INSTITUTIONAL AND MANAGERIAL OWNERSHIP ON EARNINGS MANAGEMENT: COPRPORATE GOVERNANCE

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ABSTRACT

The objective of the research is to analyse about the affect of institutional and managerial ownership on earnings management. This research used 107 manufacturing companies which listed in IDX, selected by purposive sampling. Data analysis used multiple regression. The result of the paper shows that the affect of institutional ownership on earnings management is significant and negative. The affect of managerial ownership on earnings management is not significant. Institutional ownership can reduce earnings management. This shows that institutional shareholders want management to report the state of financial performance, especially profit, in accordance with the actual situation.

Keywords: Institutional Ownership, Managerial Ownership, Earnings Management, Corporate Governance.

INTRODUCTION

Financial reports aim to provide information to help users make business decisions for the company. The information referred to in the financial statements is a description of the financial and economic condition of a company, in which management has the prerogative rights over such financial reporting. The expertise and knowledge possessed by management in business is expected to present good financial reports to assist users in making business decisions (Bandarlipe II, 2009). Managers manipulate earnings in the use of accrual accounting techniques in the hope that it can influence several decisions such as giving bonuses, better performance appraisals or minimizing the tax expense (Nurdiniah & Herlina, 2015).

Managers can manipulate earnings because they have responsibilities in financial reporting. Managers have full control over the accounting system and records in preparing financial statements. An increase or decrease in accounting numbers occurs because managers have the ability to assess and provide information held through option shares and accounting estimates. This flexibility of management provides an opportunity for managers to carry out earnings management through the freedom to choose or change accounting methods (Wiyadi et al., 2015). Earnings management is an intervention by management in determining profit for personal gain (Susanto et al., 2021; Subramanyam, 2014). However, Kusumawardhani (2012) explains that earnings management is not always detrimental if it is carried out within the corridor of opportunity. Earnings management also does not manipulate financial statements because there are options to use several methods and do not violate the provisions. One of the methods used to oversee companies and impose limits on management behavior is corporate governance.

This research is a development of Alzoubi (2016) with several differences including (1) the research period used in this study is 2015 to 2017, while the research conducted by Alzoubi (2016) is 2006 to 2013; (2) the sample used is a public manufacturing company. The

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research objective is to analyse about the effect of institutional and managerial ownership on earnings management.

Institutional Ownership

Institutional ownership is one way of monitoring the performance of company management in managing the company (Mahiswari & Nugroho, 2014). Institutional investors are considered more experienced and can perform better analysis so that management finds it difficult to manipulate them. Therefore, managers tend to avoid earnings management practices and higher quality earnings (Asward & Lina, 2015).

The affect of Institutional ownership on earnings management is significant and negative (Swai & Mbogela, 2016; Alzoubi, 2016). Susanto (2013), Guna & Herawaty (2010), Yang et al. (2009) have different results, namely the affect of institutional ownership on earnings management is not significant. This study contradicts Jao & Pangalung (2011) which have the results of institutional ownership having a positive effect on earnings management. The higher the level of institutional ownership will encourage earnings management.

***H_1*:** *The affect of institutional ownership on earnings management.*

Managerial Ownership

The shares owned management are shares of the company where he works (Agustia, 2013). According to Jensen & Meckling (1976), managerial ownership is one way of reducing earnings management practices. The management who owns a portion of the company's shares will certainly not act fraudulently and will always put shareholders first. Managerial ownership can equalize the interests of management and shareholders.

The affect of managerial ownership on earnings management is significant and negative (Asward & Lina, 2015; Alves, 2012; Larastomo et al., 2016). Kusumawardhani (2012), and Kusumawati et al. (2015) show different results, namely managerial ownership has a positive effect on earnings management. Meanwhile, Agustia (2013), and Susanto (2013) state that the affect of managerial ownership on earnings management is not significant.

***H_2*:** *The affect of managerial ownership on earnings management.*

Independent Commissioner

An independent commissioner is a member of the board of commissioners who has no business or kinship relationship with company officials, which can affect his ability to act independently (Mahiswari & Nugroho, 2014). The independent board of commissioners is responsible for overseeing the quality of information released by management in the financial statements (Agustia, 2013). Therefore, that information in financial reports can be transparent and informative and can facilitate investors' rights to obtain quality information (Mahiswari & Nugroho, 2014).

The independent board of commissioners has a positive influence on earnings management (Susanto, 2016; Arifin & Destriana, 2016). Meanwhile, Agustia (2013), Swastika (2013), and Guna and Herawaty (2010) show different results, namely the affect of independent commissioners on earnings management is not significant. Alzoubi (2016), Asward & Lina (2015), and Susanto (2013) state different results, namely that the affect of independent commissioners on earnings management is significant and negative.

