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**| RESEARCH ARTICLE**

**Analysis of Audit Quality, Bonus Mechanism, and Company Size on Earning Management with Managerial Ownership as Moderating**

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**| ABSTRACT**

This study aims to examine audit quality, bonus mechanisms, and company size on earning management moderated by managerial ownership. The purposive sampling method was used to collect research data, and the multiple regression equation models were used as a statistical analysis tool. The sample in this study were 46 issuers on the Indonesia Stock Exchange, especially manufacturing sector companies whose financial reports had been published for 3 (three) years from 2019 to 2021. Based on the results of this study, it shows that audit quality has a positive effect on earning management. This research has implications for earnings management which tend to be influenced by the audit quality owned by the company and to be able to see sustainable developments that support the survival of the company and expand previous research, especially the detection of earnings management.

**| KEYWORDS**

Audit quality, Bonus Mechanism, Company Size, Managerial Ownership

**| ARTICLE INFORMATION**

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**1. Introduction**

The objective of financial reports is to provide information regarding the financial position, performance, and changes in the financial position of an entity that is useful to a wide range of users in making economic decisions. However, in the report, finance does not provide all possible information needed by the user in taking a decision because, in a manner, it generally describes the influence of finance from what happened in the past and is not required to provide information nonfinancial. Management, as agents trusted by the holder shares (principals), are expected can and can create and maintain report finance with ok. Problem agency appears when the principal difficulty ensures that the agent Act maximises the well-being principal. As an agent trusted by shareholders (principals), management is expected to be able and able to properly prepare and maintain financial reports. Agency problems arise when the principal has difficulty ensuring that the agent acts to maximize the welfare of the principal. According to agency theory, one of the mechanisms that are widely used and are expected to align the objectives of the principal and the agent is the financial reporting mechanism.

According to Manossoh (2016), management profit is a condition where party management turns out not succeed and achieves the specified profit target; then, management will utilise flexibility allowed by the standard accountancy in arranging report finance to modify reported earnings. Management is motivated to show that performance is good in producing a score or profit maximum for the company, so management tends to choose and apply methods of possible accounting to give information to profit. Management is motivated to show good performance both in generating maximum value or profit for the company, so management tends to choose and apply accounting methods that can provide better profit information.

According to Jaya (2021), several cases of earnings management in Indonesia seem to never subside every year. Various cases of earnings management are summarized as follows:

1. PT Karina Utama Tbk, which was established in Indonesia on June 20, 1997, has manipulated the 2008 financial statement and has manipulated the 2009 audited financial statements.
2. PT. Garda Tujuh Buana Tbk (GTBO) was also proven to have falsified the company's 2012 financial statements, which were not in accordance.
3. In May 2015, the company Toshiba stated that the company was investigating an internal accounting scandal internal accounting and should revise the calculation of the profit in 3 years last. After conducting an investigation in a thorough manner, you know that Toshiba has had difficulty achieving profit targets business since 2008, the time of the middle of happen global crisis. The crisis also hit Toshiba's business up to finally. Toshiba did something like this through accounting fraud. This action is conducted with various efforts, so it produces no profit corresponding with reality.

According to Barghathi et al. (2021), auditors have the fortitude to handle client and company pressure that can result in hidden anomalies and earnings management practices that lower audit quality, particularly in non-Big Four companies. The International Auditing and Assurance Standards Boards (IAASB) launched an extended audit report and created the International Standard on Auditing (ISA)-701 in January 2015 to address concerns regarding the lack of transparency. Key Audit Matters (KAMs), which went into effect on December 15, 2016, are required to be included in independent audit reports in accordance with the standards (IAASB, 2013). The auditor does not express a separate opinion on these matters, according to ISA-701 (KAM), "matters that matter most in an audit of financial statements" and that their handling is in the context of an audit of the financial statements as a whole and in providing an opinion (ISA 701, par. 11).

According to Debnath et al. (2021), one of the reasons the capital market is ineffective is that listed companies do not accurately report their financial status, and auditors do not offer high-quality audit services. If an auditor has the knowledge and desire to provide high-quality audit services, it can restrict the activities of its clients to earnings management and may also insist on the transparency of its financial reports.

According to Platinum et al. (2019), there is evidence of a desire to manage earnings with the goal of receiving a sizable bonus in share ownership levels below 5%. Contrarily, when ownership exceeds 25%, there is no desire to manage earnings because there are control rights in the business, which reduces information asymmetry. According to Gayatri et al. (2021), one of the elements that can motivate businesses to implement earnings management is the size of the organization. Small businesses often manage their earnings to attract investors to buy their shares, as evidenced by the high total assets of the business, whereas large businesses manage their earnings to prevent profit fluctuations.

