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The Effect of IFRS Convergence toward Earnings Management with Managerial Ownership as a Moderating Variable

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Abstract
This study aims to determine the effect of IFRS convergence on earnings management using corporate governance as a moderating variable. The population in this study are manufacturing companies listed on the Indonesia Stock Exchange during the period of 2015-2017. This study used a purposive sampling method to select 38 companies with 114 units of analysis. The results indicate that IFRS convergence do not affect earnings management. The results also show that managerial ownership and auditor quality cannot moderate the influence of IFRS on earnings management. Meanwhile, the number of audit committee meetings can alter the effect of IFRS convergence on earnings management.

Keywords: *IFRS convergence; earnings management; corporate governance*

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INTRODUCTION

International Financial Reporting System (IFRS) is an international accounting standard released by the International Accounting Standard Board (IASB) which is expected to overcome the differences of local accounting standards in various countries. The implementation of IFRS in Indonesia began gradually in 2008 and effectively applied since 1st January 2012 for public companies (listed in Indonesia Stock Exchange, IDX) in Indonesia. The aim of establishing IFRS is to provide more accurate, comprehensive and timely financial information compared to national accounting standards which tend to influenced by state, political and taxation laws in a country (Ball, 2006).

The performance of a company can be measured and assessed from financial statements for a period. Increasing company competition makes management put more effort as well as earnings management to survive and be able to compete with other companies and attract investors. According to Healy & Wahlen (1999), earnings management occurs when managers use judgment in financial reporting and preparation of transactions with the aim of manipulating the earnings generated that possibly mislead stakeholders about the actual economic performance of the company or to influence the results related to contracts that depend on accounting figures.

Many cases of giant companies involved in financial reporting scandals, such as British

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Telecom in 2017 that manipulated their company profits through fake contract extensions and invoices and also fake transactions with suppliers (Priantara, 2017). Not only international companies, some national companies have also been involved in the same case, such as the case of PT. Bank Bukopin Tbk in 2018 which allegedly manipulated earnings by manipulating credit card data (Bachman, 2018).

A number of studies have been conducted before on the influence of IFRS on earnings management and found mixed results. Research by Sellami & Fakhfakh (2014), Mas et al. (2018), Sari et al. (2017) and Jaya (2017) found evidence that there was a decline in earnings management after IFRS. In contrast to previous studies, Anagnostopoulou (2016) found evidence that there was accrual earnings management shift towards real earnings management in Greece after IFRS adoption.

However, those studies contradict with research conducted by Asni & Mayasari (2018), Firmansyah & Irawan (2017), and Nastiti & Ratmono (2015) who found evidence that the IFRS convergence application was unable to change accrual earnings management behavior. Other research is shown by Zuhair & Nurdiniah (2018) who found evidence that IFRS convergence does not affect accrual earnings management while Firmansyah & Irawan (2017) obtained evidence that IFRS convergence does not affect real earnings management.

Agency theory is a theory that explains the relationship or contract between the principal (capital owner) and the agent (company management). This theory focuses on maximizing its own interests, giving rise to conflicts of interest between the two. This conflict arises because of the existence of asymmetric information (imbalance of information held between the principal and the agent).

Corporate governance (CG) is a system that regulates and controls companies to create value added for stakeholders. The role of CG effectiveness is very relevant in overseeing managers as company managers. The earnings management actions carried out by managers can be minimized by the presence of a good corporate governance (GCG) mechanism. Based on previous studies managerial ownership is considered by researchers as the most effective GCG mechanism because the results tend to be consistent in reducing earnings management. Previous studies by Junaedi & Farina (2017), Lestari & Murtanto (2017), Pramesti & Budiasih (2017), Siregar (2017), Alzoubi (2016) and Nastiti & Ratmono, (2015) have documented that the GCG mechanism is able to reduce earnings management. The results of the study concluded that IFRS convergence would further reduce opportunistic behavior of managers in managing earnings when there is a GCG mechanism.

This study aims to determine the effect of IFRS convergence on earnings management which is moderated by corporate governance. This research is expected to provide an evaluation material in an effort to improve the quality of accounting information through regulations that refer to IFRS. This study also uses the method of accrual earnings management detection, namely the Stubben method which is rarely used by previous studies. The object of this study is manufacturing companies that observed from 2015-2017.

