

Strategies to Reduce Earnings Management: The Role of Leverage, Profitability and Company Size

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Abstract

This research was conducted to determine the test results on the effect of financial performance in the form of leverage, profitability and company size on earnings management with a focus on all sub-sectors of holding and investment companies listed on the Indonesia Stock Exchange (IDX) for the period 2019-2022. The financial statements of a company are the data used in this study. This research is important because earnings management has a negative impact that can lead to bankruptcy for an entity, so it needs to be considered in order to prevent and minimize the impact that occurs. The findings presented in this research are based on the results of multiple linear regression tests which state that (1) leverage significantly has a positive effect on earnings management; (2) profitability has a negative and significant effect on earnings management; and further findings state (3) company size has a negative and significant effect on earnings management. The results obtained in this research are a form of empirical confirmation of the importance of taking action to minimize earnings management practices for the sustainability of the company in the future. The novelty of this research is in the object of research, namely the holding and investment company sub-sector.

Keywords: Leverage, Profitability, Company Size, Earnings Management.



INTRODUCTION

Information related to profit serves as an indicator of assessment of the effectiveness of management performance in achieving the intended success, this is in accordance with Statement of Financial Accounting Concepts (SFAC) No. 1. Investors will use profit and loss information in the financial statements to assess the evaluation of the company's performance for risk or uncertainty in the acquisition of cash flow (Irawan, 2021); because of this, with the aim of showing good company performance, managers will choose the appropriate accounting method when preparing financial statements (Utari & Sari, 2016). Accounting techniques that are often considered related to the manager's efforts to intervene in the preparation of financial statements with the aim of benefiting certain parties are known as earnings management (Dewi, 2014). Earnings management practices are very important to pay attention to because earnings management is often associated with manager behavior in presenting financial reports as an achievement of management performance (Sari et al., 2021); Earnings management is seen as being able to reduce the value of information contained in financial reports as a medium of communication between investors, shareholders and the public (Sari & Khafid, 2020); earnings manipulation usually occurs frequently for various reasons, including efforts to increase compensation, avoid liabilities, meet analyst expectations and have an impact on stock prices (Andawiyah & Furqani, 2016). If earnings management is not detected, the impact will be very bad for the cash flow and future of the entity (Robik et al., 2022); The practice of earnings management is very detrimental to external parties because it can affect external parties' errors in decision making, this occurs because of the asymmetry of information contained in the financial statements (Apriadi et al., 2022).

The phenomenon of earnings management is something that is rampant in entities in Indonesia. One of the cases occurred when the first quarter 2018 performance of PT Astra International Tbk (ASII) was announced. The increase in revenue obtained by PT ASII in 2018 exceeded revenue in 2017 in the same period of three months. However, the net profit was lower compared to the first quarter of 2017. Quoted from the company's financial statements, PT ASII's net income reached Rp 55.82 trillion, showing an increase of 14.43% compared to net income in the first quarter of 2017 which only amounted to Rp 48.78 trillion (cnbcindonesia.com). As for other cases that occurred in 2020, the BPK found window dressing at PT Jiwasraya and findings regarding the recording of false profits over the years. BPK announced that the potential state losses due to the case reached 16.81 trillion (ekonomi.republika.co.id).



Research related to the effect of leverage, profitability and company size on earnings management has been conducted by several researchers with conflicting results. The level of company leverage is considered to have no influence on earnings management stated by (Safitri & Triyonowati, 2015) & (Astria et al., 2021) in the research they have conducted, while other results are obtained from the results of research conducted by (Khairani et al., 2022) showed that leverage has a negative effect on earnings management and (Mariam et al., 2021); (Rosady & Abidin, 2019); (Astuti et al., 2017) in his research states the finding that leverage has a positive influence on earnings management. (Khairani et al., 2022); (Mariam et al., 2021); (Siringoringo & Sijabatb, 2023); (Astria et al., 2021) state that profitability has a positive effect on earnings management, while the findings that profitability has a negative effect on earnings management are stated by (Safitri & Triyonowati, 2015), then in research (Safitri & Triyonowati, 2015); (Santika & Herwiyanti, 2020) presents the results that profitability has no effect on earnings management. As for company size, (Joe & Ginting, 2022); dan (Nalarreason et al., 2019) put forward findings in the form of company size having a positive influence on earnings management, while (Safitri & Triyonowati, 2015); (Utami & Handayani, 2019) state the findings that company size has a negative effect on earnings management practices, the opposite results are presented in research conducted by (Astuti et al., 2017), (Astria et al., 2021) & (Rosady & Abidin, 2019); (Siringoringo & Sijabatb, 2023) with the finding that company size has no effect on earnings management.

