

The Effect of Institutional Ownership, Managerial Ownership and Deferred Tax Expense on Earnings Management in Indonesia

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Abstract

The goal of this research was to see how Institutional Ownership, Managerial Ownership, and Deferred Tax Expense affected Earnings Management. In this study, 811 non-financial businesses listed on the Indonesia Stock Exchange from 2017 to 2019 were used as a sample. The independent factors in this study were Institutional Ownership, Managerial Ownership, and Deferred Tax Expense, while the dependent variable was Earnings Management. Multiple linear regression analysis was used to analyze the data in this study. This study's findings suggest that institutional and managerial ownership have an impact on earnings management. The Variable for Deferred Tax Expenses has no effect.

Keywords: *Institutional Ownership, Managerial Ownership, Deferred Tax Expense, Earnings Management*



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INTRODUCTION

The company must have a competitive advantage in order to maintain its business continuity (going concern). Kamran & Shah (2014) states that financial statements are one way to provide information about a company's financial performance and how the company's management is responsible for its owner. Information concerning a company is one of them contained in the financial statements so that financial statements become a medium of communication for the company manager and other stakeholders.

Earnings is one of the measuring instruments used to determine the company's performance. The greater the profit figures earned, indicating the better the company's ability to manage resources in an effort to earn profit. Earnings information from financial statements will be used by external parties as well as internally to make decisions related to compensation, bonuses, measures of achievement, management performance, and tax collection (Suputra, 2017).

According to Kusumawardhani (2012), earnings management is not a detrimental thing as long as it is done in the corridors of opportunity. Profit management is not always interpreted by the process of manipulation of financial statements because there are several options of methods that can be used and not as a prohibition.

One of the phenomena regarding the engineering of financial statements conducted by PT Asuransi Jiwasraya (AJS) was revealed by the Audit Board of Finance (BPK) through the assessment of preliminary investigations. In 2006 there was a profit manipulation of Rp 360.3 billion. It was said by Agung Chairman Firman Sampurna that the opening of AJS's financial profit obtained adverse or modified opinions (Putri, 2021). The Audit Board of Finance (BPK) said AJS profited from the engineering of financial statements

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(window dressing) since 2006. AJS's finances also deteriorated until October 2018 there was a failure to pay customer claims amounting to Rp 802 billion (Wicaksono, 2021).

Related to tax, there is a phenomenon by PT DC that reduces the amount of value-added tax (VAT) deposited into the state treasury using unauthorized invoices in the period of 2010 to 2012 (Mediatama, 2021). Another phenomenon concerning taxes delivered by the Regional Office of the Directorate General of Taxation of West Jakarta at a press conference on February 10, 2020, concerning PT Gemilang Sukses Garmino which issued a fictitious tax invoice or TBST (Not Based on Actual Transactions) in violation of Law No. 16 of 2009 concerning General Provisions and Procedures for Taxation (Cahyani, 2021).

There are many studies conducted to examine issues related to profit management, especially regarding corporate governance and deferred tax expense, Wang & Siyu (2012); Suputra (2017); Mudjiyanti (2018); Achyani & Lestari (2019); Bunaca & Nurdyadi (2019) showed inconsistent results. Based on the background of the problem, the problem formulation in this study is "Does Institutional Ownership, Managerial Ownership and Deferred Tax Expense affect Profit Management in Indonesia?"

LITERATURE REVIEW

Agency Theory

The owner and the manager have an agency connection, which produces an agency conflict because the mutualism symbiosis is not related to differences in interests. Profit management is explained using the agency theory method, which claims that conflicts of interest have an impact on profit management (Suputra, 2017). The principal and the agent have a contractual relationship in which the agent has the power to act on behalf of the principal and is compensated for doing so. The relationship between investors and management might be described as agency relations. When the principal is a shareholder or investor, and the agent is management, agency theory helps explain management behavior (Suwardjono, 2014). The importance of transferring over the company's operability from the owner (principal) to a party who can better manage the organization is emphasized by agency theory (agent) (Sulistyanto, 2008).

Earnings Management

Earnings management is a managerial endeavor to make use of the freedom to employ accounting methods and judge the worth of accounting in dealing with financial statement information (Sulistyanto, 2008). According to Scott (2015), Profit management is a management accounting policy that focuses on the process of generating external financial statements for the purpose of personal gain. Earnings management can influence financial data by employing accounting methods, accounting estimation values, or both at the same time (Sulistyanto, 2008). Earnings management practices are carried out by management due to several motivations, namely: (1) Motivation of bonus programs; (2) Tax motivation; (3) Political motivation; (4) CEO switching motivation; (5) Initial Public Offering (IPO) (6) Motivation of debt agreement.

