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Effect of Board of Commissioners and Audit Committee on Earning Management

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***Abstract*—Earning Management is actions taken through the choice of accounting policies with the aim to fulfilling own interest or increasing the market value of company. The aim of this research is to analyze the influence of board of commissioners and audit committee to the earning management in bank sub sector manufacturing companies listed on Indonesia Stock Exchange. This research with quantitative method. Populations of this research are bank subsector manufacturing companies listed on Indonesia Stock Exchange in 2015-2017. This research uses purposive sampling method and analysis used multiple linear regression. The result show that board of commissioners and audit committee not significantly effect on earning management of bank companies listed on Indonesia Stock Exchange.**

Keywords: earning management, board of commissioners, audit committee

I. INTRODUCTION

Financial statements are one component to measure financial performance. Financial statements are the end result of a series of accounting processes that are sources of information for users of financial statements including information about profits therein. Profit is an important information for external and internal parties contained therein regarding management accountability. By making profits a performance evaluation parameter, it encourages management to practice earnings management.

Earnings management is an action taken through the choice of accounting policies to obtain certain objectives, namely to meet their own interests or increase the company's market value [1]. To prevent uncontrolled earnings management, a mechanism which is able to balance the interests of the parties in the company is needed. The mechanism in question is corporate governance.

Corporate governance is a process and structure used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability [2]. Corporate governance is also defined as a set of mechanism by which outside investor protect themselves against expropriation by insiders [3].

The collapse of WorldCom (USA), Enron (USA), Parmalat (Italy), and Air New Zealand (Australia) brought to the fore the failure of the governance process, and this contributed to the emphasis on board composition. Later, in 2008, the financial meltdown that was triggered by the collapse of major firms globally led to the attention on administrative wage and board independence. This heightened anxiety for accountability, controlling, transparency and which led to the firm and board governance/effectiveness especially among big firm issues all over the world [4].

One of the internal elements of corporate governance is managers. Managers are using earnings management to maximize company’s interest (shareholders interest) or to maximize their own interest, this causes an agency problem [5].

The function of the board of commissioners is as supervisors and advisers to managers (directors) on behalf of the shareholders. Controlling by the board of commissioners will increase of confidence that management has acted in the interests of shareholders. This is because the board of commissioners is appointed by shareholders so they must represent the interests of shareholders in controlling management's actions [6].

An audit committee is a sub-committee of the board that specializes in, and is responsible for, ensuring the accuracy and reliability of the financial statements provided by management. The audit committee serves as a liaison between the external auditor and the board of directors, and facilitates the monitoring process by reducing information asymmetry between the external auditor and the board [7].

Audit committee effectiveness essentially functions on audit committee characteristics. The perfect size of audit committee was supported by combination of experiences and skills. That also support the audit committee ability to detect and prevent earning management [8].

II. RESEARCH METHOD

This research with quantitative method, because the purpose is to determine the effect of board commissioners and audit committee on earning management.

Populations of this research are bank companies listed on Indonesia Stock Exchange in 2016-2018. The data in this research used secondary data and the data retrieved from Indonesia Stock Exchange website. The sample of the study was 33 banks with using the purposive sampling method. Testing hypothesis is by using multiple regression method.

The variables in this study consisted of two independent variables namely board of commissioners and the audit committee while the dependent variable was earnings management. The board of commissioners is measured by counting the total number of board members [6]. This is similar to what Murtini et.al [9] did. For the audit committee variable is measured by counting the number of audit committee members. Earnings management as the dependent variable, measured using the Discretionary Accrual method with the Jones Model [8].

III. RESULTS

Based on statistical data processing results, it can be seen the result of normality test in the table 1.

TABLE I. NORMALITY TEST RESULT

Variable	Sig.
Asymp. Sig. (2-tailed)	0,097

Source: data processing result

Based on the results of the normality test with Kolmogorov - Smirnov, it is known that the Asymp sig (2-tailed) value is greater than the significance value of 0.05 (0.097> 0.05). This means that the regression model in this study is normally distributed so that the normality test is fulfilled.

Multicolinearity test was conducted to check whether there was a correlation between the independent variables which will mislead the result of the study. The result of multicolinearity test can be seen in table 2.