The novelty in this research that distinguishes it from previous research lies in the object of the research, namely, the Holding and Investment Company Sub-Sector. Anjarningsih et al. (2022) in his research using BUMN companies as research objects; Khairani et al (2022), Astria et al. (2021); & Rosady & Abidin, (2019) make manufacturing companies as the object of their research; while research that uses the object of the company after mergers & acquisitions (Putri, 2023); Safitri & Triyonowati (2015) and (Astuti et al., 2017) using banking companies as the object of their research; and (Septiyani & Aminah, 2023) used insurance companies in their research. In addition to the above reviews, the holding and investment company sub-sector is a new classification on the IDX since January 25, 2021 which is part of the financial sector. The financial sector itself is one of the sectors that is considered to have an influence on regional economic growth (Supartoyo et al., 2018). These things are then a consideration for the author to make the holding and investment company sub-sector the object of this research.



The main objective of this research is to determine the test results of the effect of leverage, profitability and company size on earnings management. In addition, it is hoped that this research can contribute in the field of literacy as insight and knowledge regarding earnings management, especially in the sub-sector of holding and investment companies in Indonesia.

LITERATURE REVIEW

Agency Theory

The fundamental theory that underlies this research is agency theory, which is in line with issues related to the supervisory system such as the opinion of Jensen & Meckling (1976) which suggests a relationship between the principal and the agent and hands over authority to decision making. Yusnita (2022) said that the discussion of earnings management cannot be separated from agency theory. The assumption of this theory states that each party, both the agent and the principal, tends to prioritize personal interests so that it can trigger a conflict of interest between the two parties (Bilqis & Rusdan, 2011). The conflict of interest between each party will lead to information asymmetry when the management (agent) has more information than the investor (principal). When the company is experiencing a decline in profits or even losses, the information asymmetry will be utilized by management to manipulate the numbers in the financial statements. In understanding earnings management actions, agency theory is the theory that underlies this practice.

Earnings Management

Agency theory states that the cause of earnings management actions is due to the emergence of different interests that occur in each party. This occurs when management uses opportunistic actions to increase its utility by utilizing information that is not known by the shareholders (Oktyawati et al., 2023). Earnings management can be interpreted as an intervention in the presentation of financial statements carried out by company management with the aim of deceiving investors on information related to the condition and quality of the company's performance (Cantika & Jin, 2020). According to Aminah & Gunakan (2015) earnings management is the behavior of managers in maximizing, minimizing and smoothing earnings in a company. Earnings management actions fall into the category of fraud because company management consciously presents false information related to the company's financial condition with the aim of deceiving stakeholders (Astuti et al., 2017). Based on this explanation, earnings management can

64



be defined as a deliberate and systematic managerial strategy with the aim of influencing earnings figures through the selective application of certain accounting policies for certain stakeholders. Earnings management can also be concluded as the behavior of management's efforts to reduce, increase or flatten company profits according to the manager's wishes. This action is very detrimental to stakeholders in decision making because the earnings information obtained is not a true picture of the company's condition. Earnings management practices have been proven to reduce the credibility of the company's financial statements as an indicator in determining decisions (Fadjrih Asyik, 2016). The inaccuracy of numbers as information from financial statements is of course very detrimental to external parties because it can risk errors in decision making (Apriadi et al., 2022). In addition, Yusnita (2023) said that when earnings management actions occur, managers will tend to violate government regulations such as laws related to taxation.

