

Role of Independent Commissioner in Moderating Factors That Affect Earnings Response Coefficient

Siti Azizah¹, Linda Agustina^{1,*}, Kuat Waluyo Jati¹

¹ Department of Accounting, Faculty of Economics, Universitas Negeri Semarang

*Corresponding author. Email: lindaagustina@mail.unnes.ac.id

ABSTRACT

This research aims to examine the influence of Corporate Social Responsibility (CSR), accounting conservatism, growth opportunities, and default risk on Earnings Response Coefficient (ERC) with independent commissioners as moderating variables. The population of this research is the manufacturing companies in IDX in 2016-2018. Sampling techniques was conducted using purposive sampling methods and obtained 59 companies with 114 units of analysis. The analytical method used is moderation regression analysis with absolute difference value test. The results showed that CSR has a positive effect on ERC, and default risk has a negative effect on ERC, while accounting conservatism and growth opportunities have no significant effect on the ERC. The presence of an independent commissioner is able to strengthen the influence of growth opportunities on the ERC but is unable to moderate the effect of CSR, accounting conservatism, and default risk on the ERC. The conclusion from this research is that ERC will increase if CSR increases and will decrease if there is a high default risk in the company. Independent commissioners have an important role in supporting the relationship between growth opportunities and ERC.

Keywords: *Corporate Social Responsibility, Accounting Conservatism, Growth Opportunities, Default Risk, Independent Commissioner, Earning Response Coefficient*

1. INTRODUCTION

One of the important components in financial statements is information about earnings. The company's published earnings can provide a varied response, this indicates a market reaction to the earnings information. Published earnings information can be either good news or bad news. Good news occurs when the company's actual profit is higher than estimated profit made, so investors will decide to buy shares and the company's share price will increase. When there is a decrease in profit, it is not always followed by a decrease in share price [1]. This condition can be observed in PT Indocement Tunggul Perkasa TBK (2017), PT Indofood Sukses Makmur Tbk (2018), and PT Argha Karya Prima Industri Tbk (2018) which shows a phenomenon when profit increase or decrease not necessarily followed by an increase or decrease in the company's share price, meaning that investors do not respond to this information quickly. Therefore, it becomes interesting to study what caused this to happen.

The Earnings Response Coefficient (ERC) level in Indonesia is still low, the average ERC of manufacturing

companies listed on IDX in 2018 is only -0.0688[2]. The average value of IDX-listed manufacturing companies in 2013-2014 was -8,518[3]. A low ERC value indicates that earnings are less informative for investors in making decisions so that at the time of publication of earnings information, most investors tend to be less responding to the profit presented. The phenomenon shows that the height of ERC is not only influenced by financial factors but can be influenced by other factors.

Previous research has been conducted to test earning responses coefficient, but the results found on these tests provide still mixed results ([3]; [4]; [5]; [1]; [6]; [7]; [8]; [9]; [10]; and [11]). This research aims to examine the influence of CSR, accounting conservatism, growth opportunities and default risk on ERC. The originality of this study presents independent commissioner as a moderating variable. Based on the agency theory, the board of commissioners is considered the highest control mechanism responsible for monitoring management actions [12]. Supervision from independent commissioners is expected to reduce the actions of deviant managers to increase investor confidence in the company.

CSR shows that the company's responsibility is not only to shareholders but also to the stakeholders who are affected by the company's existence [13]. The signaling theory underlies that CSR disclosure will be a positive signal for investors. CSR describes the company's responsibility towards the environment to increase investor confidence in the company. Built-up investor confidence can increase the investment that goes into the company so that the share price will increase; this indicates an increase in the value of ERC. This statement is supported by [3], [14], and [15] stating that CSR has a positive effect on the ERC.

H₁: Corporate Social Responsibility has a positive effect on the earnings response coefficient.

Accounting conservatism is a reaction or prudence in the face of uncertainty [16]. Accounting conservatism causes understatement in the current period and overstatement in the later period [1]. Based on the signalling theory, information regarding the company's profit will provide a signal for investors. Profit information resulting from the application of conservative principles is considered inaccurate because it has a lower information content, this causes investors to not response to the earnings information. The higher level of corporate accounting conservatism, the lower response that will be given by investors so that the ERC will be low. This statement is accordance with research [16] and [6], which states that accounting conservatism negatively affects the ERC.

H₂: Accounting conservatism has a negative effect on the earnings response coefficient

Growth opportunities describe the company's ability to obtain potential funding [8]. A company with good level of growth opportunity is good news for investors because the company is considered to have an effective performance. Based on signaling theory, good news and bad news published by the company will give a signal to investors. Companies with a high level of growth opportunities are good news for investors because they are considered to have an effective performance. Investors expect a better return to companies with high level of growth. The level of company's growth opportunities will attract investors to increase of ERC value. The statement is supported by [8] and [3].

