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THE IMPACT OF GOOD CORPORATE GOVERNANCE, LEVERAGE AND FIRM SIZE ON EARNINGS MANAGEMENT: EVIDENCE FROM INDONESIAN MANUFACTURING FIRMS

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ABSTRACT

The purpose of this study is to ascertain how effective corporate governance, leverage, and firm size affect earnings management in 2023 for consumer goods manufacturing businesses as well as textile and apparel subsectors that are listed on the Indonesia Stock Exchange (IDX). Purposive sampling, which selects samples based on predetermined criteria, was employed in this study. The samples were 43 manufacturing companies in the consumer goods sector, as well as textile and garment sub-sectors and components that satisfied 5 predetermined sample criteria. Based on the results, institutional ownership has no significant effect on earnings management, while independent commissioners, leverage, and firm size have a significant influence on earnings management. Institutional ownership, independent commissioners, leverage, and firm size have a significant effect on earnings management. These research findings enrich academic and practical references regarding the determinants of earnings management in the manufacturing industry listed on the IDX.

Keywords: Good corporate governance, Leverage, Company size, Earnings management

ABSTRAK

Tujuan dari penelitian ini adalah untuk mengetahui pengaruh dari good corporate governance, leverage dan ukuran perusahaan terhadap manajemen laba pada perusahan manufaktur sektor barang konsumsi dan sub sektor tekstil dan garmen yang terdaftar di Bursa Efek Indonesia (BEI) tahun 2023. Pengambilan sampel dalam penelitian ini menggunakan teknik purposive sampling yaitu penetapan sampel berdasarkan kriteria tertentu dengan sampel yang digunakan adalah 43 perusahaan manufaktur pada sektor barang konsumsi dan subsektor tekstil dan garmen serta komponen yang telah memenuhi 5 kriteria sampel yang sudah ditentukan sebelumnya. Berdasarkan hasil penelitian ini, kepemilikan institusional tidak berpengaruh signifikan terhadap manajemen laba, sedangkan komisaris independen, leverage, dan ukuran perusahaan memiliki pengaruh signifikan terhadap manajemen laba. Pada saat yang bersamaan, kepemilikan institusional, komisaris independen, leverage, dan ukuran perusahaan berpengaruh signifikan terhadap manajemen laba. Hasil penelitian ini memperkaya referensi akademik dan praktis terkait determinan manajemen laba pada industri manufaktur yang terdaftar di BEI.

Kata kunci: *Good corporate governance, Leverage,* Ukuran perusahaan, Manajemen laba

INTRODUCTION

One of the metrics used by outside parties to assess a company's performance and state is its financial report. As a tool for decision-making, financial reports can be viewed as a way for management to take accountability for the outcomes of resource management. According to Financial Accounting Standards Statement No. 1 of 2017, the goal of financial reports is to give users valuable information about an entity's cash flow, performance, and financial status so they can make informed financial decisions. Profit is used in accrual-based accounting to quantify a company's overall success. When evaluating performance or determining management's accountability, the primary focus of financial statements is profit information (Sofia & Dasmaran, 2021). As a result, many corporate actors often manipulate or manipulate earnings or profits to maximize or minimize their desired targets by selecting specific accounting policies. This manipulation activity carried out by corporate managers is often referred to as earnings management.

The recent phenomenon of earnings management is the case of PT. Indofarma Tbk, citing the website of the Republic of Indonesia Audit Board (BPK RI) in April 2024. BPK submitted the Audit Result Report (LHP) of the investigation into the Financial Management of PT Indofarma Tbk from 2020 to 2023 to the Attorney General of the Republic of Indonesia. Indofarma is suspected of inflating inventory, engineering transactions, and fictitious recording, so that the financial report does not reflect the actual conditions.

BPK found irregularities in the financial report owned by PT. Indofarma Tbk. Findings of disbursement of funds and charging of costs without being based on transactions worth 24.35 billion rupiah. There is also a loan through fintech that is not for the benefit of the company worth 1.26 billion rupiah. The results of the BPK investigation, the conclusion is that there are irregularities that indicate criminal acts committed by related parties in the management of PT Indofarma Tbk's finances and subsidiaries which resulted in indications of state losses to PT Indofarma and subsidiaries amounting to Rp371,834,530,652 (Rp371.8 billion).