Scott (2012: 423) divides earnings management patterns into four different categories, namely: 1). Taking a bath; 2). Efforts to minimize profits (income minimization); 3). Efforts to maximize profits (income maximization); and 4). Income smoothing efforts. Meanwhile, the earnings management mechanism according to Subramanyam (2010: 133) is divided into two methods, namely 1). Transferring profits from one period to another, by accelerating or delaying recognition of income or expenses; and 2). Performing earnings management by classifying certain expenses contained in the income statement. In general, Sulistyanto (2008: 160) identifies that there are three approaches that can be used in detecting earnings, these approaches are 1). Aggregate Accrual; 2). Specific Accrual; and 3). Distribution of Earning After Management.

Leverage

The effectiveness of the use of resources such as receivables, capital or company assets can usually be measured using the leverage ratio (Astuti & Aminah, 2023). Heripson (2016) states that the function of leverage is as a guarantee by measuring the company's ability to fulfill its obligations in the event of dissolution and shows the extent to which outsiders (creditors) contribute to company financing. Another view of leverage says that leverage is used as a ratio measuring the level of company assets financed by debt (Kasmir, 2016). Leverage provides an overview of the company's effectiveness in utilizing external debt to finance operations and expansion or it can also be said that leverage is a company performance booster that is identical to debt (Soedarso & Arika,

65



2018). When the company's debt increases compared to its assets, the risk of the company's inability to fulfill its obligations will also increase. A high leverage ratio is an indication for the company of greater dependence on outsiders. This is a pressure for companies to carry out effective financial management to prevent a spike in the leverage ratio and results in the tendency of management to manipulate earnings. Measurement of leverage consists of several ratios, namely the debt to asset ratio (DAR), debt to equity ratio (DER), Long Term Debt to Equity Ratio, Tangible Assets Debt Coverage (TADC) and Times Interest Earned Ratio (TIE) (Purba, 2019).

Profitability

Profitability shows the company's capacity to generate profits and is an indicator of the level of success of an entity's management (Lestari & Wulandari, 2019). Purba (2019) said that profitability is an indicator used in assessing the company's proficiency and evaluating how well the company uses its resources, be it capital, assets or sales in generating profits. Another perspective indicates that profitability can be used as a parameter to evaluate the capability of the entity in generating profits (Kasmir, 2016), the high level of profitability is an illustration of a good ability to generate profits for the company. In general, the figure presented in profitability is a comparison between profit and the use of assets in an effort to generate profits, it can also be said that profitability is a measure of an entity's ability to make a profit in a certain period (Indrayenti & Jenny, 2018). Often shareholders make profitability a measuring tool in assessing the effectiveness of a company, this assessment will later be used to determine investment decisions (Santika & Herwiyanti, 2020). The assessment of profitability as an indicator of measuring the effectiveness of an entity's performance is a trigger for managers to intervene in financial reports with the aim of increasing income figures so that the assessment of the entity's performance is seen as good and convincing for stakeholders. Profitability can be assessed in several ways, depending on the comparison between profit and assets or capital with others. Brigham & Houston (2010) say that profitability can be calculated through Net Profit Margin; Return On Assets; Return On Equity; and Basic Earning Power.

Company Size

Entity classification can be categorized based on its size, which includes large size and small size. According to Malau & Parhusip (2016), The company size scale is able to categorize the size of a company through several benchmarks, such as total assets, log



size, stock market value, and so on. Company size is a measure that is calculated based on the size of the total assets or wealth of the company using the measurement of the logarithmic value of total assets (Lala Latifatul et al., 2023). A company is considered to have a large size if the company shows a high level of sales, high stability of the entity, is involved with many stakeholders and its decision-making procedures have a major impact on the public domain. In general, larger companies tend to have more complicated operational activities compared to smaller companies. The size of a company is often measured by total assets, which is defined by Kieso (2011) as resources under the control of a company that originate from past events and are expected to generate future economic benefits for the entity. Company size will also display the value of a company's performance in front of investors. Company size is also considered to have an influence in fulfilling investor or shareholder expectations because company size affects the company's funding structure. Investors tend to choose companies with good performance in order to benefit from the investment made, this tendency can then trigger earnings management actions by managers.

