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The Effect of Company Characteristics and Audit Committee Composition on Earning Management: Empirical Study of Indonesian Companies in the Food and Beverages Sector

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ABSTRACT: The purpose of this research was to analyze the effect of Financial Leverage, Sales Growth, Firm Size, and Audit Committee Composition on earnings management in the Food and Beverages sub-sector in Indonesia, an empirical study using a panel data approach. This research used panel data for the period 2018 – 2022, obtained from the financial report and annual reports of 19 FnB companies listed on the Indonesia Stock Exchange (IDX). The sample used in this research was determined by the purposive sampling method and resulted in 95 research samples. This research used the Common Effect Model (CEM) panel data regression analysis, with the following research results (1) Sales Growth has a negative and significant effect on Earnings Management, (2) Financial Leverage has no effect on Earnings Management, (3) Firm Size has a negative and significant effect on Earnings Management, and (4) Audit Committee Composition has no effect on Earnings Management.

KEYWORDS: Financial Leverages, Sales Growth, Firm Size, Audit Committee Composition, and Real Earnings Management

I. INTRODUCTION

A company that is established generally has the goal of gaining profits or benefits to be able to finance its operational expenses so that it can compete in the industrial world. To gain profits, a company can strive for the efficiency of existing resources and good financial management. One indicator of a company's success can be measured by an assessment of its finances. The correlation between the financial sector and the company's performance is proven by the company's ability to effectively manage its assets so that it can record profits in its financial statements. One form of corporate responsibility that has gone public according to OJK Regulation Number 29/POJK.04/2016 is to publicly report its financial and non-financial information annually. According to Kasmir (2019), financial reports are made to provide financial information that represents company performance, which is usually used for consideration in making decisions for stakeholders. Financial reports prepared based on accounting standards must be transparent, reliable, and relevant. Financial statements consist of income statement, equity, balance sheet, and cash flow. Information about company profits is a major concern because the value of profits can be used as an indicator to assess the performance of management in the company. Profit information can be used to improve operational activities, evaluate past activities, and plan for the future. Furthermore, for external parties, the use is as information to decide whether to maintain, sell, or increase the company's share ownership. The importance of presenting profit information to the company causes opportunistic earnings management activities on the part of managers (Hery, 2018).

Earnings management is a manager's attempt to affect the information in financial reports, to manipulate financial data to attract the attention of stakeholders (Sulistyanto, 2018). According to Healy and Wahlen (1999), managers' actions in managing earnings are based on contractual agreements between managers and external stakeholders, and for personal gain. With the probability of earnings management practices in financial reports carried out by managers, it makes stakeholders doubt the credibility and reliability of a company's financial reporting (Tolulope, et al., 2018).

Earnings management practices by managers can result in bias presented in the financial statements. Further investigation is needed regarding the indicators that affect earnings management. One indicator that can detect the occurrence of earnings management is the characteristics of the company. This is supported by research conducted by Apriadi, R., Angelina, R. P., Firmansyah, A., & Trisnawati, E. (2022) with company characteristic indicators used which are sales growth, financial leverage, profitability, and firm size affect the occurrence of earnings management. Another indicator that can be used is good corporate governance, namely the composition of the audit committee. The accounting scandal that occurred raises questions about the effectiveness of the audit committee's role in mitigating earnings management. The audit committee is considered the main monitor in a company's financial reporting system, which can provide oversight of it (Khalil, M. M. M., 2010). Klein (2002), states that if the composition of the audit committee is less than the independent directors, then the company has a greater tendency to carry out earnings management.

The companies studied are companies engaged in the manufacturing, food, and beverage sectors. This sector was chosen because it has an important role in economic growth in Indonesia, one of the triggering factors is the increasing consumption rate and lifestyle changes. Based on Indonesia Stock Exchange Report, the manufacturing sector is also the second largest sector after the financial sector, which recorded a market capitalization of 12.88% in 2021. Manufacturing companies have large operational costs to run their business, thus the potential for earnings management. The purpose of this research is to obtain empirical evidence of whether or not there is an effect of Financial Leverage, Sales Growth, Firm Size, and Composition Committee Audit on earnings management.

II. REVIEW OF LITERATURE

Research conducted by Jensen and Mecking (1976) suggests that agency relationships arise when one or more principals employ other individuals as agents to become representatives and then they were delegated to have authority in making decisions. Other problems such as asymmetry information can also occur. This can occur because the agent had obtained more total information than the principal. Therefore, the agent can have the motivation in withholding the latest information from investors to prevent adverse effects in presenting the financial reports. Reporting the profits of the company is also the responsibility of the agent to the principal. The reported profits must be presented transparently because it is one of the aspects used by investors in predicting the profit they will get (Alves, 2014).

