Exchange.

e. Audit quality negatively affects Profit Management in consumer goods companies listed on the Indonesia Stock Exchange.

f. Company Size can moderate the effect of Corporate Governance, Leverage, and Audit Quality on Profit Management in consumer goods companies listed on the Indonesia Stock Exchange.

III. Method
The population in this study were all consumer goods companies listed on the Indonesia Stock Exchange which respectively published their financial statements in 2011-2017. The total population in the study was 14 companies. The sampling method is a census, which is the entire population as a sample. Thus, the number of samples in this study were 14 companies with an observation period of 7 years (2011-2017) so that the amount of research data was 14 x 7 years = 98 company data.

The data used in this research is secondary data. Testing is done using the E-views application. The independent variables in this study are institutional ownership (IO), board size of commissioner (BSC), composition of independent board of commissioners (CIBC), leverage (LEV), and audit quality (AQ). The dependent variable is earnings management (EM). The moderating variable is the firm size (FS).

Research Model
To analyse the hypothesis, the following data panel regression estimates are used:

\[ \text{EM} = a + b_1\text{IO} + b_2\text{BSC} + b_3\text{CIBC} + b_4\text{LEV} + b_5\text{AQ} + e \]

Information:
- \( \text{EM} \): Earnings Management
- \( a \): Constants
- \( \text{IO} \): Institutional Ownership
- \( \text{BSC} \): Size of the Board of Commissioners
- \( \text{CIBC} \): Composition of the Independent Board of Commissioners
- \( \text{LEV} \): Leverage
- \( \text{AQ} \): Audit Quality
- \( b_1, b_2, b_3, b_4, b_5 \): regression coefficients
- \( e \): error

IV. Result and Discussion
Result
Sample data in the study were analysed using the E-views application. This research begins by looking at whether the data is normally distributed or not by performing a data normality test. If the probability value is greater than \( \alpha = 0.05 \) and the Jarque - Bera (JB) value <5.9915 then the residual is normally distributed. The results of the normality test can be seen from the picture below:
Based on the picture above, it can be concluded that the data is normally distributed. Testing the hypothesis in this study using the estimation results of the Random Effect Model (REM) regression model. In testing the hypothesis, the coefficient of determination analysis will be carried out, testing for simultaneous influence (F test), and testing for partial influence (t test). The results of the test, can be seen in the following table:

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>IO?</td>
<td>0.028345</td>
<td>0.017910</td>
<td>1.582624</td>
<td>0.1169</td>
</tr>
<tr>
<td>BSC?</td>
<td>0.293869</td>
<td>0.136183</td>
<td>2.157891</td>
<td>0.0335</td>
</tr>
<tr>
<td>CIBC?</td>
<td>-1.664237</td>
<td>1.583605</td>
<td>-1.050917</td>
<td>0.2960</td>
</tr>
<tr>
<td>LEV?</td>
<td>2.215073</td>
<td>0.942389</td>
<td>2.350487</td>
<td>0.0209</td>
</tr>
<tr>
<td>AQ?</td>
<td>-1.006888</td>
<td>0.823339</td>
<td>-1.222933</td>
<td>0.2245</td>
</tr>
<tr>
<td>C</td>
<td>-5.806740</td>
<td>1.514603</td>
<td>-3.833835</td>
<td>0.0002</td>
</tr>
</tbody>
</table>

Based on the results of table 1, it can be concluded that the size of the board of commissioners and leverage has a positive and significant effect on earnings management. Whereas institutional ownership, the composition of the independent board of commissioners, and audit quality have an influence, but not significantly to earnings management. Prob Value (F-statistics), which is 0.006553 <0.05, it can be concluded that all independent variables, namely institutional ownership (IO), board of commissioner size (BSC), composition of independent commissioners (CIBC), leverage (LEV), and audit quality (AQ) simultaneously has a significant effect on earnings management (EM) variables. R2 (adjusted R2) value is 0.112523, meaning IO, BSC, CIBC, LEV, AQ are able to explain EM simultaneously or together at 11.25%, the remaining 88.75% is influenced by other factors. To test whether company size can
moderate the relationship between IO, BSC, CIBC, LEV, and AQ with earnings management, a residual test is conducted with the following results:

### Table 2 Residual Test Results

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>ML</td>
<td>-3.07E+11</td>
<td>1.10E+11</td>
<td>-2.781973</td>
<td>0.0065</td>
</tr>
<tr>
<td>C</td>
<td>1.21E+12</td>
<td>3.48E+11</td>
<td>3.484996</td>
<td>0.0007</td>
</tr>
</tbody>
</table>

In table 2 it can be seen that the regression coefficient of EM is \(-3.07 \times 10^{11}\) (negative value) and significant (Prob. 0.0065 <0.05). This means that UP is significant in moderating the influence of IO, BSC, CIBC, LEV, and AQ on EM.