Leverage and Earnings Management

Leverage is considered a factor that is thought to have an influence on earnings management practices. Braindies & Fuad (2019) argue that the high level of leverage has an impact on the high potential for earnings intervention actions, this occurs because of the management's desire to get high profits even with a high level of debt with the aim of being seen as good at managing and utilizing debt so that creditors / investors are willing to always flow funds to the company. Managers are often involved in cases of earnings manipulation by following a pattern of increasing profits that can be seen and aims to lure potential investors in order to get funding sources from external parties. An increase in the company's high debt compared to its assets will increase the company's vulnerability in fulfilling its obligations and on the investor's side, it tends to create a greater desire for the profit obtained. Entities with a high leverage value will tend to implement earnings management practices, especially when faced with pressure to meet obligations on time, as emphasized by Sujadi (2023). The high level of leverage is an indication of the company's increased dependence on external parties, especially creditors, and illustrates the amount of interest obligations that must be paid by the company. Therefore, it is important for companies to implement good financial management to avoid increasing the value of leverage, so as to prevent the tendency of management to practice earnings manipulation. In short, it can be concluded that a high leverage rate correlates with a



greater tendency for managerial involvement in earnings management actions (Arlita et al., 2019). Referring to the explanation above, the hypothesis formulated in this study is as follows:

H1 : Leverage has a positive effect on earnings management

Profitability and Earnings Management

Profitability is the net profit earned by an entity as a result of asset management. The value of profitability can be used as one of the benchmarks for measuring company performance (Lestari & Wulandari, 2019). Khairudin & Dewi (2015) also said that profitability is an indicator in measuring the success of an entity. In general, profitability provides an overview of a company's performance in generating profits, the high effectiveness of the company's performance in obtaining profits is attractive to shareholders to invest in the company (Tarmizi et al., 2018). The high level of profitability indicates the high performance and proficiency of the company in earning profits, this is certainly a concern for investors. The tendency of investors to highlight matters related to profit is a trigger for managerial parties to focus on benchmarks for assessing the effectiveness of company management in order to get a good view. In order to achieve this desire, management will try to present financial reports with high and stable profit figures, so that engineering actions often occur in the presentation of financial reports through earnings management (Tallane, 2020). Profitability and earnings management are interrelated, when the company gets a low profitability value, it will trigger earnings management behavior in the company. Akbar (2023) said that high profits will provide significant benefits for shareholders, which then triggers management to tend to be triggered to take earnings management actions when the level of profitability obtained by the company is low (Tiur, 2022). Referring to the explanation above, the hypothesis formulated in this research is as follows:

H2 : Profitability has a negative effect on earnings management

Company Size and Earnings Management

In general, entities with larger sizes will get more attention from various external parties such as investors, analysis, the public and also the government. This will cause the company to be more careful in presenting its financial statements. It is expected that the company always strives to maintain stable financial performance which of course will have an impact on the company's value (Rose et al., 2021). Large companies have a tendency to report their finances carefully, carefully and transparently because their



performance is in the public spotlight, so it is less likely for large companies to be involved in earnings manipulation. Conversely, smaller companies have a high risk tendency for earnings management actions, which of course are carried out with the aim of displaying satisfactory effectiveness of company performance (Sari & Susilowati, 2021). The assumption of human nature that tends to avoid risk also supports the statement on the negative effect of company size on earnings management. Referring to the description above, the formulation of the hypothesis in this study is as follows:

H3: Company size has a negative effect on earnings management

RESEARCH METHOD

This research is included in the category of causality research using a quantitative approach. The population studied consisted of all sub-sectors of holding and investment companies listed on the IDX with a time span of 2019-2022. Purposive sampling was chosen as the research sample collection method, which is a sample selection technique based on the similarity of characteristics and certain criteria, such as: (1) Sub-sector holding and investment companies listed on the Indonesia Stock Exchange (IDX) in 2019-2022; (2) Companies that submit financial reports consistently in the 2019- 2022 time span; (3) Companies that submit financial reports in rupiah currency; and (4) Companies that make profits consecutively from 2019 to 2022. The data used in this research is the company's financial statements. The following is a table explaining the variable measurements in this study:

Variables	Variable Measurement
Leverage (X1)	$DER = \frac{\text{Total Hutang}}{\text{Total Modal}} \times 100\%$ Debt to Equity Ratio (DER) shows the comparison value between total liabilities and total equity. This comparison was chosen because capital is a description of the entity's financial condition which leads to the value of the entity (Purba, 2019).



