Influence of Good Corporate Governance and Audit Quality on Discretionary Accrual with Performance as Mediation at Aneka Industry in Indonesia

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ABSTRACT

Earnings management is engineering by managers to show better profits for bonus plans and company performance. This study aims to empirically examine the influence of good corporate governance and audit quality on earnings management with performance as a moderating variable in various industrial companies on the Indonesian stock exchange. The population of this study is various industrial companies with a sample of 180 companies during 2017-2022 with data processing using partial least squares (PLS) from secondary data from the Indonesian stock exchange's financial reports. The results of the study indicate that there is a significant effect of good corporate governance and audit quality on earnings management and performance is successful as a moderating variable in the effect of good corporate governance and audit quality on earnings management.

KEYWORDS: *good corporate governance, audit quality, discretionary accruals, performance, Indonesian stock exchange.*

Introduction

Good corporate governance is good corporate governance that can be carried out by the board of commissioners, audit committee, or share ownership by managers and the public. Audit quality is a quality examination carried out by an auditor who adheres to or is guided by the professional standards of public accountants (SPAP). Here the auditor can come from the big four or non the big four. This means that auditors who already have a good reputation or who are still being. Good corporate governance and audit quality are thought to have an effect on earnings management which has been studied by Darmawan (2019) with the results showing a significant effect of good corporate governance and audit quality on firm value and company earnings management. Another study was also conducted by Wahyuningsih (2020) on the effect of good corporate governance structure on company performance and earnings management with significant results. Different research has shown by Agustia (2020) that good corporate governance has no significant effect on earnings management. Based on previous studies that were not consistent, a study was conducted entitled The Influence of GCG and audit quality on earnings management with Performance as a mediating variable in various industries.

Literature Review

Performance

Performance is defined as the results achieved by the company during a certain period in which the company operates. Company performance can be measured by return on equity, return on assets, or Tobin's Q.

Earnings Management

Watts and Zimmerman (1986) say that there are 3 motivations for managers to manage earnings, namely: the bonus plan hypothesis, the debt contract hypothesis, the political cost hypothesis, tax motivation, leadership changes, IPO, and information communication with investors. Earnings management is proxied by discretionary accruals. Discretionary accruals are calculated by subtracting the total accrual (TA) value from the non-discretionary accruals (NDA) value.

Calculation of Total Accruals:

a. Calculation of total accruals with the Balance Sheet approach. Based on the Healy (1986) model:

$$= \frac{ДCa\ it\ -\ ДCI\ it\ -\ ДCash\ it\ -\ ДSTD\ it\ -\ Dep\ it}{A\ it-1}$$

Collins and Hriber model (1999) in Belkoui (2003)

$$= (ДCA\ it - ДCL\ it - Дcash\ it + ДSTDEBT\ it - DEPTN\ it)$$

Calculation of total accruals with the Cash Flow Approach

Based on Dechow (1994); Collins and Hribar (1999) in Belkoui (2003)

$$TACC\ it = NI\ it - CFO\ it$$

Discretionary Accrual Prediction Models

a. 1985 Healy models

The use of the discretionary accrual model was pioneered by Healy (1985). Healy used total accruals as a proxy for discretionary accruals

$$= \frac{ДCa\ it\ -\ ДCI\ it\ -\ ДCash\ it\ -\ ДSTD\ it\ -\ Dep\ it}{A\ it-1}$$

b. De Angelo 1986 model

The De Angelo model predicts non-discretionary accruals by using the ratio of total accruals before the observation period (TA t-1) compared to the difference in total assets (A t-2). So the De Angelo model for non-discretionary accruals is:

$$\frac{TA\ t-1}{A\ t-1}$$

Jones 1991 model

This model was first developed by Jones (1991) and is the most widely used in research with the accrual-aggregate approach. This model follows the suggestion from Kaplans (1985), which states that accruals are the result of management discretion and originate from changes in the company's economic conditions. The model relates total accruals with changes in sales, gross assets, and fixed assets:

$$\frac{TA\ it}{A\ it\text{-}1} = \alpha 1\ \frac{(1)}{A_{it\text{-}1}} + \beta 1\ \frac{(\text{ДREV}\ it)}{A\ it\text{-}1} + \beta 2\ \frac{(PPE\ it) + e\ i}{A\ it\text{-}1}$$

And *discretionary accrual* measure with

$$DACC\ it = \frac{TA\ it}{A\ it\text{-}1} - \left\{ \alpha 1\ \frac{(1)}{A\ it\text{-}1} + \beta 1\ \frac{(\text{ДREV}\ it)}{A\ it\text{-}1} + \beta 2\ \frac{(PPE\ it)}{A\ it\text{-}1} \right\}$$

The Jones 1991 model is based on two assumptions:

1. The first assumption is that the current accrual (change in estimated working capital) resulting from changes in the company's economic environment is associated with changes or sales growth during the first equation estimated with a variable that is deflated by slowing growth in assets and sales.