Earnings management has been a central issue in corporate finance and accounting research, influenced by both internal governance mechanisms and firm-specific characteristics (Vidiyastutik & Hendra, 2020; Ali et al., 2015). Good corporate governance (GCG) plays a critical role in mitigating opportunistic managerial behavior, with institutional ownership and independent commissioners often cited as effective monitoring tools (Sáenz & García-Meca, 2014; Santoso & Agoes, 2021). Leverage is frequently associated with earnings management because higher debt levels increase pressure to meet contractual obligations (Paramitha & Idayati, 2020; Kusuma & Lukman, 2023). Firm size may also affect managerial discretion, as larger firms tend to face greater scrutiny from regulators and stakeholders. Prior studies in emerging markets, including Indonesia, provide mixed evidence regarding these relationships (Adisty et al., 2024).

Earnings management is an interesting thing to study because it can reflect the conditions in which the behavior of management in managing profits in financial statements to be reported. The case study above is one example of negative and detrimental earnings management, it is important for us to know about earnings management so that things like the above do not happen and so that we can anticipate in the future. Actions to minimize earnings management can be done through the mechanism and implementation of good corporate governance (GCG). This study aims to examine the influence of good corporate governance (GCG), leverage, and company size on earnings management in manufacturing companies listed on the Indonesia Stock Exchange (IDX). GCG is measured through institutional ownership and independent commissioners, who play a role in overseeing management. Leverage reflects financial pressures that can encourage earnings manipulation, while company size indicates the level of oversight and flexibility in financial reporting. This study

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also analyzes the influence of these three variables simultaneously on earnings management practices.

LITERATURE REVIEW

Agency theory is a theory developed by Jensen & Meckling (1976) which explains the concept underlying financial and economic science involving a two-party relationship between the owner (principal) and the manager (agent). This theory arises based on an explanation of the background of fraud that occurs in the company. There are two basic principles of this theory, the first is that the principal is the party that provides trust while the second is that the agent is the party that is given trust, the agency relationship or contract that is carried out is the granting of authority to the agent to make the best decisions for the principal. Three assumptions of basic human nature are used as the basis for measuring agency theory by Eisenhardt (1989), namely (1) self-interest, humans who care about themselves; (2) bounded rationality, limited thinking power possessed by humans regarding future perceptions; (3) risk averse, humans who always avoid risk. These three basic human natures give rise to new problems regarding opportunism, namely when managers act to prioritize their personal interests.

Dharma et al. (2021) said that when a company experiences a condition or condition where the profit target is not achieved, this is an inability of the management to manage the company. The management will take indirect profit manipulation actions to achieve the company's goals. This happens by increasing profits when the profit condition is decreasing and the company will decrease profits when the company's profit condition is increasing. As a result of this condition, profit management actions arise. Generally, good corporate governance is carried out to minimize profit management actions. Good corporate governance is used as a reference by stakeholders because the internal system seen is from the process policy carried out by agents with how they serve, direct and control management activities by implementing business practices with integrity and objectivity (Muhthadin & Hasnawati, 2022).

Quoted by Fanani et al (2020) good corporate governance is divided into two points of view, namely a narrow point of view in the sense that the company and shareholders have an equal relationship. While in a broad point of view this relationship includes between the company and several stakeholders including employees, suppliers, customers and so on. According to Islamiah & Apollo (2020) the leverage ratio used to assess how much of a company's assets are financed by debt. Thus, the leverage ratio can be defined as the amount of debt a company has to finance its operations, this is why a comparison of assets and liabilities is used in the assessment. The leverage ratio is used as a parameter for how companies describe the sources of operating funds used by the company and shows the possible risks faced.

Astriah et al. (2021) stated that company size is a scale where the size of the company can be classified in various ways, for example, total assets, log size of stock market value and so on. Company size is an important indicator for understanding the company's more complex business processes. Company size refers to the size of the company expressed in total assets, sales, average total sales, and average total assets. Larger companies are able to attract more attention from stakeholders such as investors, creditors, and the government (Ali et al., 2015). This makes the company more careful when reporting their finances.