**Discussion**

Based on the research results obtained through the various tests mentioned above, it can be interpreted that the influence of the independent and dependent variables and the moderating variables are as follows:

a. **Effect of Institutional Ownership on Earnings Management**

The results of this study indicate that institutional ownership has a positive and not significant effect on earnings management. This means that the presence or absence of institutional ownership in a company, does not hinder the desire of managers to do earnings management to attract potential investors where investors are more interested in relatively stable or increasing profits. These results also indicate that institutional investors are investors who focus on current earnings, thus encouraging managers to conduct earnings management to meet profit goals from investors.

b. **Effect of Board of Commissioners' Size on Earnings Management**

The results of this study provide empirical evidence that the size of the board of commissioners has a positive and significant effect on earnings management. This means that a large size of the board of commissioners has an impact on increasing earnings management, because the more the board of commissioners will make it difficult for them to carry out their roles, including difficulty in communicating and coordinating the work of each member of the board, difficulties in monitoring and controlling actions from management, as well as difficulties in making decisions that are useful for the company.

c. **Effect of Independent Board of Commissioners Composition on Earnings Management**

The results of this study indicate that the composition of the independent board of commissioners has a negative and not significant effect on earnings management. This means that the composition of a high independent board of commissioners does not necessarily have the effect of reducing earnings management. From these results it shows that the independent board of commissioners who are part of the company's commissioners do not perform a function of good supervision of management, thus allowing management to manipulate financial statements.

d. **Effect of Leverage on Earnings Management**

The results of this study indicate that leverage has a positive and significant effect on earnings management. This means that high leverage has an impact on increasing earnings management. The relationship between leverage and earnings...
management practices is explained using the debt agreement theory of positive accounting theory. High leverage is found to correlate closely with violations of debt agreements (Press and Weintrop, 1990). Thus, managers in companies with high leverage tend to do earnings management and choose accounting procedures that improve earnings reporting. In addition, high leverage can also be associated with financial pressure, where financially troubled companies tend to have large negative accruals relating to renegotiation contracts that provide incentives to reduce profits.

e. Effect of Audit Quality on Earnings Management
The results of this study indicate that audit quality has a negative and not significant effect on earnings management. This means that high audit quality does not necessarily have an impact on decreasing earnings management. Quality, relevant and trustworthy financial reports are generated from audits carried out effectively by qualified auditors. Public accountants as external auditors who are relatively more independent of management than internal auditors, are expected to minimize profit engineering cases and increase the credibility of accounting information in financial statements. The use of high-quality auditors is expected to reduce the opportunity for companies to cheat in presenting inaccurate information to the public. In this study, it can be seen that high auditor quality or audited by Big 4 KAP, may not necessarily suppress earnings management behaviour carried out by the company. This is because managers have more information related to the company than outside parties in line with what is described in the asymmetry information, thus giving managers the freedom to do earnings management.

f. Effect of Firm Size as Moderating Variable
The moderating test results using the residual test show that the regression coefficient of earnings management is negative at \(-3.07 \times 10^{11}\) and significant. Negative and significant values can be interpreted that the size of the company is able to moderate the influence of institutional ownership, board size, independent board composition, leverage, and audit quality on earnings management.

V. Conclusion and Suggestion

Conclusion
This study examines whether corporate governance is measured by institutional ownership, board size of commissioners, composition of independent commissioners; leverage; and audit quality has an influence on earnings management with company size as a moderating variable in consumer goods companies listed on the Indonesia Stock Exchange in 2011-2017. From the results of the statistical tests that have been conducted, some conclusions can be drawn as follows:

a. Institutional ownership has a positive and insignificant effect on earnings management, where the presence or absence of institutional ownership in a company does not hinder the manager's desire to do earnings management to attract potential investors where investors are more interested in relatively stable or increasing profits.

b. The board size of commissioners has a positive and significant effect on earnings management, where a large size of the board of commissioners has an impact on increasing earnings management, because the more the board of commissioners will make it difficult for them to play a role that will provide management opportunities for earnings management.
c. The composition of the independent board of commissioners has a negative and insignificant effect on earnings management, which indicates that the independent board of commissioners does not perform a good oversight function of management.

d. Leverage has a positive and significant effect on earnings management. This is in accordance with the debt agreement theory of positive accounting theory, where management will be motivated to do earnings management to avoid violating the debt agreement.

e. Audit quality has a negative and insignificant effect on earnings management, where high auditor quality or audited by Big 4 KAP cannot necessarily suppress management behaviour to conduct earnings management.

f. Firm size is able to moderate the influence of institutional ownership, board size, independent board composition, leverage, and audit quality on earnings management.

**Suggestion**

Some suggestions that researchers ask for several parties, namely:

a. For the next researcher, it is suggested to add other independent variables such as compensation bonuses, profitability, the effect of IFRS adoption, Free Cash Flow, Green Accounting or other variables that might affect earnings management.

b. Using populations and samples outside the company of the consumer goods sector and adding a longer period of bonding.

**Reference**


FCGI. (2000). The Role of the Board of Commissioners and the Audit Committee in the Implementation of Corporate Governance, the Corporate Governance Series. Jakarta: Second Volume.


