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EFFECT OF FAMILY OWNERSHIP IN THE RELATIONSHIP BETWEEN CORPORATE GOVERNANCE MECHANISM AND EARNING MANAGEMENT

PENGARUH KEPEMILIKAN KELUARGA DALAM HUBUNGAN MEKANISME TATA KELOLA PERUSAHAAN DAN MANAJEMEN LABA

Zirman[1], Fitri Humairoh[2], Vera Oktari[3], Jonnius[4]
Fakultas Ekonomi dan Bisnis, Universitas Riau[1,2,3]
Fakultas Syari'ah dan Hukum, Universitas Islam Negri Sultan Syarif Kasim[4]
mailto:zirman@lecturer.unri.ac.id[3]

ABSTRACT
Financial statements are the basis for many parties' decision-making in describing the condition of a company, so companies must present the quality of the information therein. This study examines the relationship between corporate governance mechanisms and earning management and how family ownership influences this relationship. This empirical study uses companies on the Kompas 100 index from 2015 to 2019 to be tested using Generalized Least Squares(GLS). This study finds that the board of commissioners affects earnings management, and family ownership strengthens the role of the board of commissioners in suppressing earnings management. This study strengthens the literature on family ownership in companies. Internal auditors can consider the implication of increasing the effectiveness of internal audits to produce more accurate quality financial reports. In addition, the implications of this study also recommend restructuring the internal audit function, especially its role in management and governance, to be more objective and also impartial.
Keywords: *Audit Committee, Board of Commissioner, Corporate Governance, Earning Management, Family Ownership, Financial Reporting Quality.*

ABSTRAK
Laporan keuangan menjadi dasar pengambilan keputusan bagi banyak pihak dalam menggambarkan kondisi suatu perusahaan, sehingga perusahaan harus dapat menyajikan informasi yang memiliki kualitas didalamnya. Penelitian ini bertujuan untuk mengkaji hubungan antara mekanisme tata kelola perusahaan dan manajemen laba serta bagaimana dampak kepemilikan keluarga dalam mempengaruhi hubungan tersebut. Studi empiris ini menggunakan perusahaan yang masuk dalam indeks Kompas 100 dari tahun 2015 hingga 2019 untuk diuji menggunakan metode pengujian *Generalized Least Squares* (GLS). Hasil pengujian data penelitian ini menemukan bahwa dewan komisaris berpengaruh terhadap manajemen laba, dan kepemilikan keluarga dapat memperkuat peran dewan komisaris dalam menekan manajemen laba. Studi ini memperkuat literatur tentang kepemilikan keluarga di perusahaan. Auditor internal juga dapat mempertimbangkan implikasi peningkatan efektivitas audit internal untuk menghasilkan laporan keuangan yang lebih akurat dan berkualitas. Selain itu, implikasi dari penelitian ini juga merekomendasikan restrukturisasi fungsi audit internal, khususnya perannya dalam manajemen dan tata kelola, agar lebih objektif dan tidak memihak.
Kata Kunci: Komite Audit, Dewan Komisaris, Tata Kelola Perusahaan, Manajemen Laba, Kepemilikan Keluarga, Kualitas Pelaporan Keuangan.

INTRODUCTION

The primary purpose of reporting is to offer helpful information to interested parties in financial reports. As a result of a cycle, financial reports are expected to provide quality information so that users can make accurate decisions. Information quality is also essential for directing achievement, increasing competitiveness, creating added value, and providing products and services that are beneficial to potential customers on an ongoing basis to improve company performance (Alshirah et al., 2020; Laudon et al., 2015; Pham et al., 2021; Tsoncheva, 2012). Therefore, the company's financial statements must be considered free from misstatement and reliable.