Based on the understanding, objectives, and literature discussed previously, the research concept is developed to examine the impact of good corporate governance, leverage, and firm size on earnings management. Prior studies provide empirical support for these relationships. Putri (2021) found that good corporate governance mechanisms, including audit committees, managerial ownership, and institutional ownership, positively influence

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earnings management, while independent commissioners have a significant negative effect. Similarly, Setiowati et al. (2023) demonstrated that leverage significantly affects earnings management, as firms with high debt ratios are more likely to engage in earnings management to avoid default risk. Furthermore, Inge (2019) revealed that firm size has a positive impact on earnings management, suggesting that larger firms, due to their need to maintain reputation and public image, are more inclined to manage earnings to present favorable financial performance. Based on Figure, the following research hypotheses are put forward:

H1: Good Corporate Governance has a significant effect on earnings management.
H2: Leverage has a significant effect on earnings management.
H3: Company Size has a significant effect on earnings management.
H4: GCG, Leverage and Company Size have a significant effect on earnings management.

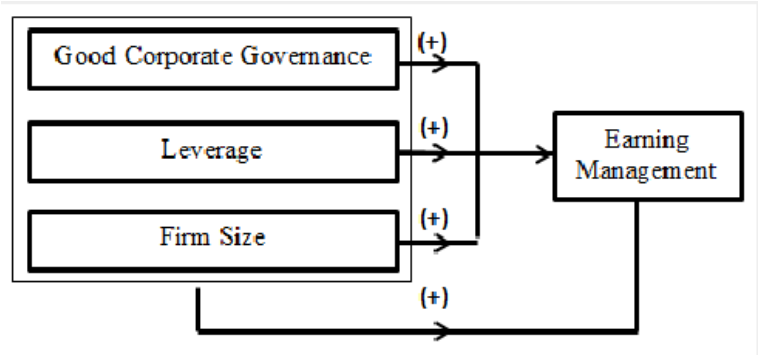

Figure 1. Research Model

METHOD

Design

In this research method, the approach used by the researcher is a quantitative approach. This study was chosen because this type of research uses a hypothesis with a statistical test tool to conclude a hypothesis that uses causal testing. Data for this study were collected using documentation techniques, namely by using documents in the form of images, photos, diagrams, charts, artwork, texts, and so on. The analysis technique used in this study is a descriptive statistical analysis technique. Data analysis using descriptive analysis techniques is a research method that collects, processes, and analyzes data to describe the problem being studied. The research used is Manufacturing Companies in the Food and Beverage industry sector in Indonesia and listed on the Indonesia Stock Exchange for the 2023 period. This study uses financial report data and financial ratio reports published by the Indonesia Stock Exchange for 70 companies. The existing research uses a purposive sampling technique, namely taking samples intentionally according to the requirements or sample criteria required. The criteria used in this study are as follows:

1. Manufacturing companies in the consumer goods sector and textile and garment sub-sectors listed on the IDX
2. Companies that upload and publish complete financial reports in 2023
3. Companies that have independent commissioners
4. Companies whose shares are owned by institutional shareholders
5. Companies that have positive profits in 2023

With the criteria that have been carried out previously, the researcher managed to obtain 43 research samples for manufacturing in the consumer goods sector and textile and garment sub-sectors

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Variables and Measurements

Earnings Management

Healy (1985) created a model to detect profit manipulation by comparing total accruals and total assets. In addition to detecting profit management, this method can also be used to measure profit quality and assess financial risks in the company. The measurement can be done using the following equation:

$$EM = \frac{\sum TAt}{T}$$

Description:
EM: Earning's Management
TAt: (total accruals)/(total assets), where total accruals are obtained from (net income - operating cash flow)
T: 1, 2, 3,….etc (year period)
T: observation year

Good Corporate Governance (GCG)

Institutional ownership indicator, namely company shares owned by institutions.

$$KI = \frac{\text{Total institutional shares}}{\text{Total shares outstanding}}$$

Independent Commissioners

Independent commissioners function as parties who oversee the company's activities to achieve the goals the company wants to achieve.

$$KI = \frac{\text{Total independent commissioners}}{\text{Total board of commissioners}}$$

Leverage

Leverage can be calculated using the formula for calculating the debt-to-asset ratio (DAR), which is based on how much debt the company uses to finance its assets. the calculation can use the following formula:

$$DAR = \frac{Total\ Liabilities}{Total\ Assets}$$

Firm Size

Measuring company size using total assets can be done using the following equation:

Company size = Ln Total Assets

Analysis Method

This study's data analysis processing method makes use of the IBM Statistical Product and Service Solutions (SPSS) Statistics 25 program application. Descriptive Analysis Test. The descriptive statistical analysis test's objective is to assess data by summarizing or describing the gathered information. Data analysis in this study went through several stages, namely, (a) Classical Assumption Test, (1) Normality. The normality test's objective is to determine whether or not the distribution of research data is normal. The sig test of 0.05 indicates that the data is regularly distributed if sig> 0.05; (2) Multicollinearity. To ascertain whether independent variables in a regression model have a strong association with one another, the multicollinearity test is used. Multicollinearity arises if the tolerance value is less than 0.1 or if the VIF value is greater than 10. Multicollinearity does not arise if the tolerance value is greater than 0.1 or if the VIF value is less than 10; (3) Autocorrelation. The autocorrelation test is a procedure used to ascertain whether successive values in a time series are related; and (4) Heteroscedasticity. The Heteroscedasticity Test determines if the residual

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variance for each observation in a linear regression model is unequal. Heteroscedasticity arises when the independent variable's significant value is less than 0.05. It doesn't happen if the independent variable's significant value is greater than 0.05, and (b) This study employed multiple linear regression analysis to examine the effect of institutional ownership, leverage, and firm size on earnings management. Hypothesis testing was conducted using both partial (t-test) and simultaneous (F-test) approaches. The t-test was applied to determine the individual influence of each independent variable, where a t-value exceeding the t-table and a significance level below 0.05 indicate a significant effect, while values above 0.05 indicate no significant effect. The F-test assessed the combined influence of all independent variables on earnings management, with the null hypothesis being rejected if the F-count exceeded the F-table at a 5% significance level. Furthermore, the coefficient of determination (adjusted R^2) was employed to evaluate how strongly the independent variables collectively explain the variation in earnings management, providing insight into the overall explanatory power of the model (Ghozali, 2016).

RESULTS AND DISCUSSION

Nomality Test

The purpose of the normality test is to check whether the distribution of research data to be evaluated is normal or not. The Kolmogorov-Smirnov test has standards or criteria. If sig > 0.05, then the data is normally distributed according to the sig test of 0.05. As can be seen in the Table 1, the Asymp. Sig value has a value of 0.188, this means the data is normally distributed because it has a significance value of more than 0.050.

Table 1. Normality Test

One-Sample Kolmogorov-Smirnov Test	
	Unstandardized Residual
N	43
Asymp. Sig. (2-tailed)	.188[c]

Multicollinearity

The results of the Table 2 in the study show that each variable has a VIF value smaller than 10. Institutional ownership of 1.071; independent commisioner of 1.071; leverage of 1.053 and firm size of 1.043. Meanwhile, the tolerance value of each variable also has a value > 0.1. Institutional ownership of 0.934; independent commisioner of 0.934; leverage of 0.950 and firm size of 0.959. So it can be concluded that the data for each research variable shows no multicollinearity.

Table 2. Multicollinearity Test

Coefficients[a]		
Model	**Collinearity Statistics**	
	Tolerance	**VIF**
GCG (INSTITUTIONAL OWNERSHIP)	.934	1.071
GCG (INDEPENDENT COMMISSIONER)	.934	1.071
LEVERAGE (DAR)	.950	1.053
FIRM SIZE (LN TOTAL ASSETS)	.959	1.043

Autocorellation

The autocorrelation test is a process to determine whether there is a relationship between consecutive values in a time series. The dU value obtained in the table is 1.5367.

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The Durbin-Watson value in Table 3 is 1.773. The value of 4 - dU is 2.463. Therefore, it can be concluded that 1.537 < 1.773 < 2.463. No autocorrelation occurs.

Table 3. Autocorellation

Model Summary[b]					
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**	**Durbin-Watson**
1	.329[a]	.108	.014	.296	1.773

Heteroscedasticity

The requirement for a heterocedasticity test is that the significance value of each independent variable must be above 0.50. Based on Table 4, it can be concluded that heteroscedasticity does not occur in the regression model. Each variable has a significance value greater than 0.050: 0.905 for institutional ownership, 0.226 for independent commissioners, 0.351 for leverage, and 0.129 for firm size.