TABLE II. MULTICOLINEARITY TEST RESULT

Variable	VIF
Board of commisioners	4,274
Audit committee	1,116

Source: data processing result

The multicollinearity test results showed that the Variance Inflation Factor (VIF) value of the board of commissioners and audit committee was smaller than 10 (VIF <10). It can be concluded that this study did not occur multicollinearity.

TABLE III. HETEROSCEDASTICITY TEST RESULT

Variable	t-count
Board of commisioners	0,698
Audit committee	0,405

Source: data processing result

Based on the results of the Glejser test as shown in the table above, the significance value of all independent variables is more than 0.05. Thus it can be concluded that there were no symptoms of heteroscedasticity in the regression model of this study.

TABLE IV. AUTOCORRELATION TEST RESULT

Variable	Sig.
Asymp. Sig. (2-tailed)	0,176

Source : data processing result

Based on the results of the autocorrelation test with the Run Test in the table above, an Asymp value is obtained. Sig (2-tailed) is 0.176. This value is greater than the significance level of 0.05 (0.176 > 0.05). So it can be concluded that there was no autocorrelation in the regression model in this study.

TABLE V. MULTIPLE REGRESSION ANALYSIS RESULT

Model	Unstandardized coefficient (B)
Constant	0,208
Board of commissioners	-0,008
Audit committee	-0,011

Source: data processing result

Multiple linear regression analysis with a significance level of 5% obtained the following equation:

$$\mathbf{Y = 0{,}208 - 0{,}008X1 - 0{,}011X3} \quad (1)$$

The equation shows that the independent variable consisting of the board of commissioners, and the audit committee has a negative coefficient. This means that the increasing number of boards and audit committees is not able to reduce earnings management in the company.

TABLE VI. T-TEST RESULT

Variable	t-count	t-table	Sig.
Board of commissioners	-0,882	1,987	0,380
Audit committee	-0,056	1,987	0,294

Source: data processing result

Based on the calculation results in the table presented, it is known that the board of commissioners has a t count of – 0,882 smaller than t table 1,987 and a significance value of 0,380 (0,380> 0,05). Therefore, it can be concluded that the board of commissioners had no effect on earnings management, H1 was rejected. Based on the calculation results in the table presented, it is known that the audit committee has a t-count of -0,056 smaller than t table 1,987 and a significance value of 0,294 (0,294> 0,05). Therefore, it can be concluded that the audit committee has no effect on earnings management, H1 was rejected.

TABLE VII. COEFFICIENT OF DETERMINATION TEST RESULT

Model	Adjusted R Square
1	0,053

Source: data processing result

Based on the table presented, an adjusted R^2 value of 0.053 was obtained. This means that variations in earnings management variables can be explained by the variables of the board of commissioners and audit committee of 5.3% while the remaining 94.7% is explained by other variables.

IV. DISCUSSION

The results showed that the board of commissioners had no effect on earnings management. This proves that the large number of board of commissioners has not been proven to be able to conduct good supervision in reducing earnings management. This result of this study contradicted with the results of Sumanto's research [8], that the size of the board of commissioners is able to influence earnings management. With a small number of the board of commissioners so many more earning management's actions. It is happened because of the lack of board of commissioner makes it possible for the organization to be dominated by management in carrying out its role.

Similar to a board of commissioners, the audit committee has no effect on earnings management. The average company has 3 audit committees in accordance with the conditions set by Financial Service Authority in Indonesia. This is done only to comply with Financial Service Authority regulations. While there are some corporate audit committees whose educational backgrounds are not as they should be, such as from the military and law. The results of this research are in line with research by Mansor et.al [2] and Khosheghbal et.al [10].

V. CONCLUSIONS

Based on the result of testing process that has been done, the conclusions are the board of commissioners and audit committee have no effect on earnings management in bank sub sector companies listed on the Indonesia Stock Exchange.

Based on the conclusions presented, some of the suggestions are recommended. The research population is limited by bank companies. The next researcher is expected to be able to increase the number of research subjects and the observation period so that the research results can approach the actual conditions. The next researcher is expected to be able to test other variables that are considered to affect earnings management, such as the age of the board of commissioners, the number of audit committee meetings, institutional ownership, etc. This is because the adjusted R^2 value is relatively low, which is 5.3%.

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