H₃: Growth opportunities have a positive effect on the earnings response coefficient

Default risk reflects the condition when the debtor unable to pay off the obligation plus interest in accordance with the agreed agreement. Based on the signal theory, investors will trust companies with a low default risk rate because they are considered capable of providing a return on their invested funds. [11] states that companies that have high levels of debt, increased profits are believed only to strengthen the position and security of bondholders rather than shareholders. This causes

investors to be slow to react to the company's published earnings information. The higher the default risk, the lower the ERC value [17]. The statement is following research [10] which states default risk negatively affects ERC.

H₄: Default risk has a negative effect on the earnings response coefficient

High CSR disclosure by companies reflects that the company is responsible for the environment. According to the agency's theory, management will try to get a good view of stakeholders. Independent commissioner in charge of ensuring the implementation of Good Corporate Governance (GCG) which is expected to encourage the company to be more transparent in conducting its business activities. With this, investor confidence will increase so that independent commissioners who carry out their duties properly will strengthen the effect of CSR on ERC which can be seen from investors considering CSR information in decision making and this will increase the value of ERC.

H₅: Independent commissioner strengthens the influence of Corporate Social Responsibility (CSR) on earnings response coefficient

The application of accounting conservatism causes the resulting profit to be less qualified because earnings information does not reflect the actual situation. Independent commissioner is expected to ensure that the implementation of the principle of conservatism within the company following the prevailing accounting standards, so that the resulting earning information is not misleading for investors or stakeholders. With the supervision of the independent commissioner, it is expected that the earning information will reflect the actual condition so that it will be a signal for investors in decision making. A positive response from investors can increase ERC value.

H₆: Independent commissioner weakens the influence of accounting conservatism on earnings response coefficient

Growth opportunities describe the company's future prospects. Higher level of growth opportunities can increase investor confidence in the company. Companies with high growth opportunities need more funds expand [18]. Nevertheless, on the other side investors expect a high return. Based on agency theory, the independent commissioner are a principle who expected to serve as a tool to give investors confidence that they will receive a return on the funds they invest [19]. The existence of good supervision will improve the result of company performance so that it can increase the company's growth opportunities, so that independent commissioners are able to strengthens the influence of growth opportunities on ERC.

H7: Independent commissioners strengthens the effect of growth opportunities on earnings response coefficient

Companies with high default risk reflect the use of high debt in those companies. The higher default risk level is lower the ERC value. Independent commissioner based on the agency's theory can confidence that investors will receive a return on the funds they have invested. The supervisory mechanism of the independent commissioner will oversee the optimal level of debt for the company so that the interests of shareholders relating to dividends and others are not less than what the company provide to creditors. This is expected to increase investor confidence in the company.

H8: Independent commissioners weaken the effect of default risk on earnings response coefficient

2. METHOD

This research is quantitative research. The data used in this research is secondary data. This research data is taken from annual report of manufacturing companies listed on the Indonesia Stock Exchange with three years of observation. The data was obtained from the company's website, yahoo finance, and IDX. Then, the data analysis was carried by testing the absolute value difference with a significant level of $\alpha=5\%$. The samples were determined by purposive sampling techniques and obtained a sample of 59 companies with 114 observation units.

The definition of the variable tested is as follows, earning response coefficient (ERC) is a measure the level of abnormal return on stockin response to unexpected earnings reported by the company issuing securities [20]. CSR is social commitment from the company as a form of corporate concern for the community and also environmental sustainability and responsibility for the welfare of the company's workforce in the company's business practices [13]. Accounting conservatism (KONS) is a prudent action principle in face of uncertainty in the company [11]. Growth opportunities (GROWTH) market assessment of the growth possibilities of a company [21]. Default risk (DEFAULT) shows the company's failure to pay off interest and loans on time [16]. Independent Commissioner (KI) is a commissioner who is not from an affiliated party [12].

3. RESULT AND DISCUSSION

Table 1 shows the results of the descriptive statistical variables tested in this study. The of classic assumptions test have also been carried out and shows the results that sample data is normally distributed, free of multicollinearity, no autocorrelation, and no heteroscedasticity. The result of hypothetical testing in this study were obtained by an absolute difference test

with a significance level of 0.05 which can be see in table 2.