According to Naz et al. (2011), a company's size had a favorable relationship with management profit. Internal system control is primarily related to business size. More substantial businesses have sophisticated internal controls. Internal controls that are effective as a system might enable the company to inform the public of inaccurate information. In 2020, Oktasari's rising large-scale income, total assets, and total capital will reflect the state of the company's strong growth. Size Company describes a scale with different scores for equity, sales, and assets. The company's progressively higher score reflects a stronger company. Malau (2017) Size Company is a scale that reflects a small company's average total sales and total assets. In actuality, the business was divided into three categories: small, medium, and large.

Ningrum (2021) asserts that management will carry out earnings management actions to the greatest extent possible if incentives are low; conversely, if incentives are high, management will exercise less control over earnings. This study aimed to investigate the impact of audit quality, bonus structures, and firm size on earning management. The impact of audit quality, bonus structures, and company size on earnings management in manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the study period will also be investigated.

This study's research covered the five-year period (2017-2021) of a company listed on the Indonesia Stock Exchange. The company subsector industry goods consumption is the focus of this study. A study was done on the business subsector of the manufacturing industry, which has made a significant contribution to the expansion of the economy. The sector's business also helps to sustain people's daily activities. The title of this study is "The Effect of audit quality, bonus mechanisms, and company size on earning management, with managerial ownership as a moderating variable," based on the background that has been explained.

## 2. Agency Theory

Jensen and Meckling (1976) explain several forms of agency costs, which consist of:

1. Monitoring costs  
Monitoring costs to be incurred by the owner. These costs are incurred to monitor managers by measuring, observing, and controlling the behaviour of managers.
2. Guarantee fee  
Costs that must be incurred as a result of monitoring must be issued by the principal to the agent. These costs arise to guarantee managers to make decisions that are not detrimental and in accordance with the interests of shareholders.
3. Residual losses  
Cost this is incurred losses although monitoring and assurance have been carried out. Problem agency appeared when the principal difficulty ensured that the agent Act maximize the well-being principal. According to the theory of agency, one mechanism that is widely used and expected could align the purpose principal and agent; this is through mechanism reporting finance. Agency theory suggests that the agent, as a principal representative, should be transmitted success signals or failures that have been achieved to principals.

### **2.1 Earning Management**

A manager has the opportunity to use wisdom in preparing and reporting information accounting for personal gain due to information asymmetry among managers and users, according to Ghazali et al. (2015). Accounting is management profit when information is prepared and reported with discretion.

According to Ghazali et al. (2015), information asymmetry between managers and users of external information accounting provides the manager with the opportunity to use judgment when preparing and reporting information accountancy for personal gain. Accounting is management profit when information is prepared and reported with discretion.

### **2.2 Quality audits**

According to Oluwasegun and Awuye (2022), audit quality has an impact on earnings management. Higher accrual and real levels of earnings management are reported by Big Four audit clients. This claim has a low likelihood of being challenged in court by auditors. Limiting the issue of earnings manipulation in a company's financial statements is possible through an efficient corporate governance mechanism called audit quality. Debnath et al. (2021) came to a different conclusion, and Kurniawan et al. (2022) came to the conclusion that audit quality has no bearing on earning management.

H1: Audit Quality has a positive effect on Earning Management

### **2.3 Bonus Mechanisms**

According to Prihastomo et al. (2018), bonus compensation has a detrimental impact on earning management. The management's actions in managing earnings are generally worse the higher the bonus they receive. This is so that the decisions made by company managers are constantly under the scrutiny of outside parties (investors) so that business executives don't engage in unethical behavior that could lead to high-earnings management techniques. Contrary to Platina et al. (2019) and Edwita et al. (2022)'s findings, bonus plans do not affect the management of earnings and the smoothing of income.

H2: Bonus Mechanisms influential negative to Earning Management

### **2.4 Company Size**

According to Swastika's (2013) research findings, firm size has a detrimental impact on earning management. More sophisticated internal systems, more capable auditors (the big four), and more reputable companies will prevent earning management. The different finding is that firm size has no bearing on earning management, according to Naz et al. (2011), Siregar (2017), and Rely (2022).

H3: Firm Size Has a negative effect on Earning Management

### **2.5 Managerial Ownership strengthens the relationship between audit quality and earnings management.**

Oluwasegun and Awuye (2022) draw the conclusion that audit quality affects revenue management. Higher accrual and real levels of earnings management are reported by Big Four audit clients. This claim has a low likelihood of being challenged in court by auditors. Limiting the issue of earnings manipulation in a company's financial statements is possible through an efficient corporate governance mechanism called audit quality. Because managerial ownership determines policies and decisions about accounting methods applied to managed companies, both can have an impact on earnings management. The study by Malau (2020) on

management motivation for sustainability reporting offers much-needed insight into the underlying variables that affect reporting practices.