Many cases related to the low quality of financial reporting caused shocks to the world's financial and economic markets, such as Xerox and Worldcom in the US, Toshiba in Japan, Luckin Coffee TAL and the Education C group in China, as well as the Bach Tuyet Cotton Corporation, Bibica and Vien Dong Pharma JSC in Vietnam. In Indonesia alone, financial statement fraud is the third most detrimental (Association of Certified Fraud Examiners, 2018). The above cases cannot be separated from the manipulation of information carried out by management, who wants their performance to look good.

One way of manipulation by management is profit manipulation (earnings management). Wardani & Kusuma (2012) state that earnings management can negatively affect company profitability in the future, and this is done by opportunistic management. Soon (2012) also found that managers obtain more significant incentives for earnings management, such as income smoothing or increasing profits. From the several studies above, it can be concluded that earnings management is deliberately manipulated by management to achieve personal interests.

As a party that is fully responsible for the implementation of company supervision, the board of commissioners has an important role in overseeing company activities. With the board of commissioner's supervision of company management, it will be difficult for management to fulfil their personal interests so that conflicts of interest can be minimized (Fama & Jensen, 1983; Jensen & Meckling, 1976; McIntyre & Murphy, 2008). Hussain & Shah (2017) and Hasan & Butt (2009) states that governance mechanisms are very effective in increasing the accuracy of financial reports, even in the non-profit sector (Yetman & Yetman, 2011). In addition, the audit committee, as an extension of the board of commissioners in overseeing the management of the company, is also another factor in creating a good corporate governance mechanism (Rifani & Astuti, 2019).

Based on the fact that the potential for losses created by earnings management is still high, it is suspected that there is influence from other factors in the relationship between the governance mechanism and earnings management. From some of the results of previous research in this study, family ownership has a major influence on a business (Ahmad et al., 2020; Memili et al., 2018; Minh Ha et al., 2022). Ownership is one aspect of the control mechanism in corporate governance, and the topic of family ownership is currently an important issue considering the large influence of ownership in creating value and business performance.

This study aims to prove the influence of corporate governance mechanisms on earning management and moderation of family ownership in this relationship. This research contributes to filling the gap that exists in the results of previous research, which are still inconsistent, as well as adding to literacy and empirical evidence about the effect of family ownership on the quality of financial reports. In the next section, this research report will discuss theory and hypothesis development, followed by methodology, discussion of research results, and conclusions.

Agency theory has become an essential theoretical paradigm in management accounting in recent decades. The theory developed by Jensen and Meckling in 1976 develops a framework for understanding processes within companies from the perspective of principals and agents (Jensen & Meckling, 1976). Jensen (2000) defines an agency relationship as a contractual relationship where one person or party acts as a principal who employs one or more people who act as agents, according to their wishes, by delegating decision-making power to the agent. From this relationship, fundamental problems are created related to the agent's behaviour and desire to maximize his profit, which is very different from the principal's goal (Boučková, 2015).

Agency problems are stated to originate from an imbalance in the ownership of corporate information between principals and agents, which is known as information asymmetry. Information asymmetry arises when one party has more information than the other, which is used for personal gain (Jensen & Meckling, 1976). Information asymmetry leads to two specific problems of agency theory: the creation of moral hazard and adverse selection. A moral hazard is a condition in which one party exploits information asymmetry that occurs for personal gain, while adverse selection is created due to a lack of information (Boučková, 2015).

Several factors that can reduce the occurrence of problems between principals and agents are internal controls. Some previous research results show the importance of the internal audit function in companies (Herranz et al., 2022; Inaam & Khamoussi, 2016; Ismael & Roberts, 2018; Krishnan et al., 2020; Lois et al., 2020; Mihret, 2014; Saleh et al., 2007; Sun et al., 2014). Reasonable internal control serving consulting can produce effectiveness and efficiency in the company's overall goals to produce the rate of return on capital used (Mihret, 2014).

