

The Effect of Dividend Policy, Executive Compensation, Leverage and Information Asymmetry on Profit Management

(Empirical Study of Manufacturing Companies Listed on the Indonesia Stock Exchange Period 2018-2021)

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Abstract: This study aims to examine the effect of dividend policy, executive compensation, leverage and information asymmetry on earnings management. This research is important to do because the results of the research will contribute to investors and potential investors that there are several factors that can affect earnings management actions that are opportunistic. The population in this study are manufacturing companies listed on the Indonesia Stock Exchange for the 2018-2021 period. The data analysis technique used is multiple linear regression analysis technique. Sampling in this study using purposive sampling technique. The research found that dividend and leverage policies have an effect on earnings management, while executive compensation and information asymmetry have no effect on earnings management.

Keywords: Dividend Policy, Executive Compensation, Leverage, Information Asymmetry, Earnings Management

1. Introduction

A company is established with the aim of making a profit or profits. This profit or profit is needed by the company to be able to carry on the life of the company. Profit itself is a measurement of a company's performance summary which is carried out based on accrual-based accounting. Profit information in financial reports is generally the main concern in assessing performance or seeing how management is accountable (Astria et al., 2018). However, profit information also often becomes the target of engineering through management's opportunistic actions to maximize satisfaction, because there are parties who pay attention to profits and this is realized by management, especially managers whose performance is measured based on this profit information, thus encouraging actions to regulate profits or normal. known as earnings management (Savitri, 2014).

Earnings management may be familiar to management and accounting observers, both practitioners and academics. The term has begun to attract the attention of researchers, especially accounting researchers, because earnings management is often associated with the behavior of managers or financial report preparers. Earnings management is closely related to the level of profit earned or the business performance of an organization because the level of profit or profits earned is often associated with management performance. The size of the bonus that will be received by the manager depends on the size of the profit earned. Therefore managers manage profit figures with accrual engineering to influence the final results of various decisions made by changing accrual figures to make profits lower or higher.

Earnings management itself is influenced by several factors, among others; dividend policy, executive compensation, leverage, and information asymmetry. Large companies tend to practice earnings management for the benefit of managers or the company itself. Managers will reduce profits to avoid paying dividends to external shareholders. By managing profits like that, the dividends distributed can be reduced so that the funds and retained earnings managed by the manager become larger. This will provide flexibility for managers in developing investments that promise a positive NPV, which will result in an increase in company value in the future with the hope that managers will get an additional higher bonus. Thus, dividend policy is one of the factors that can encourage management to take earnings management actions.

2. Literature Review and Hypothesis Development

2.1 Agency Theory

Agency theory is based on three important assumptions, namely: human assumptions, organizational assumptions, and information assumptions (Eisenhardt, 1989). Jensen & Meckling (1976) stated that agency theory describes shareholders as principals and management as agents. Agency problems arise because of the separation between owners and managers of companies (agents) and humans tend to have self-interest.

Agency conflict will generate agency costs which are costs incurred to maintain an effective agency relationship between the principal and the agent. Generally, every company has agency costs because agency costs can be used to ensure managers act in the interests of shareholders and are not concerned with personal interests.

2.2 Profit Management

Earnings management as disclosure management in the sense that management intervenes with a specific purpose in the external financial reporting process on purpose to obtain some personal gain (Barus & Setiawati, 2015).

2.3 Dividend Policy

Dividend is the distribution of profits made by a company to shareholders. Dividends are distributed in the same amount for each share and the amount of dividends depends on the remaining profits after deducting the deductions specified in the deed of establishment and also depends on the resolution of the General Meeting of Shareholders (GMS).

H₁: Dividend policy affects earnings management

2.4 Executive Compensation

Compensation is an agency cost incurred for monitoring in overcoming agency conflicts which can be determined based on the manager's performance and also the final outcome based on the results of the funding and investment decisions made by the manager. Agents will be paid according to their compensation contract and the utility of the principal will be affected by the compensation paid to agents either directly or indirectly, namely influenced by the strategy chosen by the manager which affects the distribution of outcomes (Wirawati et al., 2018).