Signaling Theory explains that there is an assumption that the information provided by the management is received with different contents. This theory explains that the management of the company will inform stakeholders when the company reports good things, for example, the increase in sales value. However, the information recipients do not trust the reports provided by company managers because they think managers have their own goal of obtaining their own satisfaction. This is reinforced by research conducted by Marlina (2022), stating that signaling theory is a theory that provides logical consequences that managers' encouragements are to give signals to get profit. So it can be concluded that signaling theory discusses how managers should convey the success and failure information to the stakeholders. Signals or information are conveyed through financial reports, which contain information about profit-making conservatism accounting.

Financial reports are important sources of information for companies, which are the results of accounting processes that are useful in describing business results in a certain period. According to Darmawan (2020), financial reports simply present information about the activities of a company that functions in assessing the condition of a company, and its performance. In addition, financial reports are also a benchmark regarding the responsibility of managers for the resources they managed in a certain period. The objectives of the financial statements according to PSAK No. 1 The 2017 revision are to provide information regarding changes and financial positions that are useful for other parties in making economic decisions.

Earnings management can be interpreted as a policy implemented by managers and has a real effect on company profits with specific goals (Scott, 2009). According to Marai and Pavlovic (2013), there are two main characteristics of earnings management. First, earnings management actions taken by managers are actions taken consciously and deliberately, with the aim of manipulating the earnings presentation report. Second, in its application, earnings management can be carried out from the accounting system and the transactions that occurred in the company's operations. Therefore, earnings management can occur when managers use policies in reporting the financials, to make changes to income or profit levels in an effort to give a good impression to stakeholders. Companies that are indicated to practice earnings management in their financial statements will make financial statements biased and disturb users of financial statements who trust the financial reports that have been manipulated (Setiawati and Na'im, 2000). Patterns in practicing earnings management according to Scott (2009) are classified into four, namely taking a bath, income minimization, income maximization, and income smoothing. Various previous researches have concluded that there is an effect between Financial Leverage, Sales Growth, Firm Size, and Committee Audit Composition in the practice of Earnings Management in a company. The following are previous researches that were used to strengthen the theoretical basis for this research.

No.	Researchers	Results
1	Simon, F., Devi, C. M., Ariani, Y., & Winata, H. A. (2022)	This research is to analyze whether there is an effect on earnings management application in company performance. The earning management proxy used is real earnings management, which is proxied by discretionary expenses. For company performance, it will be proxied by ROA. The results of the research showed that earnings management (real) has a significant effect on the company's financial performance.
2	Apriadi, R., Angelina, R. P., Firmansyah, A., & Trisnawati, E. (2022)	The summary results of this research are: Sales growth has a negative effect on earnings management. Financial leverage has a positive effect on earnings management. Profitability has a positive effect on earnings management. And firm size has a negative effect on earnings management.
3	Fahmie, A. (2018)	The summary results of this research are: Profitability has a significant effect on earnings management. Leverage does not affect earnings management. Ownership structure has a significant effect on earnings management. Sales do not affect earnings management. Independent commissioners do not affect earnings management
4	Bassiouny, S. W. (2016)	This research analyzed the effect of company characteristics on earnings management. The summary results of this research are that Leverage has a significant positive effect on earnings management. While the other variables used do not affect earnings management.
5	Asitalia, F., & Trisnawati, I. (2017)	This research analyzed the effects of good corporate governance and Leverage on earnings management. The summary results of this research are that only Leverage affects earnings management.
6	Agustia, Y. P., & Suryani, E. (2018)	This research analyzed the firm size, the effect of firm size, firm age, leverage, and profitability on earnings management. The summary results of this research showed that firm age and leverage have a significant positive effect on earnings management. Meanwhile, firm size and profitability do not affect earnings management.
7	Anindya, W., & Yuyetta, E. N. A. (2020)	The results of this research, of the four variables used in the research, only sales growth has a significant positive effect on earnings management.
8	Edison, A., & Nugroho, A. P. A. (2020)	Analyzed whether there is an effect between leverage and sales growth on earnings management. The results of this research on the two variables used affect earnings management.
9	Irawan (2019)	This research concluded that firm size has a significant effect on earnings management in manufacturing companies. Meanwhile, inventory management and leverage do not have a significant effect on earnings management.
10	Abdul Rahman, R., & Haneem Mohamed Ali, F. (2006)	This research analyzed the effect of the board of directors' characteristics, audit committee, concentrated ownership, and cultural characteristics on earnings management. There is only one variable that has a relationship with earnings management, namely board size.