IFRS convergence is a process of gradually integrating accounting standards in a country into international accounting standards namely IFRS (Qomariah & Marsono, 2013). IFRS convergence implemented in Indonesia is expected to reduce the information gap between the two parties so that it can minimize earnings management actions due to more disclosure. Stubben (2010) argues that revenue is the largest component of overall earnings (earnings) so it is ideal to test the existence of earnings management and can test the effect of income manipulation (recognition of earlier income) on the relationship between incomes and accounts receivable.

H_1: IFRS convergence has a significant negative effect on Earnings Management.

Beckeret al (1998) states that clients of Non Big 6 auditors report discretionary accruals that are higher than those reported by Big 6 auditors' clients. It means that it can be concluded that clients from Non Big 6 auditors tend to be higher in earnings management. Because at the time of

this study the Big 6 auditors had changed to Big 4, it was also suspected that clients from Non Big 4 auditors tended to be higher in earnings management compared to Big 4 auditors' clients. Audit quality was seen from the competent auditor role adequate and independent attitude is the party that can provide certainty about the integrity of accounting figures reported by management. Thus, IFRS which demands transparency in all fields is thought to reduce the occurrence of earnings management practices by being strengthened by high auditor quality.

H_2: Audit quality has an effect on the relationship of IFRS Convergence to Earnings Management.

According to the Decree of the Chairperson of BAPEPAM and LK Number: Kep-643 / BL / 2012 in regulation number IX.1.5 concerning the establishment and guidance of the implementation of the work of the audit committee no. 7 regarding the audit committee meeting stated that the audit committee holds regular meetings at least once in 3 (three) months. Audit committee meetings can only be held if more than 1/2 (one-half) of the members are attended. According to Xie et al. (2003), the more active audit committee has a greater composition to monitor effectively short-term discretionary accruals. Thus, an increasingly active audit committee will have a greater opportunity to monitor management actions. Thus, with the adoption of IFRS as an accounting standard that demands transparency in all fields, it is possible for the number of audit committee meetings to influence IFRS convergence towards increasingly poor earnings management practices.

H_3: The number of Audit Committee Meetings influences the relationship of IFRS Convergence to Earnings Management.

Managerial ownership is the number of shares owned by the company's management (Lestari & Murtanto, 2017). Based on agency theory, the presence of managerial ownership can align incentives between managers (agents) and shareholders (principals) and reduce agency costs so as to minimize the costs incurred by the company. Large share ownership in terms of economic value has incentives to monitor (Shleifer & Vishny, 1997). IFRS convergence creates restrictions on management policies, so that the existence of a managerial ownership mechanism can reduce earnings management behavior caused by the implementation of IFRS through improving accounting quality. This study tries to present managerial ownership as a moderating variable because the existence of this variable is expected to overcome the inconsistency of the results of previous studies regarding the effect of IFRS convergence on earnings management. Some previous studies such as Lestari & Murtanto (2017) and Alzoubi (2016) find evidence that the presence of managerial ownership can reduce earnings management.

H_4: Managerial ownership affects the relationship of IFRS Convergence to Earnings Management.

The thinking framework in this study can be described by Figure.

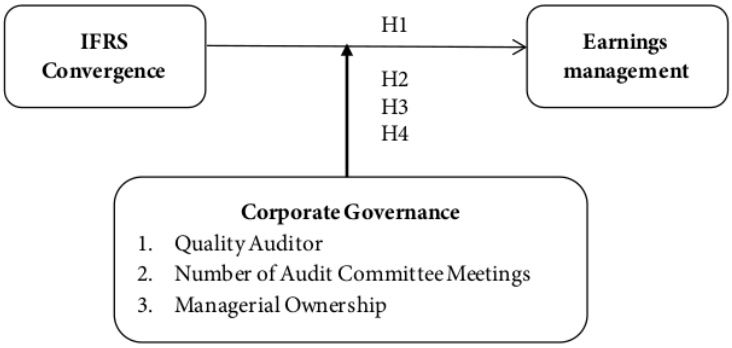

Figure 1. Research framework

METHODS

This research is quantitative research and uses secondary data. The population in this study is a BEI registered manufacturing company (www.idx.co.id) in the period 2013-2017 consisting of 152 companies. The sample selection method uses purposive sampling and obtained 38 companies with 114 units of analysis. The sample selection criteria are shown in table 1.

