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INTERACTION OF INDEPENDENT COMMISSIONERS AGAINST EARNING MANAGEMENT DETERMINANTS

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Abstract:

This research aims to test the related party transaction influence, company size and managerial ownership of profit management. The research also aims to test the influence of independent Commissioner's interaction on the factors of the earning management determinant. The samples used in this study were the manufacturing companies listed in the Indonesian Stock Exchange (IDX) during the period 2014 and 2015. Total samples amounted to 25 companies using the purposive sampling technique. The analysis method uses multiple regression and moderating regression with an absolute value-difference approach. The results of hypothesized testing showed that related party transactions had significant positive impact on earning management. Company size and Manejerial ownership have significant negative effect on earning management. In addition, the results showed that independent commissioners were interfering with the influence of the company's size on profit management, as well as independent commissioners to However, independent commissioners do not Interveny related party transactions against earning management.

Keywords: Manejerial Ownership; Independent Commissioner; Earning management; Related party transaction; Company Size.

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1. Introduction

Competition between companies triggers the attention of investors from outside with the presentation of the company's financial statements. All sorts of ways include manipulating profits so that the company's financial statements look attractive. One form of management accountability to shareholders is a financial statement, which provides an overview of financial position, company performance and financial position change. The financial reporting information is aimed at the decision making process, both for internal and external parties (Sukman *et al.*, 2017). Earning management is a management intervention in the financial report compilers to raise or lower the accounting profit according to its interests (Scott, 2009), in line with Healy and Wahlen (1999). Management is the one who gives the information of the financial statements, which will be assessed and evaluated in performance based on the company's financial statements. Therefore,

the management of the company may use the basis of accruals (accrual basis) for specific purposes which are opportunistic, which in turn is intended to be an attempt to obtain bonuses and other compensation (Wulandari and Kusuma, 2011).

Earnings Management is described as the behavior of managers who aim to influence the profit to achieve a specific goal (Yendrawati and Paramitha, 2014). Regardless, Enron's fraud involves dealing with a special relationship (Farahmita, 2011). Sherman and Young (2001), mentioning an indexed area aggressive accounting, a related party transaction, which allows the company to arbitrarily raise profits. Related party transactions in the company are viewed as having the goal of maximizing the shareholder's wealth (Hutapea, 2008). Various factors that can affect the action of earning management, one of which is the size of the company (Prasetya and Gayatri, 2016). Muliati (2011) and Jao and Pagalung (2011) find that the company's size negatively affects earning management negatively. In contrast, Rahmani and Akbari (2013) found that the company's size was positively influential in earning management.

Then, the ownership structure is a factor that is also able to influence the company's course which ultimately affects earning management due to the control they have. Ownership of a manager also determines the policy and decision-making of the accounting method applied to the managed company (Boediono, 2005). The concept of agency theory according to Anthony and Govindarajan (1995:143) is a contract between principal and agent. Through agency theory, management actions can be overcome and minimized through the mechanisms of good corporate governance (Naftalia and Marsono, 2013).

The practice of corporate governance has a significant relationship to earning management such as research conducted by Watfield et al. (1995), Gabrielsen et al. (1997), and Wedan (2004). Meanwhile, Siregar and Bachtiar's Research (2004) and Darmawati (2003) are inversely proportional, i.e. not finding a significant relationship between corporate governance practices and earning management. This research aims to test the related party transaction influence, company size, and managerial ownership of earning management. In addition, this research also aims to test the interaction of independent Commissioners on related party transactions, company size, and managerial ownership with earning management.

Hypothesis Development

Related Party Transaction and Earning Management

The factors that cause earning management one is done through the transactions of Related Party Transaction-RPT, which is the interaction of the child and parent in conducting transactions (Guing and Aria, 2011). Disclosure of the parties having a special relationship is expressed in the Financial Accounting Standard statement (PSAK) No. 7 Revised 2010. This statement is explained about the relationship with the special parties, balances, and commitments between the entities and the parties that have a special relationship. The statement is expressed due to financial position reports, income statements, transactions and balances influenced by the existence of parties with special relationships including commitments with such parties. Prasyasa Research (2014) proves that transactions with special parties influence significantly on the quality of profits. Thus, the research hypothesis is formulated as follows:

H₁: Related party transactions have positive effect on earning management.