In addition to internal control, corporate governance is another factor needed to reduce agency problems and information asymmetry. In their research, Ismael & Roberts (2018) stated that agency problems between management and owners and the audit committee's effectiveness affect the internal audit function. As the executor of internal control, the audit committee is one of the essential mechanisms in corporate governance. It is recognized that its function is to suppress earnings management within the company (Inaam & Khamoussi, 2016; Mardjono et al., 2020; Mohd Saleh et al., 2007). Another governance mechanism that can reduce agency problems is the board of commissioners. The board of commissioners has the role of supervising the management of the company carried out by management. Mardjono et al. (2020) state that the effectiveness of the monitoring function carried out by independent commissioners can reduce agency costs because management prioritizes achieving the owner's wishes by maximizing company resources.

The Board of Commissioners (BoC) is a crucial governance mechanism in exercising control over agency costs and is directly involved with oversight of business management. BoC quality is believed to direct the validity of accounting statements, resulting in stakeholder confidence in the corporate governance mechanism, which in turn has a positive effect on the company. Companies with high board quality will reduce inherent risk due to reduced agency problems and increased monitoring of managerial performance, which will lead to credible financial reporting (Anderson et al., 2004; Bhojraj & Sengupta, 2003; Ertugrul & Hegde, 2008; Klai & Omri, 2010).

Another governance mechanism that is suspected to be related to earnings management is the audit committee. The audit committee is an extension of the BoC in supervising management in managing the company. Several research results found that audit committees negatively affect earnings management, where it was concluded that audit committees could reduce earnings management practices by management (Herranz et al., 2022; Mohd Saleh et al., 2007; Yang & Krishnan, 2005).

H1a: There is influence from the independent board of commissioners and earning management.

H1b: There is an influence of the audit committee and earning management

Some of the results of previous studies state that family ownership in a business dramatically influences the performance of governance mechanisms in improving the quality of financial reports (Amrah & Obaid, 2019; Lefort & Urzúa, 2008). Amrah & Obaid (2019) states that the quality of financial reporting can be improved by governance mechanisms, but this will be stronger when tested on companies without family ownership, and conversely, this effect is weakened when tested on companies with family ownership in it. However, on the other hand, it is also known that companies with family ownership in them can improve company performance. Based on the description above, the hypotheses that can be built are as follows:

H3a: Family ownership moderates the influence of the board of commissioners and earning management

H3b: Family ownership moderates the influence of the audit committee and earnings management.

RESEARCH METHODS

This study analyzes the relationship between corporate governance mechanisms, namely the ratio of the board of commissioners and the number of company audit committees, on the quality of financial reporting as measured by earning management with the moderating effect of family ownership. Analysis was performed with moderated regression model unbalanced panel data. The sample for this study were companies listed on the Indonesia Stock Exchange (IDX) on the Kompas 100 Index for the 2015-2019 period for reasons of data availability. The sample companies in this study are characterized by the criteria that the company is listed on the stock exchange during the observation period and has data availability that can be traced.

The dependent variable in this study is Financial Reporting Quality (FRQ). The quality of financial reporting (FRQ) is adjusted to the model of Chen et al. (2011), which is a formulation of earning management consisting of four proxies, Discretionary Accrual (Dacc), Discretionary Revenue (DR), Accrual Quality (AQ), and Aggregate Standardized Value (ASV), where the higher these four values, it is concluded that the higher the quality of financial reporting.

The independent variables in this study is governance mechanisms. The Board of Commissioners (BoC) and the audit committee are used in the governance mechanism variable as measurement proxies. BoC will be measured using the ratio of independent commissioners to the company's entire board of commissioners. The following corporate governance mechanism also measures the audit committee as an extension of the board of commissioners in overseeing management's implementation of company activities. The measurement of the audit committee uses the POJK regulation approach 55 of 2015, which requires a minimum of three audit committee members, and we used number of audit committee's member.