Profitability (X2)	$ROA = \frac{\text{Laba Bersih}}{\text{Total Asset}} \times 100\%$ Return On Asset (ROA) shows the efficiency of the use of company assets in obtaining profits (Kusumaningtyas & Dzulkirom, 2017).
Company Size (X3)	Size = Ln Total Asset The proxy for company size in this research is total assets which are transformed into logarithms as a measuring tool for company size because of their relatively large value (Wardani et al., 2018). The choice of total assets as a proxy in this study is due to its perceived stability.
Earnings Management (Y)	$DA_{it} = \frac{TA_{it}}{A_{it-1}} - NDA_{it}$ The modified Jones model based on Dechow et al. (1995) is used to calculate the value of discretionary accruals (DA) in the measurement of earnings management. Compared to other models, the Modified Jones Model provides the strongest test results on earnings management measurement compared to other models (Dechow et al., 1995: 223).

In this research, the analysis methods used are descriptive statistical tests, classical assumption testing and multiple linear regression. The regression equation



model used to test the effect of leverage, profitability and company size on earnings management can be represented as follows:

$$DA = \alpha + \beta_1 DER + \beta_2 ROA + \beta_3 LNA + \varepsilon$$

Where DA is a symbol of earnings management that uses Discretionary Accrual (DA) as its measurement; α as a symbol of the constant; β_1 DER as a symbol of the leverage regression coefficient; β_2 ROA as a symbol of the profitability regression coefficient; β_3 LNA as a symbol of the company size regression coefficient; and ε as a symbol of the error term.

RESULTS

The results of this study were obtained based on purposive sampling of all sub-sectors of holding and investment companies listed on the IDX with a research period of 4 consecutive years. Descriptive statistical tests conducted on 36 samples during the study period stated that earnings management as the dependent variable obtained a minimum value of -20.89, namely at PT Saratoga Investama Sedaya Tbk in 2020. Meanwhile, the analysis results obtained a maximum value of 5.24 obtained by PT Pasific Strategic Financial Tbk in 2021, this result indicates that companies tend to practice earnings management through a method called income increasing or increasing the value of earnings in that year.

Table 1. Descriptif Statistic					
Variables	N	Minimum	Maximum	Mean	Std. Deviation
Leverage	36	.0024	4.16	1.6338	1.2922
Profitability	36	.0004	.41	.0494	.0197
Company Size	36	26.93	32.40	30.0951	1.5631
Earnings Management	36	-20.89	5.24	-1.0296	1.0187
Valid N (listwise)	36				

Source: Data Processed, 2023



The level of leverage in this study uses DER measurement, namely the ratio between the company's total debt and the company's total capital, the results show that PT Buana Artha Anugerah Tbk in 2022 is the company with the lowest leverage level of 0.0024, which means that in its operations the company does not depend on debt because the total equity owned by the company in that year is much greater. The company with the highest leverage value of 4.16 obtained by PT Sinar Mas Multiartha Tbk in 2021, this figure shows that the company has a relatively high dependence on debt in operating the company. This is due to very little profit, while the value of the company's liabilities is much greater than the value of its equity in that year. The high level of leverage owned by companies like this will trigger manipulation of financial statements. The sample companies analyzed in this research have a mean leverage value of 1.6338 which reflects that the average leverage level in the sample companies is 163%. This indicates a high dependence on external funding sources so that the company is vulnerable to external pressure. In the profitability variable measured using ROA, the results show a minimum value of 0.0004, namely at PT Capital Financial Indonesia Tbk in 2019, meaning that the company only has the ability to earn a profit of 0.04%, this is because the revenue figure only has a small difference with the operating expenses owned, which has an impact on the small profit in that year and the maximum value of 0.41 obtained by PT Saratoga Investama Sedaya Tbk in 2021, which means that the highest level of profitability in the research sample is in that company. This happened because the company experienced an increase in securities income so that the company was able to earn a profit of 41%. In general, the average value of this variable is 0.0494, this figure indicates that the average level of the company's ability to generate profits in sample companies is 4.9%. The company size variable used in this study is the Natural Logarithm of the company's total assets. PT Buana Artha Anugerah Tbk is the smallest company in this study with a value of 26.93, while the maximum value of 32.40 is achieved by PT Sinar Mas Multiartha Tbk, which means that the company is the company with the largest size in this study. In general, the average company size in this research was recorded at 30.09. This numerical representation indicates that the companies included in the sample have a relatively large average size, as it is closer to the value of 32.40 (the maximum value of company size).