2. The second assumption is that the gross value of assets controlling total accruals is associated with non-discretionary depreciation expense.

c. Modified Jones Models

Dechow et al., (1995) tested various alternative accrual models and they stated that the modified Jones model was the best model for testing earnings management. Jones's modification model is as follows:

Good Corporate Governance

Syakarosa (2002) defines good corporate governance as a system used by the board to direct and control and supervise the management of organizational resources in an efficient, effective, economical, and productive (E3P) manner with the principles of transparency, accountability, responsibility, independence and fairness to achieve organizational goals and with the existence of an independent board of commissioners, independent audit committee, institutional ownership structure by the majority, minority as well as managerial and the public.

The board of commissioners has a very important role in managing the company, especially in monitoring top management (Fama and Jansen, 1983). The board of commissioners is seen as a center for effective agency problem-solving between managers and shareholders (Fama and Jensen, 1983 as stated in Pratana, 2002). The proportion of the board of commissioners must be such that it enables effective, precise, and fast decision-making and can act independently. In the context of implementing good corporate governance, listed companies are required to have a board of independent commissioners whose number is proportional to the number of shares owned by non-controlling shareholders provided that the number of independent commissioners is at least 30% of the total number of commissioners.

The definition of an audit committee is a group of people selected by a larger group, to do certain work or to perform special tasks. The benefits of the audit committee which was formed as a company special committee to optimize the oversight function which was previously the full responsibility of the board of commissioners. The audit committee is at least owned by a company with a total of 3 (three) people who are supervised by at least 30% of the board of commissioners for good corporate management.

The close relationship between the audit committee and the board of commissioners is also evident in the reporting obligations of the audit committee. The audit committee is responsible to the board of commissioners for the implementation of the assigned tasks and is required to make a report to the board of commissioners for each use given.

Audit Quality

Audit quality is the quality of audit work carried out by the auditor by adhering to or guided by the professional standards of public accountants (SPAP) consisting of general standards (3 standard items), fieldwork standards (3 standard points), and reporting standards (4 standard points).
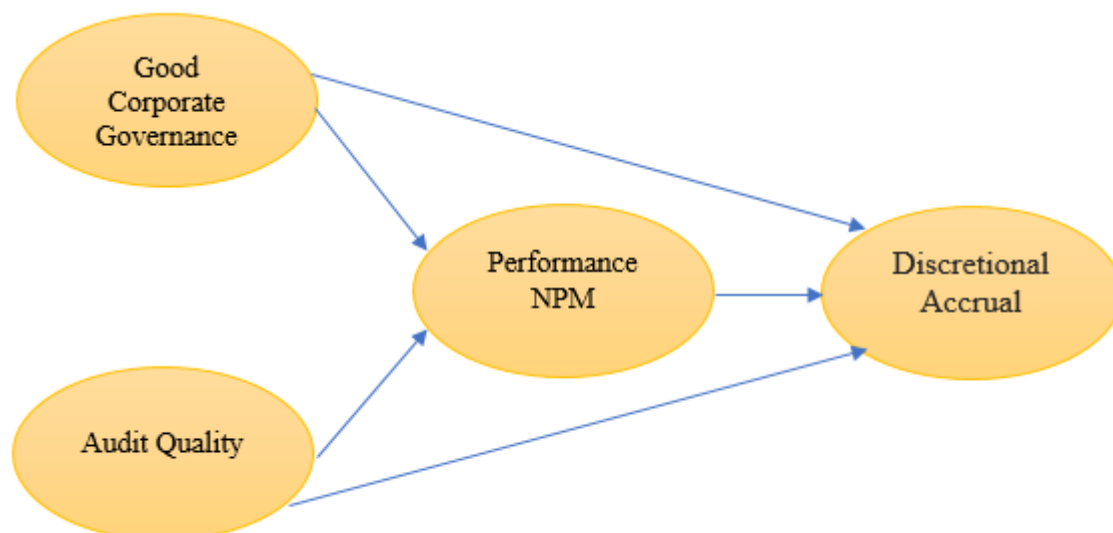
The Conceptual Framework