This study raises the element of moderation carried out by Family Ownership (FO). For measuring family ownership, this study uses a measurement of 1 for companies with family ownership and 0 for companies that do not have family ownership in them. The control variables in this study adopted by Klai & Omri (2010), namely firm size (Size), Leverage (Lev), and firm age (Age). Firm size in this study is calculated by the natural logarithm of the book value of the company's total assets. In contrast, leverage is calculated by total liabilities divided by total assets. Meanwhile, Age has used the ratio of the company's age since its founding.

RESULTS AND DISCUSSIONS

This chapter will explain the results of testing the research model conducted with the Stata application version 17 to determine the relationship between variables. This test includes descriptive statistics, pairwise correlations, cross-sectional time-series GLS regression and a discussion of the results. The subject of this study is the Kompas 100 company listed on the Indonesian stock exchange. This study aims to find out how the quality of financial reports directly affects or indirectly with family ownership as the moderating variable.

Table 1 describes the summary of descriptive statistics on all the variables tested in the research model. It can be seen that the companies on the compass index 100 from 2015 to 2019 show that the number of valid observational data for each variable is 498. The Earning Management sample data has a minimum value of -2,312 and a maximum value of 959,736. From the 2015-2019 period, it is known that the mean value is 7,412, smaller than the standard deviation value of 74,819, so it can be concluded that earnings management has a relatively higher distribution in this index company.

The ratio of independent commissioners is known the minimum value is 0, the maximum value is 0.833, the mean value for the 2015-2019 period is 0.419, and the standard deviation value is 0.124, meaning that the mean value is greater than the standard deviation value so this indicates that the variables have been grouped and are homogeneous. Furthermore, the audit committee's minimum value is 2, and the maximum is 7. From the 2015-2019 period, it is known that the mean value is 3,362, which is greater than the standard deviation value of 0,781, so it can be concluded that the most significant number of audit committees is seven people. Companies still need to comply with applicable regulations requiring a minimum number of audit committee members to be three people.

Tabel 1. Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
EM	498	7.412	74.819	-2.312	959.736
Kom	498	.419	.124	0	.833

Kom_Aud	498	3.362	.781	2	7
FODummy	498	.363	.481	0	1
LEV	498	26.698	32.975	.06	100
SIZE	498	6.580e+08	1.009e+09	15.803	2.757e+09
AGE	498	38.641	21.792	3	122

Source: Results of data processing

Tabel 2. Pairwise correlations

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
(1) EM	1.000							
(2) Kom	-0.066	1.000						
(3) Kom_Aud	0.014	0.121*	1.000					
(4) ICW	-0.244*	0.031	0.210*	1.000				
(5) FODummy	-0.022	0.056	0.063	-0.022	1.000			
(6) LEV	0.004	0.187*	0.300*	-0.056	0.193*	1.000		
(7) SIZE	-0.058	-0.001	-0.060	0.242*	-0.194*	-0.518*	1.000	
(8) AGE	-0.075	0.105	0.304*	0.079	-0.042	0.230*	-0.134*	1.000

*** $p<0.01$, ** $p<0.05$, * $p<0.1$

Source: Results of data processing

Family ownership is known that the minimum value is 0, and the maximum value is 1. From the 2015-2019 period, it is known that the mean value is 0.363, and the standard deviation value is 0.481, meaning that the mean value for the 2015-2019 period is smaller than the standard deviation value, so it can be concluded that the total percentage relatively higher family ownership is equal to 1% spread in this index company. The control variables, namely size, financial leverage, and company age, have good data distribution.

Table 2 describes the results between the variables used. Commissioners are positively correlated with audit committees of 0.121 and leverage of 0.187. Meanwhile, the Audit Committee is also positively correlated with Leverage and Age at 10%. The moderating variable, namely family ownership, is positively correlated with leverage ($p<0.1$) and negatively correlated with size ($p<0.1$).

The results of research from Yasmeen & Hermawati (2015) do not support this study which states that the Board of Commissioners does not affect the quality of financial reporting. However, research Hapsari et al. (2021) and Iswara (2016) supports this research which shows that independent commissioners are related to earnings management, meaning that the number of commissioners in a company can reduce earnings management practices which will have an impact on higher quality financial reports.