III. RESEARCH METHOD

This research was conducted to analyze the effect of Financial leverage, Sales Growth, Firm Size, and Audit Committee Composition on earnings management in food and beverage sub-sector companies. The object of this research is a manufacturing company in the food and beverage sub-sector, and the subject is financial reports and annual reports for the period 2018 – 2022. The quantitative data in this research were obtained from annual reports and financial reports. The secondary data were obtained by using a purposive sampling method in which the researcher chose the samples that were the most relevant and met the research criteria and also used a literature study where the researcher collected information for a theoretical basis and as a guide by reading and studying various kinds of literature such as books, articles, and journals. There are 84 companies listed in 2022, and 27 companies listed on the IDX from 2018 to 2022. While 19 companies were used as research samples. The research data is a combination of cross-section and time series data with quantitative testing. For analysis and hypothesis testing, panel data regression analysis was used by using the Microsoft Excel application and STATA V.14 (Software for Statistics and Data Science).

IV. RESULT AND DISCUSSION

Model Specification and Assumption Test

The Chow test was conducted to determine which model to use in the research, between the Common Effect or Fixed Effect models. Based on the statistical results, it can be concluded that the Prob value is greater than the significance value, where 0.139 > 0.05. These results indicate that in this test, the model that fits the research data is Common Effect or H0 is accepted. The Hausman test was carried out to determine which model to be used in the research, whether Fixed Effects or Random Effects. From the test results, it can be concluded that the Prob > chi2 value indicates a value that is greater than the significance value, namely 0.8325 > 0.05. These results mean that the model used in this research is Random Effect or H0 is accepted. The Lagrange Multiplier test is a test to determine which model is the most appropriate to be used in this research, whether Common Effect or Random Effect. Statistical results from the Lagrange Multiplier Test state that the most appropriate model used in this research is the Common Effect. This can be seen from the value that is greater than the significance level, namely 0.1778 > 0.05. So in conclusion, in this research, the regression model used is the Common Effect model.

The Normality test aims to determine whether the residuals in a regression model have a normal distribution or not. The results of the normality test are seen from the observation of the skewness and kurtosis values. The data provided can be said to be normally distributed if the skewness value is between -3 to 3, and for kurtosis, the value is less than 10. This statistical output shows the results of the normality test which shows that the variables used in the research have met the normality assumptions because it can be seen from the skewness and kurtosis values that are in accordance with the provisions, so there are no numbers that exceed the requirements that the data has been properly and normally distributed. Multicollinearity test is carried out to provide information that there is no correlation or connection between each variable (Ghozali, 2018). The provisions applied to this test are using the Variance Inflation Factor (VIF) limit value. The data used do not indicate multicollinearity if the VIF value is < 10, and the 1/VIF value is above 10%. Based on the results of the multicollinearity test, it can be interpreted that the VIF values for all variables obtained after processing the data comply with the requirements or criteria where the VIF value is not more than 10 or the 1/VIF value is more than 0.10. So, it can be concluded that the research data is free from multicollinearity problems. The autocorrelation test aims to detect a correlation between the confounding errors in the current period (t) and the previous period (t-1) in a regression model. Autocorrelation problems can occur due to data correlation in an over-time successive observation because residual values are not independent between observations. The Durbin-Watson value of this research is 0.570 which is between -2 < dw < 2. It can be concluded that the data does not experience autocorrelation errors. The heteroscedasticity test is used to test whether there is an unequal variance between the residual values. The criteria used in this test is the Breusch Pagan / Cook-Weisberg Test. From the results of the heteroscedasticity test, it is known that the Prob > Chi2 value is greater than the significance level of 5%. The provisions are, if the Prob > Chi2 value is greater than the significant value, then the data in this research are not affected by heteroscedasticity problems. It can be concluded that the research data is safe and not affected by heteroscedasticity problems.

Hypothesis testing

Test the Coefficient of Determination

The purpose of the Determination Coefficient Test is to show the magnitude power of the independent variables in providing information to explain the dependent variable. The coefficient of determination ranges from 0 to 1, the closer the value is to 1, the greater the effect of the determination of the regression model on all independent variables on the dependent variable.

R-Squared	0,3105
Sig.	0,05

Based on the test results for the coefficient of determination above, using a proxy value of R-Squared 0.3105 or 31.05%, which means the ability of the independent variable; Sales Growth, Financial Leverage, Firm Size, and Composition Committee Audit can affect earnings management in a company. And the remaining value of 68.95% is affected by other factors that are not used as independent variables in this research.