The Effect of Corporate Social Responsibility (CSR) on Earnings Response Coefficient (ERC)

Corporate Social Responsibility (CSR) has a positive effect on ERC. The results of this study are in line with signalling theory. Investors as one of the company's Stakeholders feel given the facilities of sufficient information about the company's activities, both social and financial, so that it will increase investors response to earning information [3]. Positive response from investors in investment decision making will increase the ERC. The results of this study are consistent with [3], and [15], which provide empirical evidence that CSR has a positive effect on ERC.

The Effect of Accounting Conservatism on Coefficient Earnings Response

Accounting conservatism has no affect the ERC. The results of this study show a discrepancy with signaling theory. Based on data tabulation of this research, PT Garuda Metalindo Tbk in 2018 had the highest level of conservatism in this research sample, which is 0.36 and had a high ERC value of 0.23. The ERC value exceeded the average ERC value of the sample companies in the observation year, which is -0.15. This shows that investors tend to no longer see accounting conservatism as a consideration in investment decision making. The results of this study are consistent with [8] and [11] which state that accounting conservatism has no affect ERC.

The Effect of Growth Opportunities on Earning Response Coefficient

Growth opportunities have no effect on ERC. The results of this study indicate discrepancy with signalling theory. Based on the tabulation of research data, the average growth opportunities of manufacturing companies in 2016-2018 have decreased, where in 2016 it was 1.12, in 2017 decreased by 1.11 and in 2018

Table 1. Descriptive Statistic

Variable	N	Min	Max	Mean	Std. Deviation
ERC	114	-3.66	3.51	-.16	.904
CSR	114	.01	.13	.06	.028
KONS	114	-.28	.36	-.02	.078
GROWTH	114	.0001	3.17	1.09	.261
DEFAULT	114	.08	2.05	.50	.391
KI	114	.25	.80	.40	.102
Valid N (listwise)	114				

Source: Secondary data processed, 2020

Table 2. Summary of Hypothesis Test Results

	Hypothesis	Regression Coefficient	Sig	Decision
H₁	Corporate Social Responsibility has a positive effect on the Earnings Response Coefficient.	0.161	0.045	Accepted
H₂	Accounting Conservatism has a negative effect on the Earnings Response Coefficient	0.064	0.411	Rejected
H₃	Growth Opportunities has a positive effect on the Earnings Response Coefficient	0.074	0.373	Rejected
H₄	Default Risk has a negative effect on the Earnings Response Coefficient	-0.270	0.004	Accepted
H₅	Independent commissioner strengthens the effect of Corporate Social Responsibility on Earnings Response Coefficient	-0.067	0.570	Rejected
H₆	Independent commissioner weakens the effect of Accounting Conservatism on Earnings Response Coefficient	-0.002	0.967	Rejected
H₇	Independent commissioner strengthens the effect of Growth Opportunities on Earnings Response Coefficient	0.367	0.000	Accepted
H₈	Independent commissioner weakens the effect of default risk on Earnings Response Coefficient	-0.158	0.154	Rejected

Source: Secondary data processed, 2020

decreased again to 1.10. The decrease was not followed by decreased in the average ERC value. The results of this study are consistent with [1] which state that growth opportunities do not affect with ERC.

The Effect of Default Risk on Earnings Response Coefficient

Default risk has negative effect on ERC. The results of this study are in line with the signalling theory. The high level of default risk causes the company's profits to flow more to debtholders or creditors so that good news on profits will be given to creditors rather than investors [1]. This cause investors to not respond to company's earning information which caused the ERC to decline. The results of this study are consistent with [10] and [22] which state that default risk has negative effect on ERC.

The Effect of Corporate Social Responsibility on Earning Response Coefficient moderated by Independent Commissioners

Independent commissioners are unable to strengthen the influence of CSR on the ERC. The results of this study indicate a discrepancy with the agency's theory. Based on descriptive statistics, independent commissioners have an average of 0.40. This is presumably due to the existence of an independent commissioner as mandatory regulatory compliance and not intended to enforce the practice of Good Corporate Governance (GCG) [23]. So can be concluded that

independent commissioners are unable to moderate CSR influence on ERC.

The Effect of Accounting Conservatism on Earnings Response Coefficient Moderated by Independent Commissioners

The results of this study showed that independent commissioners were unable to weaken the influence of accounting conservatism on the ERC. This condition indicates a discrepancy with the agency's theory. Based on the tabulation data of this study, the average independent commissioner at manufacturing companies for the period 2016-2018 is 40%, exceeding the minimum set by IDX of 30%. The larger proportion of independent commissioners will be more difficult and expensive and take a long time in the process of communication, task coordination and effectiveness in decision making [24]. This resulted in the oversight of independent commissioners not running effectively so that independent commissioners were unable to weaken the effect of accounting conservatism on ERC.