Because it presents financial reports in real terms, this study proves that the higher number of independent commissioners owned by a company affects the earning management carried out in the company's annual report.

The research results from Al-Homaidi et al. (2018) do not support this study which states that audit committees have a significant effect on the quality of financial reporting. However, research Baxter & Cotter (2009) and Shah et al. (2019) support this research, which shows that audit committees are not related to earnings management in financial reporting.

The Effect of Family Ownership on Earning Management

Based on table 4, the results of hypothesis testing show that family ownership significantly negatively affects earnings management. Family ownership has a significance value of less than 0.01. The results of the research hypothesis test also show that the coefficient value of family ownership is negative. This means that the higher the ratio of family ownership, the tendency to carry out earning management is getting lower, or the quality of financial reporting is getting better.

Family ownership in this study was measured using the dummy method, namely a score of 1 for companies with family ownership and 0 for companies without family ownership. The results of this study support the research of Dashtbayaz et al. (2019), Weiss (2014) and Bardhan et al. (2015), which shows that family ownership has a significant effect on earning management in financial statements.

The Influence of the Moderating Effect of Family Ownership on the

Relationship between the Board of Commissioners and Earning Management

Based on table 4, the hypothesis test results show that the proportion of independent commissioners has a significant negative effect on earnings management. Namely, the higher the proportion of independent commissioners, the lower the earning management potential. In the moderating effect, family ownership is also seen to have a significant relationship with the board of commissioners and earnings management. The results of the research hypothesis test also show a positive coefficient value. This means that in the moderating effect, family ownership can also strengthen the function of the board of commissioners as a supervisor of management performance so that the tendency for earnings management to be carried out by company managers will also decrease. This research is in line with the research results of Hashim & Amrah (2016), Amrah & Obaid (2019), and Alshirah et al. (2020), which state that there is a significant relationship between corporate governance and earning management in family-owned companies.

Influence of the Board of Commissioners on Earning Management

Tabel 3. Cross-sectional time-series FGLS regression

EM	Coef.	St.Err.	t-value	p-value	[95% Conf	Sig
Kom	-79.397	33.796	-2.35	.019	-145.636	**
Kom_Aud	7.371	5.609	1.31	.189	-3.622	
FODummy	-188.037	51.617	-3.64	0	-289.205	***
KomxFODummy	113.235	52.783	2.15	.032	9.783	**
Kom_AudXFODummy	7.418	9.164	0.81	.418	-10.543	
LEV	-.061	.122	-0.50	.618	-.299	
SIZE	0	0	-0.36	.719	0	
AGE	-.222	.159	-1.40	.162	-.533	
Constant	208.894	30.594	6.83	0	148.931	***
Mean dependent var	7.426		SD dependent var			74.894
Number of obs	497		Chi-square			72.575
Prob > chi2	1.000		Akaike crit. (AIC)			5661.861

*** $p<0.01$, ** $p<0.05$, * $p<0.1$

Source: Results of data processing

The Effect of Moderating Family Ownership on Relationships with Audit Committees and Earning Management

Based on table 4, the results of the hypothesis test show that the audit committee has no significant effect on earnings management, namely the number of audit committees does not affect the implementation of a quality audit process, so earnings management can still occur even though the company already has a large number of audit committees. After being moderated, family ownership is also seen not to affect the relationship between the audit committee and earnings management. This happens with the allegation that earnings management can occur when company management has the opportunity to manipulate so that no matter how significant the number of audit committees is, manipulation can still occur. It also concludes that many company audit committees are not the main factor in creating reasonable internal control. Meanwhile, the characteristics of family firms in Indonesia also cannot influence the relationship between the number of audit committees and earnings management. The results of this research differ from those of Natsir & Badera (2020) and Al-Shaer & Zaman (2021), which state that family ownership weakens the influence of audit committees on company earnings management practices. This study also does not support the results of research from Amrah & Obaid (2019), stating that there is a significant relationship between corporate governance and earnings management in owned companies.