Individual Parameter Significance Test (T-Test)

Partial hypothesis testing using the T-test aims to see how significant the independent variable is to the dependent variable. The significant test in this research was carried out by comparing the significant value with alpha. The significance level used was 5%.

Common Effect Model			
Variable	*Coefficient*	*t*	*Prob > |t|*
_cons	-6,5294	-16,88	0,000
SG	-0,3509	-2,40	0,018
FL	0,1011	1,93	0,057
FS	-0,1017	-5,28	0,000
CCA	0,0085	0,10	0,923

Multiple Linear Regression Test

Multiple linear regression analysis is used to analyze the magnitude of the correlation and the effect of the independent variables which are more than two. In this research, to determine the magnitude effect of the independent variables, namely Sales Growth (SG), Financial Leverage (FL), Firm Size (FS), and Composition Committee Audit (CCA) on the dependent variable, namely Earnings Management (EM) with the regression model as follows: $EM = \alpha + \beta 1SG + \beta 2FL + \beta 3FS + \beta 4CCA + \varepsilon$. Then it can be arranged for sales that the regression is $EM = -6.5294 + (-0.3509)\ SG + 0.1011\ FL + (-0.1017)\ FS + 0.0085\ CCA + \varepsilon$. The Chow test was conducted to determine which model to use in the research, between the Common Effect or Fixed Effect models. Based on the statistical results, it can be concluded that the Prob value is greater than the significance value, where 0.139 > 0.05. These results indicate that in this test, the model that fits the research data is Common Effect or H0 is accepted. The Hausman test was carried out to determine which model to be used in the research, whether Fixed Effects or Random Effects. From the test results, it can be concluded that the Prob > chi2 value indicates a value that is greater than the significance value, namely 0.8325 > 0.05. These results mean that the model used in this research is Random Effect or H0 is accepted. The Lagrange Multiplier test is a test to determine which model is the most appropriate to be used in this research, whether Common Effect or Random Effect. Statistical results from the Lagrange Multiplier Test state that the most appropriate model used in this research is the Common Effect. This can be seen from the value that is greater than the significance level, namely 0.1778 > 0.05. So in conclusion, in this research, the regression model used is the Common Effect model.

DISCUSSIONS

The Effect of Sales Growth on Earnings Management

From the results of the previous discussion, it is known that the Sales Growth variable has a significant effect, with a negative direction. So it can be concluded that H1 is accepted, which means that there is an effect of Sales Growth (X1) on Earnings Management (Y). This means that if sales growth has increased, earnings management has decreased, and vice versa. Companies that have high sales growth have a lower probability of carrying out profit manipulation actions in their financial statements. This is because, with a good level of sales growth, the opportunistic actions of managers to falsify performance results by increasing the results of net sales are not needed. This statement is supported by research conducted by Anindya & Yuyetta (2020); Destiana, S. (2020); and Harni, et al. (2022). The results of this research are in contrast to research conducted by Handayani & Rachadi (2009); Hapsoro and Anisa (2017); and Harahap (2021) with the result that the sales growth variable has a significant positive effect on EM. It is stated that companies with high sales growth rates also have the motivation in carrying out earnings management when faced with problems to maintain profit trends and sales trends. In some cases, a manager is also motivated to increase the sales growth rate for the selected period so that the company is considered to have good and stable performance, so that managers get incentives for their performance, as well as attract investors to invest.

The Effect of Financial Leverage on Earnings Management

From the results of the previous discussion, it is known that the financial leverage variable calculated using the Debt to Equity Ratio has no significant effect. So it can be concluded that H2 is rejected, which means there is no effect of Financial Leverage (X2) on Earnings Management (Y). This means that if the company has high leverage, the earnings management actions taken by managers will be constant. This statement is supported by research conducted by Fahmie (2018); and Anindya & Yuyetta (2020). If it is seen from the average value of the FL variable in the descriptive statistics table, it shows a value that is still safe because it is still below 100%. It can be concluded that the food and beverage sector studied in this research has safe leverage, which means that the company is able to pay off its debts which are used to finance company assets. Then managers do not need to take action to manipulate financial statements to create secure corporate value. This research is inversely proportional to the research conducted by Asim & Ismail (2019), which states that the FL variable has an effect on earnings management. Companies that have a high level of leverage are said to be insolvable, which means that these companies have higher debt compared to their wealth, which makes funding dominated by debt (credit). Having a high level of leverage means diverting funding from loan sources to equity sources. Thus, companies must create a good image by reporting good financial performance and high profits to attract potential investors.