Table 1. Research Sample Selection Criteria

Criteria	Number
All manufacturing companies listed on the IDX as of December 31, 2017	152
Manufacturing companies that have complete data, do not generate profits and use foreign currencies during the 2015-2017 research period and are presented in foreign currencies	(114)
Selected manufacturing companies whose data is used as research	38
Total unit analysis for 3 years of observation (38 x 3 years)	114

The dependent variable in this study is accrual earnings management, while the independent variable in this study is IFRS convergence. Auditor quality, number of audit committee meetings, and managerial ownership are moderating variables in this study. The operational definitions of each variable are explained as follows:

Table 2. Operational Definition of Variables

Variable of	Definition	Measurement
Earnings management	Behavior changes the amount of earnings in the financial statements in the form of non-discretionary accruals and discretionary accruals (Sellami & Fakhfakh, 2014).	***Stubben – Revenue Model*** $\Delta AR_{it}\ \Delta AR_{it} = \propto\ + \beta_1 \Delta R1\_3_{it}$ $\propto\ + \beta_1 \Delta R1\_3_{it} + \beta_2\ \Delta R\_4_{it} \beta_2\ \Delta R\_4_{it} + \epsilon_{it}$ ϵ_{it} (Stubben, 2010)
IFRS Convergence	The process of gradually integrating accounting standards in every country into an international accounting standard, IFRS (Qomariah & Marsono, 2013).	This variable is measured using items that must be disclosed as many as 73 items (the chairman's decision of BAPEPAM-LK No.kep-347/BL/2012). **Disclosure of IFRS convergence** $= \frac{\sum Xyi}{ni} \frac{\sum Xyi}{ni}$ (Amatullah, 2014)
Auditor Quality		This variable uses a dummy measurement which is a value of 1 for companies audited by Big 4 PUBLIC ACCOUNTING FIRM and a value of 0 for companies audited by Non Big 4 PUBLIC ACCOUNTING FIRM.
Number of Audit Committee Meetings	Number of meetings or meetings conducted by the audit committee within one year.	The measurement is done by counting the number of meetings conducted by the audit committee in the company's annual report.
Managerial ownership	The percentage of shares owned by the company's management (Lestari & Murtanto, 2017).	**Managerial ownership** = $\frac{\text{Total shares owned by management}}{\text{Total outstanding shares}}$ $\frac{\text{Total shares owned by management}}{\text{Total outstanding shares}}$ (Lestari & Murtanto, 2017)

Regression testing with moderating variables can be done with several tests, namely interaction test, absolute difference test, and residual test. This study uses a model of absolute difference by adding the difference between the independent variable and the moderating variable. The equations in this study are as follows:

$$Y = \propto + \beta 1\, X1 + \beta 2\, Z + \beta 3|X1 - Z| + e$$

Y	=	Accrual earnings management (Stubben model)
X1	=	IFRS Convergence
Z1	=	Auditor quality
Z2	=	Number of Audit Committee Meetings
Z3	=	Managerial ownership
α	=	intercept
β1-3	=	regression coefficients
e	=	Error

RESULT AND DISCUSSION

Classification of earnings management in the study is presented in Table 3.

Table 3. Earnings Management (PM) Value Classification

Note	Classification	Status	Year					Total	%
			2013	2014	2015	2016	2017		
EM	<-0.075	MLA indicated	18	21	11	16	11	77	30.20
	-0.075 to 0.075	Not MLA indicated	21	21	28	23	24	117	45.88
	>0.075	MLA indicated	12	9	12	12	16	61	23.92
Total			51	51	51	51	51	255	100

This research refers to research conducted by Roychowdhury (2006) to measure the occurrence of earnings management. The study measures the indication of real earnings management practices using residual values. The residual value is an error value with intervals of less than –0.075 and exceeding 0.075 (ε <–0.075 or ε> 0.075) indicating the practice of earnings management. When testing the revenue model formula (Table 1) a value of less than -0.075 is 77 (30.20%) and a value that exceeds 0.075 is 61 (23.92%). Whether be combined, there are 54.12% of the 255 units of analysis indicated to do earnings management and 45.88% or 117 units of analysis that are not indicated to do earnings management from all samples tested.