H4: Managerial Ownership strengthens the relationship between audit quality and Earning Management.

### **2.6 Managerial Ownership strengthens the connection between the bonus mechanism and earning management.**

According to Prihastomo et al. (2018), bonus compensation has a detrimental impact on earning management. The management's actions in managing earnings are generally worse the higher the bonus they receive. This is so that the decisions made by company managers are constantly under the scrutiny of outside parties (investors) so that business executives don't engage in unethical behavior that could lead to high-earnings management techniques. Because managerial ownership determines policies and decisions about accounting methods applied to managed companies, both can have an impact on earnings management.

H5: Managerial Ownership strengthens the relationship between the bonus mechanism and Earning Management

### **2.7 Managerial Ownership Strengthens the Relationship between company size and earnings management**

According to Sholichah et al. (2022), the size of the company has a negative impact on management profit. A larger company with sophisticated internal controls, competent Big Four auditors, and a better reputation will avoid earning management. They may also have an impact on management profit because ownership managers decide on accounting policies and decisions that are applied to managed companies.

H6: Managerial Ownership strengthens the connection between company size and Earning Management

## **3. Methods**

This study falls under quantitative research. The population of the study consists of companies in the goods consumption industry subsector that are listed on the Indonesia Stock Exchange for the years 2017 through 2021. Purposive sampling was used to collect sample of 46, with the following criteria:

1. The company publishes audited financial statements using the rupiah currency for the period 31 December 2017 – 31 December 2021.
2. The company did not experience a delisting from the stock exchange during the period 31 December 2017 – 31 December 2021.
3. The company experiences profit before income tax

## **4. Results and Discussion**

Variable	Prediction	Coefficient	1-Tailed	Statistics Collinearity	
				Tolerance	VIF
Constanta		1,784	0,000		
AQ	+	0,293	0,014**)	0,892	1,122
BM	-	0,686	0,005*)	0,953	1,050
CS	-	-0,036	0,086**)	0,941	1,063
MO*AQ	+	-2,538	0,385	0,894	1,119
MO*BM	-	4,583	0,226	0,723	1,382
MO*CS	-	0,058	0,188	0,734	1,363
Normality Test		0,200			
Durbin-Watson Stat		2,374			
Uji Glejser		3,744			
Adjusted R2		0,087			
Prob (F-Statistics)		0,023			
Total Observation		101			

\*\*\*Signifikan pada level 1%, \*\*Significant pada level 5%  
Note: Table this presented descriptive statistics for each variable research. The purpose of this table is to give a description of the conditioned tendency central.

Source: SPSS Output Results

#### **4.1 Normality test**

Results of Table 1 above show significant data of 0.200, which is above 0.05. Therefore, the residual values are normally distributed so that the research model stated has fulfilled the assumption of normality.

#### **4.2 Heteroscedasticity Test**

In this case, using the Glejser test where regress absolute error with variable independent, expected no there is a significant variable. The result of this test is a score probability bigger from level significant (0.05) then no reject  $H_0$ . Got concluded that the residual model had fulfilled the assumption of homogeneity / non-heteroscedasticity.

#### **4.3 Multicollinearity Test**

Table 1 shows that variable Audit Quality, Bonus Mechanism, Company Size, Managerial Ownership \* Audit Quality, Managerial Ownership \* Bonus Mechanism, Managerial Ownership \* Company Size has VIF < 10. Then  $H_0$  is accepted, meaning variables that show, not there is, symptom collinearity. In other words, relationships between variable no have a very strong correlation with variable other. In other words, it can be concluded that the regression model used spared from problem multicollinearity.

#### **4.4 Autocorrelation Test**

Autocorrelation test results in Durbin-Watson (DW), from the table above, show that the DW value is 2,374 (DW numbers between -2 to +2), which means that there is no regression model autocorrelation in research this.

#### **4.5 Testing hypothesis**

##### **4.5.1 R & R-Square Test (Coefficient of Determination)**

Table 1 shows the score adjusted r square 0.087 > 0 and close to 1, so variables independent give almost all required information for predicting variation variable dependent. Whereas the R value 0.377

##### **4.5.2 F Test (F Test)**

Table 1 shows variables independently tested have a significant influence on variable quality profit. This could see from the F value calculation, which is a value of 2.592 with a level probability of 0.023 (significance); because the probability is far smaller than 0.05 then, the regression model could be used for predicting the score company

#### **5. Discussion**

##### **5.1 Audit Quality Has a positive effect on Earning Management**

The results of the regression analysis show that the significance value is 0.014, and it has a beta value of 0.293. When compared with the alpha value of 5%, this significant value is much smaller (0.014 < 0.05). Audit quality matters positively to earning management. Research results correspond with the results study Oluwasegun (2022) and Awuye (2022). Big Four audit clients record higher accrual and real levels of earnings management. This assertion can be associated with a low level of auditor litigation risk. Audit quality is an effective corporate governance mechanism to limit the problem of earnings manipulation in a company's financial statements.