Table 4. Heteroscedasticity

Coefficients[a]						
Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**T**	**Sig.**
		B	**Std. Error**	**Beta**		
1	(Constant)	1.327	.769		1.726	.092
	Institutional ownership	.026	.216	.019	.120	.905
	Independent commisioner	-.525	.426	-.195	-1.231	.226
	Leverage	.241	.256	.148	.944	.351
	Firm size	-.041	.027	-.243	-1.551	.129

Multiple Linear Regression Analysis Test

The results in Table 5 show that the institutional ownership variable has a coefficient of 0.026, indicating that every one-unit decrease in institutional ownership will increase management earnings by 0.026 units. Conversely, independent commissioners have a negative coefficient of -0.525, meaning that every one-unit decrease in this indicator actually decreases management earnings by 0.525 units. Meanwhile, leverage shows a positive coefficient of 0.241, indicating that a one-unit decrease in leverage will increase management earnings by 0.241 units. Meanwhile, firm size has a coefficient of -0.041, indicating that every one-unit decrease in company size will increase earnings management by 0.041 units.

Table 5. Multiple Linear Regression Analysis Test

Coefficients[a]						
Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**T**	**Sig.**
		B	**Std. Error**	Beta		
1	(Constant)	1.327	.138		9.589	.000
	GCG Institutional ownership	.026	.039	.051	.666	.509
	GCG Independent commisioner	-.525	.077	-.528	-6.840	.000
	Leverage DAR	.241	.046	.401	5.246	.000
	Firm size	-.041	.005	-.656	-8.618	.000

Partial Test (T)

Based on the statistical test results in Table 6, the Good Corporate Governance (GCG) variable with institutional ownership indicators shows a t-value of 0.666 which is smaller than the t-table of 1.684, and a significance value of 0.509 which is greater than 0.05. This

indicates that institutional ownership does not have a significant effect on earnings management. In contrast, the independent commissioner indicator has a t-value of -6.840 with a significance of 0.000, which is smaller than 0.05 and smaller than the t-table of -1.684, so it can be concluded that independent commissioners have a significant and negative effect on earnings management. Furthermore, the leverage variable shows a significant and positive effect on earnings management, with a t-value of 5.246 which is greater than the t-table and a significance value of 0.000. Meanwhile, firm size has a t-count of -8.618 and a significance of 0.000, which shows a significant and negative influence on earnings management, considering that the t-count is smaller than the t-table indicating a negative direction.

Table 6. Partial Test (T)

Coefficients[a]						
Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**T**	**Sig.**
		B	**Std. Error**	**Beta**		
1	(Constant)	1.327	.138		9.589	.000
	GCG Institutional ownership	.026	.039	.051	.666	.509
	GCG Independent commissioners	-.525	.077	-.528	-6.840	.000
	Leverage DAR	.241	.046	.401	5.246	.000
	Ukuran Perusahaan	-.041	.005	-.656	-8.618	.000

Simultaneous Test (F)

The requirement for the ANOVA test, or simultaneous test, is that the calculated F-value must be greater than the F-table value. In Table 7, the calculated F-value is 35.419, which is greater than the F-table value of 3.24, and the significance value of 0.000 is less than 0.05. Therefore, it can be concluded that the variables Good Corporate Governance, Leverage, and Firm Size have a significant influence simultaneously on Earnings Management.

Table 7. Simultaneous Test

ANOVA[a]						
Model		**Sum of Squares**	**Df**	**Mean Square**	**F**	**Sig.**
1	Regression	.402	4	.101	35.491	.000[b]
	Residual	.108	38	.003		
	Total	.510	42			

Multiple Determination Coefficient Test

Good Corporate Governance, Leverage, and Company Size all have a significant impact on Earnings Management, as seen by the correlation value of 0.888 in the Table 8. An R square value of 0.789 is obtained by squaring the correlation value from the value of 0.888. The factors Good Corporate Governance, Leverage, and Company Size can influence Earnings Management by 78.9%, according to the R square value with a magnitude of 0.789. Other variables that are not the subject of this study influence the remaining portion.