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Commissioners Meeting

The board of commissioners meeting is very important to measure the performance of a company. The more frequent board of commissioners meetings are held, the more effective the board's performance will be. The board, which is active in meeting, puts forward the interests of shareholders. Whereas a board that meets infrequently may only approve management plans and listen to presentations and therefore have no time to oversee issues such as earnings management. Therefore, board meetings play an important role in inhibiting earnings management (Vafeas, 1999).

Ngamchom (2015), and Yang et al. (2009) stated that board meetings have a positive effect on earnings management. The results of the study differ from Prastiti & Meiranto (2013) which state that the affect of meetings on earnings management is not significant. Meanwhile, Kankanamage (2015), Alzoubi (2015), and Gonzales & Meca (2014) stated that the affect of meetings held on earnings management is significant and negative, because the meeting could provide information and supervision of financial reports by the boar of directors.

Board of Commissioners

The commissioners board is a group of certain people appointed by the company with the aim of leading the supervision of the company's activities. The board of commissioners is usually considered as one of the ways in the company's internal control to supervise managers at top level management and promote shareholder welfare (Uadiale, 2012).

Board members have a negative influence on earnings management (Alzoubi, 2016; Xie et al., 2003; Abed et al., 2012). A larger board size makes oversight of management more effective and can reduce earnings management practices. This study contradicts Kusumawati et al. (2015), Salihi & Jibril (2015), and Susanto (2013) state that the affect of board members on earnings management is not significant. Meanwhile, Swai & Mbogela (2016), Gonzalez & Meca (2014), and Swastika (2013) stated that board members have a positive effect on earnings management.

Audit Committee

The audit committee is an independent party or has no relationship and interest with management who understands accounting and other matters related to the company's internal control system (Mahiswari & Nugroho, 2014). Marsha & Ghozali (2017), and Alzoubi (2015) state that the affect of audit committee on earnings management is significant and negative. The same result is shown by Lidiawati & Asyik (2016) which state that an audit committee is expected to reduce earnings management actions. While different results are shown by Prasiti & Meiranto (2013), and Lin & Hwang (2010) which state that the affect of audit committee on earnings management is significant and positive. Meanwhile, Agustia (2013), and Soliman & Ragab (2014) state that the affect of audit committee on earnings management is not significant.

METHODS

This study uses the object of research in the form of manufacturing companies listed on the Indonesia Stock Exchange (IDX) with a period of 3 years. Following are the results of sample selection.

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Table 1 SAMPLE SELECTION RESULTS		
Criteria	**Firm**	**Data**
Manufacturing companies consistently listed on the IDX during 2015-2017.	143	429
Manufacturing companies that do not consistent in financial statements use the rupiah currency	(29)	(87)
Manufacturing companies that do not consistent in financial statements ended 31 December	(7)	(21)
Total	107	321

Source: Data Processing

Managers have the authority to choose accounting policies to achieve certain earnings reporting objectives is an act of earnings management (Scott, 2015). Earnings management is measured using discretionary accruals and applying the modified jones model as was done in Alzoubi's (2015), Susanto, Pradipta, & Cecilia (2019), Susanto, Pirzada, & Adrianne (2019) as follows:

$$\frac{TA_{it}}{A_{it-1}} = \beta_0 \frac{1}{A_{it-1}} + \beta_1 \frac{\Delta REV_{it} - \Delta REC_{it}}{A_{it-1}} + \beta_2 \frac{PPE_{it}}{A_{it-1}} + \varepsilon_{it} \quad (1)$$

Where TA_{it} = NIt- OCFt, TA_{it} total accruals periode t, NI_t net income period t, OCF_{it} Operating cash flow period t, A_{it-1} Total asset period t-1, ΔREV_{it} changes in revenue period t, ΔREC_{it} changes in account receivable period t, PPE_{it} Gross property, plant, and equipment period t, TA_{it} Total Accruals period t, εit DAC_{it} (Absolut of discretionary accruals).

Managerial ownership is shares owned by management or shares owned by affiliates and subsidiaries of the company (Agustia, 2013). According to Agustia (2013), managerial ownership is proxied by the number of shares owned by management to the number of company shares outstanding. Institutional ownership is the shares owned by institutional institutions, for example financial institutions, such as insurance companies, banks, pension funds, investment banking, and other institutions. Institutional ownership is measured using the proportion of the number of shares owned by institutional investors (Alzoubi, 2015).