The Effect of Growth Opportunities on Earnings Response Coefficient Moderated by Independent Commissioners

Independent commissioners are able to strengthen the effect of growth opportunities on the ERC. The results of this study are in line with the agency theory. Companies with high levels of growth opportunities require a large

allocation of funds so that the company has a low dividend rate. The supervision of independent commissioners can align the interests between the manager and stakeholders so that in decision-making management will pay attention to the interests of stakeholders. It can be concluded that independent commissioners can strengthen the influence of growth opportunities on the ERC.

The Effect of Default Risk on Coefficient Earning Response Moderated by Independent Commissioners

Independent commissioners are unable to weaken the effect of default risk on the ERC. The results of this study inconsistent with agency theory. [25] stated that investors do not pay much attention to the proportion of independent commissioners, but rather pay more attention to how the company management manages its debt effectively and efficiently to create added value for the company that can increase investor confidence in the company which can increase investor confidence in the company. So, it can be concluded that independent commissioners are unable to moderate the effect of default risk on the ERC.

4. CONCLUSION

The study examines how Corporate Social Responsibility (CSR), accounting conservatism, growth opportunities, and default risk affects on ERC with independent commissioner as moderating variable. The result of this study shows that CSR has positive significant effect on ERC and default risk has negative significant effect on ERC. While accounting conservatism and growth opportunities has no effect on ERC. Independent commissioner can strengthen growth opportunities effect on ERC.

Manufacturing companies in order to increase ERC can expand CSR disclosure and reduce the use of debt. The broader CSR can meet the needs of investor about information of the company's activities, so this is can increase the positive response from investors. The high level of debt will decrease investor confidence so that the value of ERC will decrease. Companies need to pay attention to the proportion of independent commissioners because they are able to support the relationship of growth opportunities and ERC.

The limitation of this research is that there is an element of subjectivity in the assessment of the standard GRI index in measuring CSR and using the accounting conservatism variables that was previously prevailed in the US GAAP-based SAK, but nowadays the application of accounting conservatism principle is reduced and shifted with prudence principle. Suggestion for further research is to use other proxies in measuring CSR such as corporate CSR costs and replace accounting

conservatism with prudence principles. The inability of independent commissioner as a moderating variable in this study can be replaced by other variables such as CGPI indexes issued by independent institutions to increase investor confidence in the company.

AUTHORS CONTRIBUTION

Conceptualization: Siti Azizah, Linda Agustina; Data Curation: Siti Azizah, Linda Agustina; Formal Analysis: Siti Azizah, Kuat Waluyo Jati; Writing-Original Draft: Siti Azizah, Linda Agustina; Writing-Reviewing & editing: Siti Azizah, Kuat Waluyo Jati

REFERENCES

- [1] S. W. Ghoru, "Pengaruh Konservatisme Akuntansi, Profitabilitas, Growth Opportunities, Default Risk terhadap Koefisien Respon Laba," *J. Akunt. dan Keuang.*, vol. 4, no. 1, pp. 75–84, 2019.
- [2] S. A. Faradiza, W. Setiawan, and T. bin Abad, "Dampak Konservatisme Akuntansi terhadap Koefisien Respon Laba," *J. Ris. Akunt. dan Audit.*, vol. 3, no. 2, pp. 1–14, 2017.
- [3] M. Fauzan, "Pengaruh Pengungkapan CSR, Timeliness, Profitabilitas, Pertumbuhan Perusahaan dan Risiko Sistemik terhadap Earnings Response Coefficient (ERC)," *Diponegoro J. Account.*, vol. 6, no. 1, pp. 256–270, 2017.
- [4] G. M. Abolfazl, G. S. Akram, G. S. Elahe, and M. Zakie, "Effect of The Social Responsibility on Earnings Response Coefficient," *World Sci. J.*, vol. 1, no. 10, pp. 39–49, 2013.
- [5] Y. C. Kim, I. Seol, and Y. . Kang, "A study on the earnings response coefficient (ERC) of socially responsible firms: Legal environment and stages of corporate social responsibility," *Manag. Res. Rev.*, vol. 41, no. 9, pp. 1010–1032, Jan. 2018.
- [6] A. R. Zeidi, Z. Taheri, and O. G. Farahabadi, "The Conservatism in Accounting and Its Effect on Earnings Response Coefficient in Tehran Stock Exchange Listed Companies," *Int. J. Sci. Res. Knowl.*, vol. 2, no. 1, pp. 28–37, 2014.
- [7] H. Al Awawdeh, S. A. Al-Sakini, and M. Nour, "Factors Affecting Earnings Response Coefficient in Jordan: Applied Study on The Jordanian Industrial Companies," *Invest. Manag. Financ. Innov.*, vol. 17, no. 2, pp. 255–265, 2020.
- [8] R. Syarifulloh and A. Wahyudin, "Determinan Koefisien Respon Laba," *Account. Anal. J.*, vol. 5, no. 1, pp. 1–9, 2016.
- [9] N. B. Zakaria, M. A. M. Isa, and R. A. Z. Abidin, "Default Risk and The Earnings Response