Figure 1. Concept Research Model

$Y1 = a + b\,X_1 + b\,X_2 + e$

$Y2 = a + b\,Y_1 + e$

The hypothesis is:

H1: GCG has a significant effect on the performance of NPM

H2: Audit quality has a significant effect on performance NPM

H3: GCG has a significant effect on earnings management (Discretional Accrual)

H4: Audit quality has a significant effect on earnings management (Discretional Accrual)

H5: Performance NPM has a significant effect on earnings management (Discretional Accrual)

H6: GCG has a significant effect on earnings management (Discretional Accrual) through performance NPM

H7: Audit quality affects earnings management (Discretional Accrual) through performance NPM

Research Method

This type of research is applied to quantitative research that implements and explains the effect of GCG and audit quality on earnings management and company performance as a mediating variable for various industrial companies in Indonesia in 2017-2022 on the Indonesian stock exchange. This study used a population of 30 various industrial companies listed on the IDX for 2015-2022, with a sample of 240 various industrial companies which were taken by purposive sampling. This study uses secondary data and is collected through documentation from audited financial reports of companies on the Indonesian stock exchange from 2015-2022. The data processing and data analysis method used in this research is partial lease square (PLS).

Results and Discussion

Hypothesis Testing (Path Analysis)

A causal relationship is declared insignificant if the critical ratio (C.R.) is between -1.96 and 1.96 with a significance level of 0.05. With the help of the PLS program application, the results of the estimated value of the structural model Critical Ratio are obtained. In summary, the results of calculating these coefficients are presented in the following table:

Table 1. Result Analysis SEM-PLS

The influence between latent variable			H	Track coefficients	t-value	p-value	Description
Cause Variable	**-->**	**Consequences Var.**					
Good Corporate Governance (X1)	-->	Performance NPM (Y1)	H_1	0,259	4,194	0,000	H_1 accepted
Audit Quality (X2)	-->	PerformanceNPM (Y1)	H_2	0,173	5,623	0,000	H_2 accepted
Good Corporate Governance (X1)	-->	Discretional Accrual (Y2)	H_3	0,188	2,615	0,009	H_3 accepted
Audit Quality (X2)	-->	Discretional Accrual (Y2)	H_4	0,132	2,284	0,023	H_4 accepted
Performance NPM (Y1)	-->	Discretional Accrual (Y2)	H_5	0,512	6,192	0,000	H_5 accepted

It is known that the Good Corporate Governance variable (X1) has a positive influence on NPM Performance (Y1), meaning that the higher the Good Corporate Governance (X1), the result will be an increase in the NPM Performance variable (Y1), where the Path coefficient obtained is 0.259 with a t-value of 4.194. Because the t-value is greater than the critical value (4.194>1.96), the statistical hypothesis states that H1 is accepted, meaning that the Good Corporate Governance variable (X1) has a significant influence on the NPM Performance variable (Y1).

It is known that the Audit Quality variable (X2) has a positive influence on NPM Performance (Y1), meaning that the higher the Audit Quality (X2), the result will be an increase in the NPM Performance variable (Y1), where the Path coefficient obtained is 0.173 with a t-value of 5.623. Because the t-value is greater than the critical value (5.623>1.96), the statistical hypothesis states that H2 is accepted, meaning that the Audit Quality variable (X2) has a significant influence on the NPM Performance variable (Y1).

It is known that the Good Corporate Governance variable (X1) has a positive influence on Discretional Accrual (Y2), meaning that the higher the Good Corporate Governance (X1) the result will be increasing in the Discretional Accrual variable (Y2), where the Path coefficient obtained is 0.188 with a t-value of 2.615. Because the t-value is greater than the critical value (2.615>1.96), the statistical hypothesis states that H3 is accepted, meaning that the Good Corporate Governance variable (X1) has a significant influence on the Discretional Accrual variable (Y2).

It is known that the variable Audit Quality (X2) has a positive influence on Discretional Accrual (Y2), meaning that the higher the Audit Quality (X2), the result will be an increase in the Discretional Accrual variable (Y2), where the Path coefficient obtained is 0.132 with a t-value of 2.284. Because the t-value is greater than the critical value (2.284>1.96), the statistical hypothesis states that H4 is accepted, meaning that the Audit Quality variable (X2) has a significant influence on the Discretional Accrual variable (Y2).