The Effect of Firm Size on Earnings Management

From the results of the previous discussion, it is known that the Firm Size variable has a significant effect, with a negative direction. So it can be concluded that H3 is rejected, which means there is an effect of Firm Size (X3) on Earnings Management (Y). This means that the greater the total assets of a company, the lower the occurrence of earnings management. This statement is supported by research conducted by Jao & Pagalung (2011); Herlambang & Darsono (2015); Pahmi (2018); and Purnama & Taufiq (2021) that companies with greater value will be more thorough and careful when reporting their financial conditions because they receive more attention from the wider community compared to smaller companies. The greater the assets owned by the company, the more capital invested, the higher the level of sales, and the higher the velocity of money, so that the market capitalization becomes greater. The high market cap of a company indicates that the company is known by the wider community. In line with the signaling theory, high attention from external parties only occurs in companies with large asset values. So it can be concluded that companies will avoid earnings management practices in order to avoid damaging the company's reputation. Another research conducted by Anindya & Yuyetta (2020) states that there is no effect between firm size on earnings management.

The Effect of Composition Committee Audit on Earnings Management

From the results of the previous discussion, it is known that the CCA variable has no significant effect. So it can be concluded that H4 is rejected, which means there is no effect of Composition Committee Audit (X4) on Earnings Management (Y). Unlike the research conducted by Xie, et al. (2003) and NgO & Le (2021) which stated that the number of audit committees that have a financial background in a company will reduce earnings management actions. The statement that the composition of the audit committee has no effect on earnings management is supported by research conducted by Herlambang & Darsono (2015); Vajriyanti, et al. (2016); Asitalia & Trisnawati (2017); and Idris & Natalylova (2021). As stipulated in Kep-643/BL/2012 that the composition of the audit committee in a company consists of at least three members who are from independent commissioners and parties outside the issuer, or a public company. Other than that in the Financial Services Authority Regulation Number 55/POJK.04/2015 concerning the Establishment and Guidelines for the Implementation of Audit Committee Work. For company management, the existence of an audit committee is crucial because it is a component and company control system, as well as a liaison between stakeholders and management. With these rules in place, the existence of an audit committee in a public company is considered only as a fulfillment of mandatory regulatory requirements (Effendi, 2009), therefore, in the implementation, it becomes less effective in minimizing the opportunistic actions of managers in implementing earnings management.

V. CONCLUSIONS AND SUGGESTIONS

The results of the analysis and discussion of the hypothesis testing that has been conducted previously have obtained the following research conclusions:

1) The characteristics of the company proxied by Sales Growth which is calculated by the ratio of the comparison between Net Sales of the current year and the previous year shows a significant effect in a negative direction on Earnings Management which is calculated by the Real Earnings Management method. This is proven through the results of panel data regression analysis. Thus, it can be concluded that sales growth has a significant negative effect on Earning Management in food and beverage manufacturing companies listed on the IDX for the 2018 – 2022 research period.
2) Financial Leverage calculated using the Debt to Equity Ratio shows no effect on Earnings Management which is calculated using the Real Earning Management method. This is proven through the results of panel data regression analysis. Thus, it can be concluded that financial leverage has no effect on Earning Management in food and beverage manufacturing companies listed on the IDX for the 2018 – 2022 research period.
3) Characteristics of the company proxied by firm size which is proxied by the neutral logarithm of the company's total assets shows a significant effect in a negative direction on Earnings Management which is calculated using the Real Earning Management method. This is proven through the results of panel data regression analysis. Thus it can be concluded that firm size has a significant negative effect on Earning Mannagement in food and beverage manufacturing companies listed on the IDX for the 2018 – 2022 research period.
4) Audit Committee proxied by the total number of audit Committee members in the company shows no effect on Earnings Management which is calculated using the Real Earnings Management method. This is proven through the results of panel

data regression analysis. Thus, it can be concluded that audit committee composition has no effect on Earning Management in food and beverage manufacturing companies listed on the IDX for the 2018 – 2022 research period.

Based on the results of the analysis and evaluation in the previous chapter, a theoretically tested picture of the performance level of manufacturing companies from the food and beverage sub-sector was obtained using panel data regression analysis. This research is expected to be a contribution to companies in related fields, as well as being used as a reference by management in making decisions in the future. For companies, it is expected to increase integrity and carry out supervision in order to minimize opportunistic activities of profit manipulation, as well as improve company performance so that the desired profit is achieved. It is better for investors to be more selective by paying attention to the condition of the company's performance. For future researchers, it is suggested to use other models in calculating earnings management in order to have another view on the effect of the independent variables used in research on Earnings Management. Furthermore, it is recommended to expand the use of the test sample by adding or using other independent variables in order to gain additional new insights about the variables that affect earnings management.

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