Good Corporate Governance

Corporate governance is a set of integrated systems for managing, guiding, and leading a company or a corporation with the goal of improving the firm's and the community's value. According to the OECD (The Organization for Economic Cooperation and Development) (2003), Good corporate governance is a structure where stakeholders, shareholders, commissioners, and managers draft the company's objectives in an integrated manner and contain the means to achieve these goals and oversee the performance of the

company's management. Research conducted by Chhaochharia & Grinstein (2007) shows that corporate governance influences the information reported by companies indirectly.

Institutional Ownership

Institutional ownership is regarded to be capable of providing similar internal surveillance systems. The shares of corporations controlled by institutions or institutions are referred to as institutional ownership (insurance companies, banks, investment companies, and other institutional holdings). Balsam et al., (2002) in Siregar & Utama (2005).

According to the study, large institutional ownership can reduce profit management practices, but a significant amount of ownership is required to oversee management, which has the effect of lowering managers' willingness to undertake profit management.

H1: Institutional ownership affects earnings management

Managerial Ownership

Because management owns such a large percentage of the company's stock, their mindset is that of someone who is invested in the company. As a result, management will be motivated to present accurate financial data since the contracting parties will scrutinize the management who owns the company's stock. This will lead to a better contract (Ball and Shivakumar, 2005). Therefore, it is likely that the managerial ownership level will be in the same direction to suppress the utilization of discretionary accruals (earnings management) by management.

H2: Managerial ownership affects earnings management.

Deferred Tax Expense

Expenses resulting from transient disparities between accounting profit (profit reported in financial statements for the benefit of third parties) and fiscal profit (profit used to calculate taxes), when accounting profit tends to be higher than fiscal profit (Suputra, 2017). Phillips et al. (2003) in Suputra (2017) said that management discretion would be greater when the difference in fiscal profit with accounting profit. Yulianti (2005) in Pratita (2017) mentioned the amount of management discretion contained in deferred tax expense that can detect profit management practices in the company. Suputra (2017) showed that deferred tax burden affects profit management.

H3: Deferred tax expense affects earnings management.

RESEARCH METHOD

Population and Samples

The population in this study is all non-financial sector companies listed on the Indonesia Stock Exchange in 2017-2019. The technique used in sampling in this study is the purposive sampling method with criteria: (1) Companies that have complete earnings management data; (2) Have Institutional Ownership, Managerial Ownership and deferred tax expense data.

Research Variable

Independent Variable

a. Institutional Ownership

The percentage of share ownership owned by other institutions from the total number of outstanding firm shares is used to calculate the institutional ownership variable in this study.

b. Managerial Ownership

The percentage of share ownership owned by the management of the total number of outstanding firm shares is used to proxy the managerial ownership variable in this study.

c. Deferred Tax Expense

In this study, the deferred tax expense can be calculated using the deferred tax expense formula (DTE) by weighting the deferred tax expense by total assets as follows (Phillips and Rego, 2003) :

$$DTE = \frac{\text{Deferred Tax Expense } it}{\text{total aset } it - 1}$$

Dependent Variable

a. Earnings Management

Earnings management in this study is proxied by the approach used Modified Jones Model, as follows:

$$TAC = NI_{it} - CFO_{it}$$

The total accrual value (TAC) can be estimated using ordinary least squares (OLS) to obtain the regression coefficient, as follows:

$$\frac{TA_{it}}{A_{i(t-1)}} = \alpha_1 \left(\frac{1}{A_{i(t-1)}} \right) + \alpha_2 \left(\frac{\Delta REV_{it}}{A_{i(t-1)}} \right) + \alpha_3 \left(\frac{PPE_{it}}{A_{i(t-1)}} \right) + \varepsilon$$

The value of non-discretionary accruals can be calculated by the formula:

$$NDA_{it} = \alpha_1 \left(\frac{1}{A_{i(t-1)}} \right) + \alpha_2 \left(\frac{\Delta REV_{it}}{A_{i(t-1)}} - \frac{\Delta REC_{it}}{A_{i(t-1)}} \right) + \alpha_3 \left(\frac{PPE_{it}}{A_{i(t-1)}} \right)$$

Furthermore, discretionary accruals can be calculated by the formula:

$$DA_{it} = \frac{TA_{it}}{A_{i(t-1)}} - NDA_{it}$$

Information:

- DA_{it} = Discretionary Accruals of company i in period t
- α₁, α₂, α₃ = Regression coefficient
- NDA_{it} = Non-discretionary Accruals of the company i in period t
- TA_{it} = Total accruals of the company i in period t
- Ni_{it} = Net profit of company i in period t
- CFO_{it} = Cash flow from operating activities of the company i in period t
- A_{it-1} = Total assets of company i in period t-1
- Rev_{it} = Change in revenue of company i in period t
- PPE_{it} = Fixed assets of the company i in period t
- Rec_{it} = Change in receivables of the company i in period t
- ε = error

b. Data Analysis

This research relies on secondary data. Multiple linear regression approaches were used to examine the data to see if accrual quality, corporate governance, and deferred tax expense had an impact on earnings management. Multiple regression analysis was used to evaluate hypotheses using the following model :

$$EM = \alpha + \beta_1 InsOwn + \beta_2 MOwn + \beta_3 DTE + \varepsilon$$

Information :

Y = Earnings Management

α = Intercept

X1 = Institutional Ownership

X2 = Managerial Ownership

X3 = Deferred Tax Expense

Before performing the regression test, the classical assumptions were tested, namely normality, multicollinearity, autocorrelation, and heteroscedasticity.