It is known that the NPM Performance variable (Y1) has a positive influence on Discretional Accrual (Y2), meaning that the higher the NPM Performance (Y1), the result will increase the Discretional Accrual variable (Y2), where the Path coefficient obtained is 0.512 with a t-value of 6.192. Because the t-value is greater than the critical value (6.192>1.96), the

statistical hypothesis states that H5 is accepted, meaning that the NPM Performance variable (Y1) has a significant influence on the Discretional Accrual variable (Y2).

The path coefficients in the structural model and the factor weight values of the manifest variables in the measurement model can be illustrated through the following path diagrams of the measurement model and structural model.
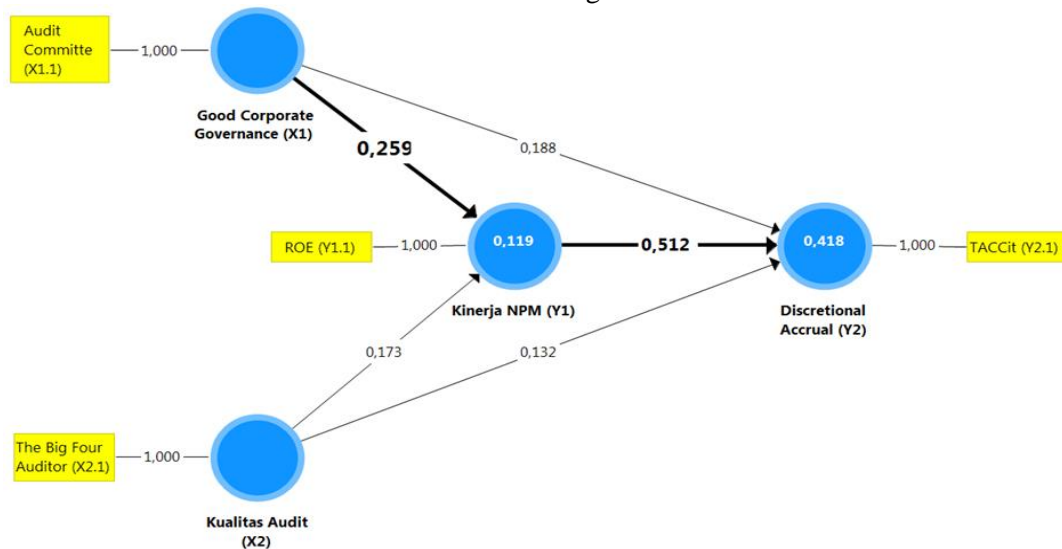
Figure 2. Path Diagram Model Measurement and Structural Model (Overall)

Table 2. Indirect Influence Between Latent Variables

Indirect influence	Count	Results	t-count	p-value	Description
Good Corporate Governance (X1) on Discretional Accrual (Y2) through Performance NPM (Y1)	0,259 x 0,512	0,133	2,584	0,010	Significant
Audit quality (X2) on Discretional Accrual (Y2) through Performance NPM (Y1)	0,173 x 0,512	0,089	3,475	0,001	Significant

Based on the table above, it can be seen that the effect of the latent variable indirectly on the intended latent variable is as follows:

1. The indirect effect of Good Corporate Governance (X1) on Discretional Accrual (Y2) through NPM Performance (Y1) is 0.1326 with a t value of 2.584>1.96 (Significant).
2. The indirect effect of Audit Quality (X2) on Discretional Accrual (Y2) through NPM Performance (Y1) is 0.0886 with a t value of 3.475 > 1.96 (Significant).

From these results, it can be concluded that the mediating variable, namely NPM Performance (Y1) is declared capable of mediating the influence of Good Corporate Governance (X1) and Audit Quality (X2) on Discretional Accrual (Y2).

Evaluation of the Structural Model (Inner Model)

To strengthen scientific ideas from the results of the synthesis of several theories in the formation of structural equations holistically (whole) it is necessary to evaluate the Structural Model (Inner Model). In this section, the evaluation is carried out by estimating the coefficient of determination (R^2) and the total coefficient of determination (R^2).

Table 3. Total Coefficient of Determination (R^2).