Table 4. Descriptive Statistics Test

	N	Minimum	Maximum	Mean	Std. Deviation
IFRS convergence	114	.59	.85	.7014	.05703
Auditor Quality	114	.00	1.00	.3772	.48682
Number of Audit Committee Meetings	114	2.00	33.00	6.3772	5.69488
Managerial ownership	114	.00	.62	.0826	.15169
Valid N (listwise)	114				

Table 4. shows the descriptive test results of each variable in this study. Especially for measurement of earnings management refers to Roychowdhury (2006) and has been described in table 3. IFRS convergence is measured using how much disclosure is made by the company in accordance with the decision of Bapepam-LK No.kep-347 / BL / 2012 with an average value of 0.7014 or 70.14%. This shows that manufacturing companies in Indonesia in making financial statements are mostly based on existing regulations. The auditor quality above shows an average value of 0.3772, then for the number of audit committee meetings shows an average value of

6.3772, while the above shareholding structure shows an average value of 0.08260 or as much as 8.26% of shares owned by a line of company managers.

The classical assumption test aims to achieve an unbiased estimator. The first test, which is the normality test using the one-sample Kolmogorov-Smirnov test shows that the significance value of each is 0.001 smaller than 0.05. The results shown from table 5 concluded that the data is normally distributed.

Table 5. One-Sample Kolmogorov-Smirnov Test

		Unstandardized Residual
N		114
Normal Parameters[a,b]	Mean	.0000000
	Std. Deviation	.94499535
Most Extreme Differences	Absolute	.185
	Positive	.177
	Negative	-.185
Kolmogorov-Smirnov Z		1.972
Asymp. Sig. (2-tailed)		.001

Multicollinearity test is used to determine between independent variables. This test is needed to be done if there are more than 1 independent variable. This study uses the value of Variance-Inflating Factor (VIF) in order to test multicollinearity. As shown in table 6, the multicolinearity test shows that there is no multicollinearity because each research variable has a tolerance value> 0.1 and a VIF value <10.

Table 6. Multicollinearity Test

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-.637	1.137		-.561			
	IFRS Convergence	1.211	1.626	.065	.745	.953	.953	1.049
	Managerial Ownership	1.782	.602	.254	2.959	.982	.982	1.019
	Number of Audit Committee Meetings	-.073	.017	-.392	-4.417	.919	.919	1.088
	Auditor Quality	.169	.200	.077	.846	.864	.864	1.157

Heteroscedasticity shows that variable variance is not the same for all observations. This study used the White Test as a tool for heteroscedasticity test. Table 7 indicated that there were no heteroscedasticity problems because each variable had a value of c2 calculated <c2 which was 39.786 <139.921.

Table 7. The White Test

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.591[a]	.349	.286	.89846	1.980

The autocorrelation test aims to test whether the linear regression model has a correlation between distrubance term-ed in the period t and error in the previous period (t-1). If there is a correlation then it shows the symptoms of autocorrelation. The test used to see whether autocorrelation occurred or not is to see the Durbin-Watson value. The autocorrelation test shows that there is no autocorrelation because the Durbin Watson test shows value du <d <4-du which is 1.7677 <1.961 <2.2323.

There are three test results in this study, each test consists of one independent variable and one moderating variable that is used to predict the dependent variable. The moderating variable regression test used in this study is the absolute difference value, by adding the difference between the independent variable and the moderating variable. The moderation regression test results in this study are as follows:

The results of the coefficient of determination of accrual earnings management (revenue model) with moderating variables indicate that the adjusted R2 value is 0.010. This shows that the magnitude of the influence of IFRS convergence variables and managerial ownership as moderating variables on accrual earnings management (revenue model) is 1% and the magnitude of other variables that influence the accrual earnings management variable (revenue model) is 99%.

Table 8. Summary of Hypothesis Test Results

	Hypothesis	Regression Coefficient	Sig	Decision
H_1	IFRS convergence has negative effect on earnings management	0.135	0.205	Rejected
H_2	Auditor quality moderates the effect of IFRS convergence on earnings management	0.191	0.189	Rejected
H_3	The number of audit committee meetings moderates the influence of IFRS convergence on earnings management	-0.253	0.049	Rejected
H_4	Managerial ownership moderates the effect of IFRS convergence on earnings management	0.005	0.965	Rejected

Effect of IFRS Convergence on Earnings Management

Table 8. shows the t test results of the effect of IFRS convergence on earnings management has a significance value of 0.205 with a regression coefficient of 0.135, so it can be concluded the hypothesis regarding the effect of IFRS convergence on accrual earnings management is rejected. The results of testing this hypothesis indicate that the implementation of IFRS as a financial accounting standard in Indonesia after full convergence on January 1, 2012 then tends to have no effect on the company's accrual earnings management level.