Company Size and Earning Management

The greater the number of company assets, the greater the amount of capital is planted, the more the sales, the more turnover the money, and the greater the market capitalization, the greater is known in society (Sudarmadji and Sularto, 2007). Choutrou et al. (2001) found that the company's size in the United States had a negative impact on earning management. Companies that have large quantities of assets, lack the urge to do earning management than small companies. Research in Indonesia by Siregar and Utama (2005), found that the company size measured by using the natural logarithmic value of the company's equity market at the end of the year significantly negative effect on the scale of earning management. That is, the larger the size of the company the smaller the management of its land. Thus, the research hypothesis is formulated as follows:

H₂: The size of the company negatively affects earning management.

Manejerial Ownership and Earning Management

Warfield et al. (1995) conducts managerial relationship testing with corporate profit information and discretionary accrual using capital market data in America. The study found evidence that managerial ownership were negatively related to earning management. Gabrielsen *et al.* (1997) proves the influence of managerial ownership of profit management by using capital market data samples. This, in line with the research of Mahariani and Ramantha (2014), that managerial ownership negatively affects earning management. The results indicated that managerial ownership managed to be a mechanism to reduce or minimize earning management. Thus, the research hypothesis is formulated as follows:

H₃: Managerial ownership affects negatively on earning management.

Independent commissioner, related party transaction, and earning management

Transaction related party transactions are more done by companies that are in groups compared to independent operating companies (Jian and Wong, 2003). The definition of related party transactions according to Chhaochharia and Grinstein (2007) are transactions between the company and its insiders or affiliates. Such transactions are the purchase and sale of goods or services from or to the insiders, giving loans to executives that are all related party transactions. Corporate governance is a good corporate governance that includes a series of relationships between company management, independent Commissioner, shareholders, and other stakeholders (Indra and Yustiavandana, 2006). Corporate governance as a guideline for controlling and directing the company so that it can achieve goals and objectives that can add value to the company and can be beneficial for all stakeholders for the long term. Stakeholders in this regard are all parties to the Board of Directors, management, shareholders, employees and the public. The explanation above requires that good corporate governance will have an impact to weaken the action of earning management because the function of good corporate governance is controlling and directing so that it will control the managers of The company. Thus the research hypothesis is formulated as follows:

H₄: Independent Commissioner interacts related party transactions against earning management.

Independent commissioner, company size, and earning management

Earning management is a condition of management that intervenes in the process of drafting financial statements for external parties so as to leveling, raising, and lowering profits (Schipper, 1989). As stated Veronica and Bachtiar (2004), that corporate governance is the concept to control

the opportunistic action undertaken by management. Thus, good corporate governance will suppress and weaken the action of earning management that is influenced by the company size. This explanation is also related to H2, that actually the earning management is influenced by the company size, thus the existence of good corporate governance as a good corporate governance concept will weaken the action of earning management. Thus the research hypothesis is formulated as follows:

H5: Independent commissioners interacted with the company's size influence on earning management.

Independent commissioner, Manejerial Ownership, and Earning management

The ownership of the company is influential in conducting profit management actions. According to Stockmans et al. (2010), the issue of the low quality of earning management action disclosure is due to high levels of stock ownership concentrations with a lack of market monitoring which causes high likelihood of controlling Shareholders to expropriate or take over minority shareholders. Corporate governance process is implementation and implementation of corporate governance through the implementation of principles of justice, transparency, accountability, and Responsibility (Majidah, 2005). Companies with good system and good governance also, will suppress the loss of actions for the company. Thus the research hypothesis is formulated as follows:

H6: Independent commissioners interacted with the influence of managerial ownership of earning management.

2. Materials and Methods

The population of this research is all manufacturing companies listed on the Indonesia Stock Exchange from 2014-2015. Sample selection is done using the purposive sampling method. Purposive sampling method is used to obtain a representative sample according to the specified criteria. The sample criteria used were: 1) the company was in the manufacturing industry listed on the Indonesia Stock Exchange (IDX) during the period 2014-2015; 2) A manufacturing company reporting in rupiah currency; 3) A company that owns the complete data of an independent board of Commissioners and data necessary to detect earning management; 4) Report company that has information related to party transaction.