##### **5.2 Bonus Mechanisms influential negative to Earning Management**

Analysis results in regression show that the score significance as the big value was 0.005, and it had a beta value of 0.686. When compared with the alpha value of 5%, this significant value is smaller (0.005 < 0.05). The bonus mechanism takes effect with no significance to earning management. Bonus implications are considered to influence management in choosing certain accounting procedures. The bonus mechanism is reflected in the positive linear function of reported earnings. The increase in the value of the bonus is based on the increase in the value of an entity's profit.

##### **5.3 Company Size influential negative to Earning Management**

The results of the regression analysis show that the significance value is 0.086, and it has a beta value of -0.036. When compared with the alpha value of 5%, this significant value is greater (0.086 > 0.05). Size company has no influential earning management. Management profits no influenced by big or small size something entity. Large companies, of course, have implemented good

corporate governance. Large companies will have good internal controls, which will lead to better monitoring of the company's activities.

#### **5.4 Managerial Ownership Strengthens the effect of audit quality on earnings management**

The results of the regression analysis showed that the significance value was 0.385, and it had a beta value of -2.538. When compared with the alpha value of 5%, this significant value is greater ( $0.385 > 0.05$ ). Managerial ownership does not strengthen the effect of audit quality on earnings management. Companies that already have good audit quality will not be strengthened by the influence of management ownership in managing earnings. External audit activities carried out by the big four public accounting firms have been tested throughout the world so that the audit quality they have is better in preventing earnings management.

#### **5.5 Managerial Ownership strengthens the effect of the bonus mechanism on earning management**

The results of the regression analysis showed that the significance value was 0.226, and it had a beta value of 4.583. When compared with the alpha value of 5%, this significant value is greater ( $0.226 > 0.05$ ). Managerial ownership no strengthens the influence of the bonus mechanism against earning management. Companies that have implemented good corporate governance will not be strengthened by the influence of management ownership in influencing the bonus mechanism and earnings management. Company procedures that are carried out properly will have a positive impact on the company, one of which is an increase in income which can trigger satisfaction with work results from management without carrying out earnings management.

#### **5.6 Managerial Ownership Strengthens the influence of company size on earnings management**

The results of the regression analysis showed that the significance value was 0.188, and it had a beta value of 0.058. When compared with the alpha value of 5%, this significant value is greater ( $0.188 > 0.05$ ). Managerial ownership no strengthens influence on company size to earning management. Great companies naturally already run Corporate Governance. Large companies, of course, have implemented good corporate governance. Large companies will have good internal controls, which will lead to better monitoring of the company's activities.

## **6. Conclusion**

Based on the results analysis and discussion that has been described, then we could take several conclusions as follows:

Big Four audit clients record higher accrual and real levels of earnings management. This assertion can be associated with a low level of auditor litigation risk. Audit quality is an effective corporate governance mechanism to limit the problem of earnings manipulation in a company's financial statements. The bonus mechanism takes effect with no significance to earning management. The bonus implications are considered to influence management in choosing procedures for Accountancy certain. The bonus mechanism is reflected in a positive linear function from reported profit. Enhancement bonus value is based on enhancement score from profit something entity.

Size company influential positive to earning management. Management profits no influenced by the big or small size of something entity. Great companies naturally already run Corporate Governance. As well as the quality of audits carried out company have a significant influence on management earnings and reports continuously on a company.

### **6.1 Limitations**

This study had limitations. The current study used a dummy variable as a proxy for audit quality variables; thus, it is recommended that future research use other proxies in more depth. Additionally, future research should examine the reinforcing or weakening effects on the research model that moderating variables may have. The study also used two control variables to examine sustainable company performance, which was audit quality and company size.

There are several implications for the research results as follows:

**Theoretical Implications:** This research provides an opportunity to further explore the consequences of information knowledge and expand upon existing insights. It is of particular interest to accountants, teachers, researchers, and readers. Additionally, this discovery has the potential to improve the ability to identify and control earnings.

**Managerial Implications:** This study demonstrates the critical role of audit quality in preventing losses to the company and is expected to serve as a reference for managers to identify potential symptoms of profit control practices.

**Further Research Implications:** Data collection for sample processing should combine primary and secondary data in order to achieve better results. It is also recommended that future research expand its sample to include companies from different countries and various industries.

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