Influence			R Square	Determination
Good Corporate Governance (X1)	-->	NPM Performance (Y1)	0,119	11,90%
Audit Quality (X2)	-->			
Good Corporate Governance (X1)	-->	Discretional Accrual (Y2)	0,418	41,80%
Audit Quality (X2)	-->			
NPM Performance Y1)	-->			

The coefficient of determination (R-square) obtained from the Good Corporate Governance (X1) and Audit Quality (X2) models on NPM Performance (Y1) is 0.119, so it can be explained that the accuracy of Good Corporate Governance (X1) and Audit Quality (X2) measurements on NPM Performance (Y1) of 11.9% and the remaining 88.1 is influenced by other variables outside the research.

The coefficient of determination (R-square) obtained from the Good Corporate Governance model (X1), Audit Quality (X2), and NPM Performance (Y1) on Discretional Accruals (Y2) is 0.418, so it can be explained that the accuracy of Good Corporate Governance (X1) measurements, Audit Quality (X2), NPM Performance (Y1) and Discretional Accruals (Y2) of 41.8% and the remaining 58.2 is influenced by other variables outside the research. The goodness of fit model test was carried out using the total coefficient of determination (Q2), where the test results can explain how much the path model formed can represent the observed data.

The total determination coefficient value ranges from 0.0 to 100.0%, where the higher the total determination coefficient value, the higher the path model can represent the observed data. The results of the calculation of the total determination coefficient are as follows.

Total Determination Coef$=1-(1- 〚R\_1〛 ^2)\times(1- 〚R\_2〛 ^2)$

Total Determination Coef$=1-(1-0.119)\times(1-0.418) = 0.487$

The Total Determination Coefficient (Q2) obtained from the SEM-PLS model is 0.487, which means that 48.7% of the data can be explained by the SEM-PLS model which is formed as a whole (holistic), while the remaining 51.3% is explained by other factors/variables outside of this study.

Research Variable Descriptive Analysis

Table 4. Deskriptif Research Variable

Variable	Minimum	Maximum	Average	Std. Deviation
Good Corporate Governance (X1)	0	1	0,716	0,452
Audit Quality (X2)	0	1	0,569	0,496
NPM Performance (Y1)	-112,21	186,48	1,669	21,83
Discretional Accrual (Y2)	-3,87	2,22	-0,104	0,729

Based on the table above, it can be seen the description of the research variables based on the size of the data concentration (Central Tendency). In the Good Corporate Governance Variable (X1) it is known that the Minimum value is 0, the Maximum value is 1, the Average value (Mean) is 0.716, and the Standard Deviation value is 0.452. In the Audit Quality Variable (X2) it is known that the Minimum value is 0, the Maximum value is 1, the Average value (Mean) is 0.569, and the Standard Deviation value is 0.496. In the NPM Performance Variable (Y1) it is known that the Minimum value is -112.21, the Maximum value is 186.48, the Average value (Mean) is 1.669, and the Standard Deviation value is 21.83. In the Discretional Accrual Variable (Y2), it is known that the Minimum value is -3.87, the Maximum value is 2.22, the Average value (Mean) is -0.104, the Standard Deviation value is 0.729

Discussion

This study discusses the effect of good corporate governance as a proxy for audit committees and audit quality as a proxy for audits conducted by the big four auditors, its effect on earnings management, and performance as a moderating variable. The results of the inanalysis show a significant effect of the audit committee and audit quality on earnings management with performance as a moderating variable. The moderating variable is successful as a moderating variable that influences audit committees and audit quality on earnings management. With the existence of an audit committee that appoints auditors to carry out audits, and with most of the auditors being the big four, in this case, it can reduce the existence of earnings management carried out by managers. The earnings management that users of financial statements want is to equalize profits so instead of increasing or decreasing profits, even profits will make financial reports more ideal. And the performance of an average net profit margin which tends to increase will also affect investors to be happier to invest their funds in the company, because of its good performance. This research supports research from Aryanti (2017), Maharani (2018), Septiyani (2018), Darmawan (2019), Wahyuningsih (2020), Anggun Putri Wibowo (2021), and Himawan (2022).

Conclusion

The conclusion from this study is that there is a significant influence from the audit committee on earnings management. There is a significant influence of audit quality on earnings management. And performance is successful as a moderating variable that influences audit committees and audit quality on earnings management. This study implies that performance variables can strengthen the influence of audit committees and audit quality on earnings management.

The limitations of this study are only on the audit committee and audit quality on earnings management with performance as a mediating variable in Aneka Industries companies with a sample of 150 companies in 2017-2022. For future research to add variables that can affect earnings management in companies listed on the Indonesian stock exchange.

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