Table 8. Determination Coefficient

Model Summary				
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	.888[a]	.789	.767	.05324
a. Predictors: (Constant), Firm Size, Leverage DAR, GCG Institutional Ownership, GCG Independent Commissioners				

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Disscussion

Based on previous research, the research results show that institutional ownership has a positive but insignificant effect. This means that companies whose shares are owned by institutions do not guarantee not to carry out manipulation through positive profit mechanisms. This possibility can occur because management is required to meet the profit targets determined by investors, making it unable to reduce manipulation or profit management. This situation is inversely proportional to the theory and hypothesis which states that the value of high share ownership means that control should be held by the highest shareholder as the decision maker in the company (Asim & Ismail, 2019). The results of this study are strengthened by research conducted by (Potharla et al., 2021) which states that Institutional ownership has no effect on earnings management. The regulatory environment in Indian companies should further promote institutional ownership.

Based on previous research, the research results show that independent commissioner has a negative but significant effect. This indicates that it has been demonstrated that the presence of independent commissioners can reduce profit management activities. The more supervision is carried out in the preparation and reporting of profits, the less the possibility or opportunity to carry out profit management. The results of this study are strengthened by research conducted by (Putri, 2021) which states that the greater the proportion of independent commissioners, the less likely it is that companies will engage in profit management practices due to stricter supervision in financial preparation and reporting.

Based on previous research, the research results show that leverage has a positive and significant effect. This means that companies with high debt levels tend to be more closely monitored by creditors, making it difficult for them to identify loopholes for earnings management. Debt levels exceeding assets are more likely to lead to earnings management because companies want to demonstrate good financial management performance (Hashed & Almaqtari, 2021). The results of this study are strengthened by research conducted by (Usman & Yahaya, 2025) which states that Leverage correlates and significant with earnings management. Companies with high debt levels are thought to encourage earnings manipulation.

Based on previous research, the research results show that firm size has a negative and significant effect. This indicates that because big businesses receive more media attention, they are more likely to report with caution. Small businesses are also frequently disregarded in order to relax reporting requirements. The results of this study are strengthened by research conducted by (Githaiga et al., 2022) which states that there is an interaction between company size and earnings management, with the results showing a significant effect. Company size is considered to minimize earnings management. Using company size and other variables in this study, researchers demonstrated that it can effectively prevent opportunistic behavior (Ghofir & Yusuf, 2020).

CONCLUSION AND RECOMMENDATION

The findings of the study on the impact of Good Corporate Governance, Leverage, and Company Size on profit management in manufacturing companies listed on the Indonesia Stock Exchange are based on statistical data processing and data analysis description, it can be concluded that institutional ownership was found to have a positive but insignificant relationship with earnings management practices. Conversely, independent commissioners showed a negative and significant relationship, indicating the important role of independent oversight in curbing financial statement manipulation practices. Leverage showed a positive and significant effect on earnings management, indicating that debt pressure can encourage management to engage in earnings management. Company size also had a negative and significant relationship, indicating that the larger the company, the stronger the supervision

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received, thus lowering the tendency to engage in earnings management. Simultaneously, good corporate governance, leverage, and company size were shown to have a significant influence on earnings management. This third variable plays a crucial role in limiting earnings management activities and can be considered a strong predictor in identifying the tendency of such practices in the manufacturing sector.

The study's findings imply that future researchers should reexamine the characteristics that may lead to earnings management activities by taking into account additional variables that affect earnings management, such as profitability, managerial ownership, audit quality, and a number of other variables. This is due to the fact that factors other than the independent variables in this study can influence profits management by up to 21.1%. Additional researchers can also retest with a larger population and different time periods.

This study has several limitations that should be considered as evaluation material for further research development to achieve more comprehensive results. First, this study only used three variables: good corporate governance, leverage, and company size, although many other factors can also influence earnings management practices. Second, the time span used was limited to one financial year, thus not being able to comprehensively depict long-term trends. Third, the population coverage in this study was limited, covering only two subsectors of the manufacturing industry. Based on the conclusions and limitations, the researchers offer several recommendations for further research. This study suggests that future researchers re-examine the factors influencing earnings management practices, taking into account other variables such as audit quality, managerial ownership, profitability, and other relevant variables. This is important because the results indicate that 21.1% of the variation in earnings management is influenced by factors outside the independent variables used in this study. Furthermore, the researchers recommend using a longer time period and a broader population, such as in the banking sector, Islamic banking, hospitals, and other entities that have the potential to make significant contributions to a more comprehensive understanding of earnings management practices.

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