Related Party transactions can be assessed on three indicators of the post that come from the financial position report and the income statement of the company, where is the transaction of sales, asset transactions and transaction obligations. These transactions will be seen how much the value of the asset transactions, liabilities and sales overall. It can be described Jian and Wong (2003) with the following formulations:

$$RPA = \frac{RPT \text{ Assets Transaction}}{\text{Total Assets}}$$

$$RPL = \frac{RPT \text{ Liabilities Transaction}}{\text{Total Liabilities}}$$

$$RPS = \frac{RPT \text{ Sales Transaction}}{\text{Total Sales}}$$

$$RPT = \frac{RPA + RPL + RPS}{3}$$

Description:

RPA : *Related Party Assets*

RPL : *Related Party Liabilities*

RPS : *Related Party Sales*RPT : *Related Party Transaction*

According to Dinni (2008) company size as a whole of the assets owned by the company, which can be seen from the left side of the financial position report. Thus, the size of the company is measured by the following formulations:

Company size (UP) = Ln (Total assets)

Managerial ownership (MGROWN) is a proxy of differences in managers and shareholders' purpose of controlling ownership. The greater the ownership of managers on the company, the lower the interest in doing earning management activities because there is a goal alignment between managers and shareholders. Managerial ownership can be measured from the percentage of the manager's share (Wahidahwati, 2002). Good Corporate governance In this study was proscribed with independent commissioner. The proportion of independent Commissioners is measured using the percentage of independent commissioners who came from external companies from all sizes of the company's independent commissioners (Herawaty, 2008).

Measurement of earning management using Discretionary accrual (DAC). Discretionary accrual, because it is a component that can be manipulated by managers like credit sales. To measure the DAC, it will first measure the total accruals. The Total accruals are classified into discretionary and non-discretionary components (Midiastuty and Machfoedz, 2003), with stages:

$$NDA_{it} = \alpha_0 + \alpha_1 CO_{it} + \alpha_2 NPA_{it} + \alpha_3 \Delta NPA_{it} + 1 + \epsilon$$

$$DA_{it} = TA_{it} - NDA_{it}$$

Description:

Coit : *Loan charge-off.*

LOAN : *Loan outstanding.*

NPA : *Nonperforming asset.*

ΔNPA : Difference between nonperforming assets T + 1 and nonperforming assets are all variables deflated with Equity book value Plus loan loss backup.

TA : Total accruals (for which the special accrual model is calculated based on the total balance of elimination of productive assets).

DA : Discretionary accruals

NDA : Nondiscretionary Accruals.

Analytical techniques

The analytical techniques used to examine the research hypothesis are multiple linear regression analyses and the analysis of moderated regression with absolute difference value approaches. The second equation of the analysis technique is as follows:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e$$

$$Y = \alpha + \beta_1 ZX_1 + \beta_2 ZX_2 + \beta_3 ZX_3 + \beta_4 ZM + \beta_5 |ZX_1 - ZM| + \beta_6 |ZX_2 - ZM| + \beta_7 |ZX_3 - ZM| + e$$

Description:

Y : Earning Management

 α : ConstantX₁ : Related party transactionX₂ : Company SizeX₃ : Managerial Ownership β_1 - β_3 : Multiple regression coefficient

ZX1 : Standardize related party transaction

ZX2 : Standardize Company Size

ZX3 : Standardize Managerial Ownership

ZM : Standardize Independent commissioner

|ZX1 – ZM| : It is a measured interaction with the absolute difference values between ZX1 and ZM

|ZX2 – ZM| : It is a measured interaction with the absolute difference values between ZX2 and ZM

|ZX3 – ZM| : Merupakan interaksi yang diukur dengan nilai absolut perbedaan antara ZX3 dan ZM

e : Error term

Hypotheses are tested by using significance levels (α) = 0.05 or 5%. To test the related party transaction influence, company size, and managerial ownership of earning management are conducted by testing the T value at significance level (α) = 0.05. Similarly, hypothesis testing that demonstrates the influence of independent commissioners ' interactions with related party transactions, company size, and managerial ownership with earning management. If the value significance is < 0.05 then the hypothesis is acceptable, conversely if the value significance is > 0.05 then the hypothesis is rejected (unacceptable).

3. Results and Discussions**Descriptive Variables**

A descriptive analysis aims to give the reader a general overview of the research variables (Hadi, 2006). Descriptive variables of the study were shown in the following Tabel.

Tabel 1: Descriptive variables

	N	Min	Max	Mean	Std. Dev
<i>Related Party Transaction</i>	50	,0000003	,6670445	,095592557	,1583306145
Company Size	50	25,72	34,62	28,4284	2,39503
Managerial Ownership	50	,003	12,76	2,0828	3,39170
Independent commissioner	50	,25	,60	,3845	,08184
Earning Management	50	-,0027648	,0320971	,003505421	,0085520046
Valid N (listwise)	50				

Source: Processed Data (2017)

Table 1 shows the descriptive statistics of the standard deviation value of 0.15 indicating that the special transaction performed on the related party is almost the same, the lowest minimum value of 0.0000003, the highest of 0.66, the average of 0.09. The company size variables in this study

have a minimum value indicating that there are companies that have the lowest number of assets at 25.72, the highest of 34.62. An average of 28.42. The standard deviation value is 2.39 indicating the size of the company in this research varies greatly between companies.