The independent commissioners is measured by the proportion of the number of independent commissioners in the total board members (Alzoubi, 2016). The calculation of board meetings is the number of board meetings in a year (Alzoubi, 2016). The total combined members of the board of directors and commissioners (Alzoubi, 2016) measure the board of commissioners. The calculation of the audit committee is the number of audit committees (Alzoubi, 2016).

RESULT

Following are the results of descriptive statistics and t test:

Table 2 DESCRIPTIVE STATISTICS				
Variable	**Min**	**Max**	**Mean**	**Std. Deviation**
EM	-0.53447	0.41527	0.00000	0.08854
KI	0.00000	0.70791	0.09069	0,15224
KMN	0.00000	0.68275	0.04544	0.10664
DKI	0.20000	1	0.40708	0.10337
RD	1	36	7.1	4.6987
DK	2	12	4.093	1.7899
KA	1	5	3.065	0.4244

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Source: statistics output

Table 3
t test

Variable	B	Sig.	VIF
(Constant)	0.021	0.621	
KI	-0.063	0.060	1.082
KMN	0.009	0.846	1.031
DKI	-0.051	0.295	1.065
RD	-0.001	0.395	1.059
DK	-0.003	0.365	1.206
KA	0.009	0.994	1.104

Source: statistics output

The t test results show that institutional ownership (KI) has a coefficient of -0.063 and a significance value of 0.060. The significance value is smaller than alpha 10%, which means that H_1 is supported. This shows that the affect of institutional ownership on earnings management is significant and negative. The large number of shares owned by institutional investors can oversee management and tend not to do earnings management. The results are consistent with Alzoubi (2016), and Swai & Mbogela (2016).

The results of the t test above indicate that managerial ownership (KMN) has a coefficient value of 0.009 and a significance value of 0.846. The significance value is greater than alpha 5%, meaning that H_2 is not supported. This shows that the affect of managerial ownership on earnings management is not significant. Company shares in Indonesia that are owned by managerial parties tend to be small, as seen from the descriptive statistics with an average value of below 5%. This shows that managers are more concerned with the interests of investors because investors' share ownership is greater than managers (Agustia, 2013). The results are consistent with (Agustia, 2013; Susanto, 2013).

The t test results show that the independent commissioners (DKI) has a coefficient of -0.051 and a significance value of 0.295. The significance value is greater than alpha 5%, which means that the affect of independent commissioners on earnings management is not significant. This is because the independent commissioners is appointed by the majority shareholder, if it is not concerned with the interests of investors, the company can replace members through the GMS (Agustia, 2013). The results are consistent with (Agustia, 2013; Swastika, 2013).

The t test results show that the commissioners meeting (RD) has a coefficient of -0.001 and a significance value of 0.395. The significance value is greater than alpha 5%, which means that the affect of commissioners meeting on earnings management is not significant. Regardless of the number of board meetings, it cannot reduce earnings management practices, because members of the board of commissioners only meet at meetings and are unable to understand the company's business problems in detail (Prastiti & Meiranto, 2013). The results are consistent with (Prastiti & Meiranto, 2013).

The results of the t test above indicate that the board of commissioners (DK) has a coefficient of -0.003 and a significance value of 0.365. The significance value is greater than alpha 5%, which means that the affect of board of commissioners on earnings management is not significant. The number of the board of commissioners cannot detect earnings management practices that occur. The results are consistent with (Kusumawati et al., 2015; Susanto, 2013; Salihi & Jibril, 2015).

The results of the t test above indicate that the audit committee (KA) has a coefficient of 0.009 and a significance value of 0.994. The significance value is greater than alpha 5%, which means that the affect of audit committee on earnings management is not significant.

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The main purpose of the company to form an audit committee is only to comply with government regulations on the formation of an audit committee, not to prevent earnings management practices (Agustia, 2013). The results are consistent with (Agustia, 2013; Soliman & Ragab, 2014).

CONCLUSION

The affect of institutional ownership on earnings management is significant and negative. Meanwhile, the affect of managerial ownership on earnings management is not significant. The limitation of this study is that the period of this research is 3 years, namely 2015-2017 so it cannot describe the long-term effect, this study uses 2 independent variables, namely managerial ownership and institutional ownership as well as control variables related to corporate governance, namely characteristics of commissioners so that they are not able to explain earnings management specifically. Recommendations for further research are to increase the research period of more than 3 years in order to describe long-term effects, add other variables that can affect earnings management practices so that they can explain specific earnings management such as the characteristics of the audit committee. The managerial implication is that institutional ownership can reduce earnings management. This shows that institutional shareholders want management to report the state of financial performance, especially earnings, in accordance with the actual situation.

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