Effect of Control Variables (Leverage, Size, Age) on Earning Management

Based on table 4, the results of the hypothesis test show that the control variable has no significant effect on earning management. Company leverage cannot create a tendency for earnings management to occur. The size described by total assets is also not the cause of earnings management. Age, as measured by the age of the company's establishment, also cannot influence the rise and fall of earnings management. This study supports the results of research belonging to Hashim & Amrah (2016) and Al-Shaer & Zaman (2021), which state that leverage and age have no statistically significant effect on the quality of financial reporting. Meanwhile, Putra (2016) states that leverage and firm age have no significant effect on earnings management.

CONCLUSIONS

This study examines and analyses the effect of an independent board of commissioners, audit committee, and internal control weakness on earning management in companies on the Kompas 100 index in 2015-2019. The company sample data used in this study were 498 observations. From the results of this study, researchers can conclude as follows:

1. The results of testing the first hypothesis (H1) show that the board of commissioners variable significantly negatively affects earnings management in companies on the compass index of 100 in 2015-2019. This means that the higher the number of independent commissioners, the more supervision over management will increase, so the tendency for earnings management to be carried out by directors and managers will be lower.
2. The results of testing the second hypothesis (H2) show that the audit committee variable has no significant effect on earnings management in companies on the compass index of 100 in 2015-2019. That is, the number of audit committees does not affect the implementation of a quality audit process, so earnings management can still occur even though the company already has many audit committees.
3. The results of hypothesis testing show that the moderating effect of family ownership strengthens the relationship between the board of commissioners and earnings management in companies on the Kompas 100 index in 2015-2019. This means that the higher the ratio of family ownership, the lower the tendency to do earnings management or the better the quality of financial reporting.
4. The results of testing the fourth hypothesis (H4) show that the moderating effect of family ownership cannot influence the relationship between audit committees and earnings management in companies on the compass index of 100 in 2015-2019. This means that in the moderation effect, family ownership can also strengthen the function of the board of commissioners as a supervisor of management performance so that the tendency for earnings management to be carried out by company managers will also decrease.
5. The results of testing the sixth hypothesis (H6) show that the control variables (Leverage, Size and Age) have no significant effect on earnings management in companies on the compass index of 100 in 2015-2019. Company leverage cannot create a tendency for earnings management to occur. The size described by total assets is also different from the cause of earnings management. Age, as measured by the age of the company's establishment, also cannot influence the rise and fall of earnings management.

This research has implications for internal auditors who wish to improve the effectiveness of internal auditing and the accuracy and quality of financial reports. In addition, the implications of this study also recommend restructuring the internal audit function, especially its role in management and governance, given that its role should be objective and impartial.

Apart from the implications, based on the description of the discussion and conclusions from this study, there are limitations and also suggestions for further research, as follows:

1. There are still many variables that can affect earnings management. However, this study only used independent variables: Corporate Governance Mechanisms (Independent Board of Commissioners and Audit Committee), Internal Control Weakness and several control variables such as Leverage, Size, and Age. There is a need for additional independent variables that can affect earnings management in further research. Future research can add other independent variables whose results are inconsistent with previous studies, such as management ownership, public ownership, foreign ownership, and risk management committees.
2. In this study, the authors used data on companies at the compass index of 100 for five years (2015-2019). So the research results still need to be able to be generalised to other data or situations. Furthermore, for further research, it is hoped that it will increase the research period by taking a more extended period and using a wider research object.
3. This study uses data on companies on the compass index 100 in 2015-2019 to avoid the last data instability that was affected by the pandemic. It is hoped that future research can include the pandemic factor so that comparisons between normal conditions and conditions during a pandemic can be made.

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