FINDING AND DISCUSSION

Descriptive statistics of this study are presented in Table 1 as follows:

Table 1. Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
EM	811	-.00108	.00381	.0003993	.00109686
InsOwn	811	.48041	.91862	.7173367	.12066546
Mown	811	.00000	.25683	.0295646	.05481500
DTE	811	.00000	.03905	.0047983	.00873216
Valid N (listwise)	811				

Source: 2021 Data Processing Results

The assumptions that must be met when using multiple linear regression models are met in this investigation. The Kolmogorov-Smirnov test was used to test sample normality, the Durbin Watson coefficient test was used to test autocorrelation, the Variance Inflation Factor was used to test multicollinearity, and the Spearman Rho test was used to test heteroscedasticity.

Table 2. Result Summary of Multiple Regression Analysis

Model	Coefficient
Constant	0.001
InsOwn	-0.001
Mown	0.001
DTE	-0.003
F	5.908
R²	0.021
Adj R²	0.018

Source: 2021 Data Processing Results

Table 2 shows the results of a multiple linear regression study in which the independent variables Institutional Ownership and Managerial Ownership have an impact on Earnings Management, while the Deferred Tax Expense variable has no impact. The R² and Adjusted R² coefficients of determination are 0.021 and 0.018, respectively. This value indicates that the independent variables used in the model

(Institutional Ownership, Managerial Ownership, and Deferred Tax Expense) could only explain 1.8 percent of the variation in the value of the dependent variable (Earnings Management) with the remaining 98.2% influenced by factors not studied. It can be concluded that the study's independent variable has a limited ability to explain the study's dependent variable. The significance of the F test results in the research model is less than the set threshold (5%). These findings show that the model (Model Fit) utilized in this investigation is appropriate.

Discussion

The Effect of Institutional Ownership on Earnings Management

With a high ownership value, institutional shareholders will encourage more optimal information enhancement and management supervision, potentially reducing managers' opportunistic behavior and allowing institutional owners to receive information comparable to managers and reduce earnings management (Sari and Nur, 2013). This study is in line with research by Astari & Suryanawa (2017), which shows institutional ownership is important in monitoring management because Increased oversight will be encouraged as a result of institutional ownership, which is preferable. The welfare of shareholders will undoubtedly be improved as a result of this supervision, and institutional ownership's impact as a supervisory agent will be reduced due to their substantial capital market investment.

The effect of Managerial Ownership on Earnings Management

Offering managers stock options, often known as stock-based pay, is one strategy used to try to decrease friction generated by the separation of ownership and control between managers and stakeholders. According to (Purnama, 2017) Managerial ownership has an impact on earnings management because, in a case where the manager owns a portion of the firm, the manager will naturally behave as an external shareholder and ensure that the financial statements are presented properly and accurately reflect the company's current state. This research supports the research conducted by Aryanti & Kristanti (2017), which shows the results that managerial ownership has an effect on earnings management due to institutional ownership. Management oversight will be better controlled, resulting in more accurate information, reducing the information asymmetry caused by control. The power of institutional owners will have an impact on how profits are reported.

The effect of Deferred tax expense on Earnings Management

Because the effect of lowering the firm's profit on deferred tax expense is negligible, using deferred tax expense to identify earnings management in the company is ineffective because deferred tax expense cannot demonstrate that the company is undertaking earnings management (Fitriany, 2016). This study is in line with the research of Timuriana & Muhamad (2015). It demonstrates the existence of taxation legislation in Indonesia that places severe limitations on tax computations, stating that the basis for calculating fiscal profit or loss is to acknowledge the amount of income and costs when they are received or issued. In other words, tax computations solely account for current-period tax expense and ignore expenses and deferred tax.

CONCLUSION

The purpose of this study was to see how Institutional Ownership, Managerial Ownership, and Deferred Tax Expense influenced Earnings Management in Indonesia. The findings of this study show that

Institutional Ownership and Managerial Ownership have an impact on Earnings Management, whereas Deferred Tax Expense has no impact.

Suggestions that can be given by researchers for future research are :

1. This research yielded an Adjusted R square value of 1.8 percent, which is still quite low. As a result, more research might be done to seek other independent variables that affect earnings management.
2. The most recent observation year is supposed to be used to characterize the current state of the observed company.

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