A series of classical assumption tests such as normality test, multicollinearity test, heterocollinearity test, autocorrelation test, and multiple linear regression have been conducted in this research. The results of the statistical tests are presented in the following table:

72



Table 2. Hypotesis

Variables	Coefficient	t-Statistic	Prob
Leverage	1.7050	2.1176	0.0420
Profitability	-2.0981	-4.0114	0.0000
Company Size	-1.3390	-2.1917	0.0357
Adjusted R-square	0.189772		
Prob F-statistic	0.0208529		

Source: Data Processed, 2023

The table above shows the results of the prob F-statistic value of 0.0208529 which means that the regression model used in this research is feasible to explain the effect of leverage, profitability and firm size on earnings management practices. The t-statistic value of leverage shows a tcount value $< t_{table}$, namely $2.118 < 3.622$ and a significance of $0.042 < 0.05$ which indicates that there is a significant positive effect of leverage on earnings management, so the hypothesis (H1) is "accepted". The profitability variable has a tcount value $< t_{table}$, namely $-4.011 < 3.622$ with a significance value of $0.000 < 0.05$, these results indicate that profitability has a negative and significant effect on earnings management, this explains that the higher the level of profitability, the weaker the earnings management practices, so the hypothesis (H2) "accepted". The company size variable has a tcount value $< t_{table}$, namely $-2.192 < 3.622$ with a significance value of $0.036 < 0.05$, it can be said that company size has a negative and significant effect on earnings management, which means that the level of earnings management will be low in companies with large sizes, so the hypothesis (H3) "accepted". The Adjusted R-Square number shows a value of 0.189772, this indicates that the dependent variable (earnings management) can be influenced by the independent variables in the model (leverage, profitability and company size) by 18.9%, while the remaining 81.1% is influenced by other variables that are not tested within the scope of this research.



DISCUSSION

Leverage and Earnings Management

The findings obtained from hypothesis testing indicate a significant positive effect between leverage and earnings management. This implies that when the leverage level of an entity increases, there will simultaneously be an increased tendency for earnings management actions. Entities with high liability values tend to practice earnings management. The increasing tendency towards earnings management practices stems from the value of liabilities that is higher than the equity owned, indicating a dependence on loans from external parties to carry out company operations. Thus, the company will try to present financial reports that look good with the aim of attracting investors to invest in the company. This effort to beautify the company's financial statements is usually done by manipulating the profit figures in the financial statements. The findings in this study are in line with research conducted by (Mariam et al., 2021); (Rosady & Abidin, 2019); (Astuti et al., 2017) which states that leverage has a significant positive effect on earnings management. However, this research is not in line with the results presented by (Safitri & Triyonowati, 2015); (Astria et al., 2021); (Khairani et al., 2022) with findings that reveal the absence of leverage's effect on earnings management. The findings of this research can be said to be a form of confirmation of statements related to Agency Theory which considers that leverage plays an important role in explaining the interests of managers and shareholders (Hanafi, 2020). Jensen & Meckling (1976) stated that the relationship between the principal and the agent is in the form of granting authority by the principal to the agent to make decisions on behalf of the principal. This theory assumes that the granting of authority by the principal to the agent can lead to information asymmetry which triggers conflicts due to each party prioritizing their personal interests. The company management (agent) certainly has more information related to the company including the company's leverage value, because of the desire to get a good view of its performance, the management will try to present good financial reports by manipulating profits.