The managerial ownership variables in this study have a minimum value indicating that the shares owned by the lowest managers amounted to 0.003, while the maximum value indicates that the shares owned by the top managers amounted to 12.76. The average stock value of the managerial ownership is 2.08 indicating that the shares owned by the managers are low. The standard deviation value of 3.39 indicates that managerial ownership in the company varies greatly between companies.

Independent Commissioner variable has a minimum value of 0.25 it shows that independent commissioners tend to be low by 25. The maximum value indicates that independent commissioners tend to be high by 60. The average value indicates that the independent commissioner variable is 38. The standard deviation value of 0.08 This indicates that the independent commissioner in the company is almost equal or not diverse among companies one with other companies.

Earning management variable has an average value of 0.003 with a minimum value of -0.002 and a maximum of 0.035. The minimum value indicates that from all companies in this research there are companies that have the lowest earning management value of -0.002 the company is PT Kedaung Indah Can Tbk. Maximum value of 0.035 Show that of the many companies in this research there are companies that have the highest earning management value. Overall the company in this research has a management because it has an average value above the number 0 which is 0.003. The standard deviation value is 0.008 indicating that the value of the company's earning management in this study is almost identical, or the uniform is done by the company.

Multiple Regression Test Results

H1, H2, and H3 hypothesis testing results are shown in the following 2 tables.

Table 2: T test result (double Linear regression)

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
1 (Constant)	,025	,010		2,444	,018
Related Party Transaction	,039	,006	,723	6,748	,000
Company Size	-,001	,000	-,230	-2,303	,026
Managerial Ownership	-,001	,000	-,374	-3,520	,001

Source: Processed Data (2017)

The interpretation and discussion of the proposed research hypothesis testing (H1, H2 and H3) results can be seen as follows:

Related Party Transactions Influence on Earning Management (H₁)

Based on table 2 can be seen that related party transaction has T count > T table, ie t count of 3.420 while T table with sig. $\alpha = 0.05$ and $df = n - K$, that is $50 - 4 = 46$ of 1.679 with significance rate of 0.001 which is smaller than 0.05, then H₁ accepted. This means that related party transactions have a positive and significant effect on earning management. Thus, the first hypothesis that related party transactions have a positive and significant impact on earning management is proven. The results of this research show that the related party transactions that the company has impacted the company's earning management. The higher the related party transaction component is increasing the earning management that the company is doing. This is in accordance with the research conducted by Chen et al. (2009), found that the company is controlled by the company that controls the financial performance of the controlled company will be bad. In addition, from the results of the study Prayasa (2014) proved that the transaction with the privileged party has a significant effect on the quality of profit.

Effect of Company Size on Earning Management (H₂)

Based on table 2 can be seen that the size of the company has a T count of 2.618 > T table 1.679 with a significance rate of 0.011 which is smaller than 0.05, then H₂ accepted. This means that the company's size is negatively and significantly influential on earning management. Thus, the second hypothesis states that the size of the company negatively affects proven earning management. The results of this research show that the higher size of the company then the lower the earning management done by the company. This is in line with the research results of Muliati (2011) and Jao and Pagalung (2011), which found that the company's size negatively affects earning management. In addition, the research thought was supported by the research results of Siregar and Utama (2005) which concluded that the company's size has a significant negative effect on earning management.

Influence of Managerial Ownership of Earning Management (H₃)

Based on table 2 it can be seen that the managerial ownership has T count of -0.164 < t table 1.679 with a significance rate of 0.870 which is greater than 0.05, hence the H₃ is rejected. This means that managerial ownership has a negative effect on the company's earning management. Thus, a third hypothesis which states that managerial ownership negatively affects proven earning management. Jensen and Meckling (1976) suggest that the greater the proportion of ownership of the company's management, the management strives to meet the interests of shareholders who are not themselves. The results of this study were consistent with the research of Mahariani and Ramantha (2014) that managerial ownership negatively affects earning management.

Moderating regression test Results Absolute Difference value approach

The results of the H₄, H₅, and H₆ hypothesis tests are shown in the following 3 tables.