- Coefficient. Evidence from Malaysia,” *J. Basic Appl. Sci. Res.*, vol. 7, no. 2, pp. 131–137, 2013.
- [10] N. B. Zakaria, M. A. M. Isa, and R. A. Z. Abidin, “Sukuk Rating, Default Risk And Earnings Response Coefficient,” *Adv. Nat. Appl. Sci.*, vol. 7, no. 2, pp. 131–137, 2013.
- [11] T. Tania, “Pengaruh Akuntansi Konservatif, Default Risk, dan Profitabilitas terhadap Earnings Response Coefficient,” *J. Akunt.*, vol. 16, no. 1, pp. 1–24, 2015.
- [12] A. Aziz, “Analisis Pengaruh Good Corporate Governance (GCG) terhadap Kualitas Sustainability Report,” *J. Audit dan Akunt. Fak. Ekon. Univ. Tanjungpura*, vol. 3, no. 2, pp. 65–84, 2014.
- [13] V. P. et al Awuy, “Pengaruh Pengungkapan Corporate Social Responsibility (CSR) terhadap Earnings Response Coefficient (ERC),” *J. Akunt. dan Keuang.*, vol. 18, no. 1, pp. 15–26, 2016.
- [14] Y. Sayekti, “Strategic Corporate Social Responsibility (CSR), Company Financial Performance, and Earning Response Coefficient: Empirical Evidence on Indonesian Listed Companies,” in *Procedia - Social and Behavioral Sciences*, 2015, vol. 211, pp. 411–420.
- [15] M. B. Holbrook, “Corporate Social Responsibility and Earnings Response Coefficients,” *J. Financ. Account.*, vol. 14, no. 2, pp. 1–22, 2013.
- [16] Y. Diantimala, “Pengaruh Akuntansi Konservatif, Ukuran Perusahaan, dan Default Risk terhadap Koefisien Respon Laba (ERC),” *J. Telaah dan Ris. Akunt.*, vol. 1, no. 1, pp. 102–122, 2008.
- [17] D. S. Dhaliwal and S. S. Reynolds, “The of Effect Debt of on The Default Earnings Risk Response Coefficient,” *J. Storage*, vol. 69, no. 2, pp. 412–419, 2014.
- [18] M. Luo, T. Chen, and J. Cai, “Stock Return Predictability when Growth and Accrual Measures are Negatively Correlated,” *China Financ. Rev. Int.*, vol. 9, no. 3, pp. 401–422, 2018.
- [19] N. Restuningdiah, “Mekanisme GCG dan Pengungkapan Tanggung Jawab Sosial terhadap Koefisien Respon Laba,” *J. Keuang. dan Perbank.*, vol. 14, no. 3, pp. 377–390, 2010.
- [20] W. R. Scott, *Financial Accounting Theory*. Canada: PrenticeHall, 2006.
- [21] M. Farizky, “Pengaruh Resiko Kegagalan, Kesempatan Bertumbuh, dan Ukuran Perusahaan terhadap Earnings Response Coefficient (ERC) pada Perusahaan Sektor Keuangan yang Terdaftar di Bursa Efek Indonesia Tahun 2010-2012,” *J. Profita*, vol. 4, no. 2, pp. 1–10, 2016.
- [22] Y. An, “Earnings Response Coefficients and Default Risk: Case of Korean Firms,” *Int. J. Financ. Res.*, vol. 6, no. 2, pp. 67–71, 2015.
- [23] Nadirsyah and F. N. Muharram, “Struktur Modal, Good Corporate Governance dan Kualitas Laba,” *J. Din. Akunt. dan Bisnis*, vol. 2, no. 2, pp. 184–198, 2015.
- [24] D. Yermack, “Higher Market Valuation for Firms with a Small Board of Directors,” *J. financ. econ.*, vol. 40, no. 2, pp. 185–211, 1996.
- [25] M. Padmayanti, Suryandari, “Pengaruh Kinerja Keuangan terhadap Nilai Perusahaan dengan Dewan Komisaris Independen sebagai Variabel Moderasi,” *J. Ris. Akunt.*, vol. 9, no. 1, pp. 62–72, 2015.