Profitability and Earnings Management

The findings of the hypothesis test indicate a negative and significant relationship between profitability and earnings management. This shows that the tendency to manipulate earnings figures decreases when the entity obtains a high profitability value, and vice versa, if the company's profitability value is low, the level of earnings manipulation practices in the company's financial statements will increase. This is due to the tendency of investors who want companies with high profitability values, so

74



companies will try to provide good performance in generating profits. Companies with low profitability tend to practice earnings manipulation with the aim of attracting investors by presenting good profitability. Meanwhile, companies that have obtained high profitability will certainly no longer manipulate their financial statements. This study states results that are in line with research conducted by (Safitri & Triyonowati, 2015) with the results of profitability having a negative and significant effect on earnings management. However, this research is not in line with the results found by research (Khairani et al., 2022); (Mariam et al., 2021); (Siringoringo & Sijabatb, 2023); (Astria et al., 2021) which shows that profitability has a positive effect on earnings management and research by (Safitri & Triyonowati, 2015); (Santika & Herwiyanti, 2020) which states that profitability has no effect on earnings management. This finding also confirms the assumption of agency theory which states that shareholders who act as principals are considered to have a sole interest in the growth of their investment in the company or financial returns. This means that investors tend to be more concerned with a high level of profitability, because this tendency is the trigger for managers to intervene in earnings when the company gets a low profitability value.

Company Size and Earnings Management

The findings of hypothesis testing show evidence that company size has a significant negative relationship with earnings management. This indicates that the larger the size of the company, the possibility of earnings management actions will decrease. Conversely, if the company has a smaller size, the possibility of manipulation will be greater. This tendency occurs because companies with large sizes are considered less at risk of earnings management because the company's reputation in general attracts public attention and external parties, so the company has a lot of pressure to be transparent in the presentation of financial statements. Different things happen to smaller entities, small companies have a tendency to manipulate earnings in order to obtain a good assessment of their performance which aims to attract the attention of investors so that they are willing to invest in the company. The results obtained from this research are in line with research conducted by (Safitri & Triyonowati, 2015); (Utami & Handayani, 2019) which suggests the result that company size has a significant negative effect on earnings management. However, this research contradicts the findings (Joe & Ginting, 2022); (Nalarreason et al., 2019) which reveals a positive effect of company size on earnings management actions and the results of research by (Astuti et al., 2017), (Astria et al., 2021) & (Rosady & Abidin, 2019); (Siringoringo & Sijabatb, 2023) suggest the

75



finding that there is no effect of company size on earnings management. The findings in this study confirm the disclosure by Eisenhardt (1989) categorizes human nature in agency theory into three assumptions, one of which is the assumption regarding the human tendency to always avoid risk (risk aversion). The spotlight or more attention from external parties to large-sized companies certainly poses a risk in the form of a bad image for company management if fraud is found in the presentation of financial statements, so the company will present the financial statements as they are. This assumption then becomes the basis for the negative effect of company size on earnings management practices.

CONCLUSIONS

This research focuses on testing the effect of financial performance, which involves leverage, profitability and firm size on earnings management practices. The findings of this study state that: (1) Significantly, leverage has a positive effect on earnings management; (2) Significantly, profitability has a negative effect on earnings management practices; (3) Significantly, firm size has a negative effect on earnings management practices. This research shows that it is important for companies to minimize the occurrence of earnings manipulation because it can lead to errors in decision making which results in losses for interested parties. Earnings management practices can be minimized by improving financial management as well as managing and supervising the company's financial management so that the assets owned can be used optimally in the company's operational activities so that the company does not rely too much on debt from external parties. The limitation of this study lies in the lack of population because it only covers one sub-sector company with a relatively short period span of less than 5 years. In addition, only 18.9% of the dependent variable can be explained by the independent variable. Recommendations for further research to increase the scope of the research population and add additional independent variables can provide an explanation for their influence on earnings management practices.

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