The results above support several previous studies regarding accrual earnings management namely Nastiti & Ratmono (2015), Firmansyah & Irawan (2017), who found the results that IFRS convergence had a positive effect on earnings management in Indonesia. In line with some studies in Indonesia, Callao and Jerne's research (2010) shows that discretionary accruals have increased since the implementation period of IFRS in the European Union. Rudra and Bhattacharjee (2012) also determine that the adoption of IFRS has a positive and significant effect on earnings management in Indian companies. Thus, it can be concluded that IFRS is not necessarily suitable for application in countries with different characteristics.

The results of this test were rejected allegedly caused by several factors. The second factor that can be taken into consideration is the time of standard implementation, which is still in the convergence stage, not yet reaching the adoption stage so that it has not been effective. Another factor, IFRS made by the IASB has members who are mostly developed countries so that this can be a cause if IFRS is not necessarily fully suitable if applied in countries that have different characteristics from developed countries (Zuhair & Nurdiniah, 2018).

Auditor Quality Moderates the Effects of IFRS Convergence on Earning Management

The results of hypothesis testing on the absolute difference value of managerial ownership on the relationship between IFRS convergence on accrual earnings management (revenue model) shows a significance value of 0.189> 0.05 with a regression coefficient of 0.191. That is,

the hypothesis that managerial ownership moderates significantly the effect of IFRS convergence on earnings management is rejected. The quality of auditors with the big four public accounting firm does not guarantee that it can reduce earnings management in manufacturing companies in developing countries such as Indonesia. This is likely the company allegedly deliberately covered a fact that occurred in the company to the auditor. In addition, the existence of a particular event such as an IPO is also the reason that the practice of earnings management still exists, indicating an audit failures.

Number of audit committee meetings moderate the Effects of IFRS Convergence on Earnings Management

The results of hypothesis testing on the absolute difference value of managerial ownership on the relationship between IFRS convergence on accrual earnings management (revenue model) shows a significance value of 0.049> 0.05 with a regression coefficient of -0.253. That is, the hypothesis that managerial ownership moderates significantly the effect of IFRS convergence on earnings management is rejected. This proves that the number of audit committee meetings is able to reduce earnings management because the frequency of audit committee meetings can simultaneously monitor the condition of the company so that it minimizes earnings management practices.

The results of this study also indicate that there are still many companies that have not complied with the regulations of BAPEPAM and LK Number: Kep-643 / BL / 2012 in regulation number IX.1.5. This regulation standardizes formation and guidelines for implementing audit committee work no. 7 which states that the committee audit must have a meeting regularly at least once in 3 (three) months. This study also supports the results of the study Pamudji and Trihartati (2009) which stated that the frequency of committee meetings auditing was not effective in reducing earnings management. This is caused by the establishment of an audit committee within the company is mandatory only existing regulations. In addition, the audit committee has not yet carried out its duties and maximum responsibility so that its functions and roles are not effective.

Managerial Ownership Moderates the Effects of IFRS Convergence on Earnings Management

The results of hypothesis testing on the absolute difference value of managerial ownership on the relationship between IFRS convergence on accrual earnings management (revenue model) shows a significance value of 0.965> 0.05 with a regression coefficient of 0.005. That is, the hypothesis that managerial ownership moderates significantly the effect of IFRS convergence on earnings management is rejected.

Agency theory explains that there are differences in interests between principals and agents that can lead to information asymmetry. This information asymmetry will support the management (agent) to take action on earnings management. According to this situation, managerial ownership in the company becomes one of the important points in the company.

On the other hand, the results of this study are in line with Qomariah & Marsono (2013) who found that managerial ownership cannot reduce accrual earnings management during IFRS convergence. The hypothesis in this study was rejected because the management as well as shareholders were inadequate in understanding, reasoning, and judgment to reduce earnings management after IFRS convergence. For example, in estimating the level of uncollectible receivables, a manager must have strong understanding and reasoning as well as appropriate judgment in making decisions for his own interests which act as company management and shareholders.

CONCLUSION

This study indicates IFRS convergence does not have a positive effect on earnings management. Managerial ownership and auditor quality cannot moderate the influence of IFRS on earnings management, but the number of audit committee meetings can moderate the effect of IFRS convergence on earnings management towards negative. The limitations of this study do

not distinguish earnings management before and after IFRS convergence. Suggestions given for further research are expected to be able to compare the influence of convergence before and after IFRS convergence using the Stubben method because there are still few studies using the method.

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