Table 3: T test result (absolute difference value)

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	-,002	,002		-1,154	,255
Zscore: <i>Related Party Transaction</i>	,009	,001	1,024	6,763	,000
Zscore: <i>Company Size</i>	-,002	,001	-,270	-2,917	,006

Zscore: Managerial Ownership	-,006	,001	-,759	-5,158	,000
Zscore: Independent commissioner	-,002	,001	-,273	-2,309	,026
X1_M	-,002	,001	-,185	-1,247	,219
X2_M	,002	,001	,235	2,220	,032
X3_M	,006	,001	,578	3,864	,000

Source: Processed Data (2017)

The interpretation and discussion of the proposed research hypothesis test (H4, H5 and H6) results can be seen as follows:

Independent Commissioner Interacted Related Party Transactions Against Earning Management (H₄)

From the test result the absolute difference in value seen in table 3 indicates that the variable moderating X1_M has a T count of -1.247 > T table 1.682 with a significance rate of 0.219 which is greater than 0.05. This means that independent Commissioners do not intervening or do not corroborate related party transactions against earning management. So the fourth hypothesis (H₄) stating independent Commissioner intervening related party transactions against earning management is not proven or rejected. This is due to the independent Commissioner of the company that is observed is only formality only to comply with the regulations and is not intended to enforce the company's good corporate governance obligations. The existence of this independent Commissioner does not operate a good monitoring function and does not use its index to supervise the board of directors policy.

Independent Commissioner Interferacts with The Company's Size Influence on Earning Management (H₅)

The test result of the absolute difference in value seen in table 3 indicates that the X2_M moderating variable has a T-count of 2.220 > T table 1.682 with significance rate of 0.032 which is smaller than 0.05. This means that independent commissioners are interacted with the company's size influence on earning management. So, the fifth hypothesis (H₅) that says independent commissioners are interacting influence of the company's size against the earning management proven or accepted. According to Egon (2000), the Independent Commissioner is the core of corporate governance that has been established to ensure the implementation of the company's strategy, supervising management in managing the company, and requiring accountability. Siallagan and Machfoedz (2006) presented the role of independent Commissioner is expected to increase the quality of profit by limiting the level of earning management through the monitoring function of financial reporting.

Research on the existence of independent commissioners was conducted by Chtourou et al. (2001) who found that earning management was significantly related to the Independent Commissioner. The results showed low income increasing in the company who had outside board members who were experienced as a board members in the company and other companies. Then with the theory of agency explained that there is a principal who gives mandate to the agent in running a company. The role of independent commissioner of every large company will be more cautious to do earning management than small companies.

Independent Commissioner Interfering with The Influence of Managerial Ownership of Earning Management (H₆)

The test result of the absolute difference in value seen in table 3 indicates that the X3_M moderating variable has the count of $3.864 < t$ table 1.682 with a significance rate of 0.000 which is smaller than 0.05. This means that independent commissioners are interfering with the influence of managerial ownership of earning management. So, the sixth hypothesis (H₆) stating independent commissioners intervening the influence of managerial ownership on proven earning management. It can generally be stated that the percentage of shareholding by management (managerial holdings) tends to affect profit management actions.

According to Jensen and Meckling (1976), the practice of earning management can be minimized by aligning the differences of interest between the owner and the management, by enlarging the management ownership. For low shareholding, the incentive of the manager's opportunistic behavior will increase (Shleifer and Vishny, 1996). Agency theory is the basis of a good corporate governance and basic concept used to understand corporate governance. The agency's theory implies that there is an information asymmetry between the manager as an agent and shareholder as the principal.

4. Conclusions and Recommendations

4.1. Conclusion

Based on the collected data and tests that have been done it can be concluded that the related party transaction has significant positive impact on earning management. Company size and Managerial ownership have significant negative effect on earning management. This condition indicates that transactions with privileged parties trigger opportunistic behaviors to improve earning management, while the company size and magnitude of the proportion of managerial ownership minimizes opportunistic behavior earning management.

The results showed that independent commissioners were interfering with the influence of the company's size on earning management, and also interacted with the influence of managerial ownership on earning management. In contrast, independent commissioners do not Interveny related party transactions against earning management. The existence of independent commissioners strengthened the opportunistic behavior of large-scale enterprise earning management and with a large proportion of managerial ownership. However, independent commissioners do not corroborate the motives of special transaction parties doing opportunistic earning management.

4.2. Recommendations

Further studies are expected to observe other variables related to earning management. Some of these variables are company performance, institutional ownership, family ownership, and so forth. The samples used in this study focused only on manufacturing companies listed in the Indonesian Stock exchange period 2014-2015. Further research is suggested to enlarge the number of samples as well as extend the research period.

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