The compensation received by the manager will be influenced by the profit capability generated by the company. To get high compensation is the motivation of management or agents to take earnings management actions.

H₂: Executive compensation affects earnings management

2.5 Leverage

The greater the leverage ratio, the higher the value of the company's debt. Thus, companies that have a high leverage ratio, meaning that the proportion of debt is higher than the proportion of assets will tend to manipulate in the form of earnings management. This aims to avoid violations of debt agreements (Sosiawan, 2012).

Increasing leverage will lead to increased earnings management practices. Companies that have high levels of leverage tend to do income smoothing. The greater the leverage ratio indicates that the greater the level of dependence of the company on external parties (creditors) and the greater the burden of debt costs (interest costs) that must be paid by the company.

H₃: Leverage affects earnings management

2.6 Information Asymmetry

Information asymmetry is a situation when there are parties who benefit more than other parties because they have excess information about the assets being traded (Scott, 2003). When information asymmetry arises, disclosure decisions made by managers can affect stock prices because information asymmetry between more informed and less informed investors creates transaction costs and reduces the expected liquidity in the market for stocks.

H₄: Information asymmetry affects earnings management

3. Research Methods

3.1 Research Design

This research is a type of quantitative research, namely research that uses hypotheses using statistical test tools to conclude hypotheses using a causal relationship (Causal Hypothesis), namely a causal relationship.

3.2 Data and Data Sources

The data used in this study uses secondary data. The data comes from books and research journals related to research problems and objectives. Data sources in the form of financial reports and annual reports are obtained from the official website of the Indonesia Stock Exchange, namely www.idx.co.id and the company's official website.

3.3 Population, Sample and Sampling Method

The sampling method in this study was carried out using a purposive sampling method. The sampling criteria used in this study are as follows:

1. Manufacturing companies that publish annual reports and financial reports ending December 31 for the 2018-2021 period consecutively.
2. Manufacturing companies that use the rupiah currency in their financial reports.
3. Manufacturing companies that generate profits in a row during the 2018-2021 period.
4. Manufacturing companies that have all the data used to calculate the variables that are the focus of this study.

3.4 Operational Definition and Variable Measurement

In this study the independent variables used are dividend policy, executive compensation, leverage, and information asymmetry. As for the dependent variable used in this study is earnings management.

3.4.1 Dependent Variable

Profit Management

Earnings management is any management action that can affect reported earnings figures. Discretionary accrual (DA) values are calculated using the Modified Jones Model to measure the level of earnings management (Sari & Asyik, 2013).

1. Total Accruals (TAC)

Calculating the total accruals of company *i* in period *t* using the formula:

$$TAC_{it} = Nit - CFO_{it}$$

The total accrual value is estimated using Ordinary Least Square as follows:

$$TAC_{it}/Ait-1 = \beta_1(1/Ait-1) + \beta_2(\Delta REV_{it}/Ait-1) + \beta_3(PPE_{it}/Ait-1) + e$$

2. Non Discretionary Accrual (NDA)

NDA (non-discretionary accruals) can be calculated by re-entering the beta coefficients (β) as follows:

$$NDA_{it} = \beta_1(1/Ait-1) + \beta_2((\Delta REV_{it}/Ait - \Delta REC_{it})/Ait-1) + \beta_3(PPE_{it}/Ait-1)$$

3. Discretionary Accrual (DA)

Furthermore, the value of discretionary accruals (DA) can be calculated as follows:

$$DA_{it} = (TAC_{it}/Ait-1) - NDA_{it}$$

Description:

TAC _{it}	: Total accruals of company <i>i</i> in period <i>t</i>
Nit	: Company <i>i</i> 's net profit in period <i>t</i>
CFO _{it}	: Cash operating activities of company <i>i</i> in period <i>t</i>
Ait-1	: Total assets of company <i>i</i> in period <i>t-1</i>
β	: Regression coefficient
<i>e</i>	: Error term company <i>i</i> in period <i>t</i>
ΔREV_{it}	: Changes in company income <i>i</i> from year <i>t-1</i> to year <i>t</i>
ΔREC_{it}	: Changes in company receivables <i>i</i> from year <i>t-1</i> to year <i>t</i>
PPE _{it}	: The value of fixed assets of company <i>i</i> in period <i>t</i>
NDA _{it}	: Non-discretionary accruals of company <i>i</i> in period <i>t</i>
DA _{it}	: Discretionary accruals of company <i>i</i> in period <i>t</i>

3.4.2 Independent Variable

a. Dividend Policy

The dividend payout ratio (DPR) is the ratio used to measure the amount of dividend payments from earnings per share and measures the amount of retained earnings to increase the amount of own capital (Haneswan, 2017). The dividend payout ratio is measured by the following formulation:

$$DPR = \frac{\text{dividend per share}}{\text{earnings per share}}$$

b. Executive Compensation

According to Alam & Amanah (2019), executive compensation is defined as incentives or rewards given to the board of directors or managers for achievements towards improving company performance.

$$\text{Executive Compensation} = \ln(\text{Executive Compensation})$$

c. Leverage

The leverage ratio describes the source of operating funds used by the company and shows the risks faced by the company related to debt which can be used to predict the profits obtained by investors in the company (Asitalia & Trisnawati, 2017).

$$\text{Leverage} = \frac{\text{Total Amount of Debt}}{\text{Total Asset}}$$

d. Information Asymmetry

Information asymmetry is measured using the Relative bid-ask Spread, where information asymmetry is seen from the difference between the ask price and the company's share bid price or the difference between the selling price and the purchase price of the company's shares during one year. The bid ask spread is calculated as an average for 12 months from January to December (Wiryadi & Sebrina, 2013).

$$\text{Spread} = \frac{\text{ask price} - \text{bid price}}{(\text{ask price} + \text{bid price})/2} \times 100$$

Description:

Spread : The difference between the ask price and the bid price for 1 year

Ask : The highest ask price of the stock for 1 year

Bid : The lowest bid price of the stock for 1 year

4. Analysis Results

4.1 Descriptive Statistics

Table 1: Descriptive Statistics Results

Descriptive Statistics					
	N	Minimum	Maximum	Mean	Std. Deviation
DP	114	,066	2,516	,54784	,455154
EC	114	21,463	27,918	24,19728	1,601279
LEV	114	,063	,661	,34821	,165956
IA	114	7,074	120,879	51,35414	23,325903
PM	114	-1,898	1,235	-,17513	,605478

Source: Secondary data processed by researchers, 2023.

Based on the descriptive statistical test above, it can be concluded as follows:

- 1) The dividend policy variable has a minimum value of 0.066, a maximum value of 2.516, an average value of 0.54784 and a standard deviation of 0.455154.
- 2) The executive compensation variable has a minimum value of 21.463, a maximum value of 27.918, an average value of 24.19728 and a standard deviation of 1.601279.
- 3) The leverage variable has a minimum value of 0.063, a maximum value of 0.661, an average value of 0.34821 and a standard deviation of 0.165956.
- 4) The information asymmetry variable has a minimum value of 7.074, a maximum value of 120.879, an average value of 51.35414 and a standard deviation of 23.325903.
- 5) The Profit Management variable has a minimum value of -1.898, a maximum value of 1.235, an average value of -0.17513 and a standard deviation of 0.605478.

4.2 Classic Assumption Test

The classical assumption test is carried out with the aim of detecting the occurrence of data deviations by taking into account the regression used is feasible or not to be tested.

4.2.1 Normality Test

Table 2: Normality Test Results

	Unstandardized Residual
N	114
Test Statistic	,061
Asymp. Sig. (2-tailed)	,200 ^{c,d}

Source: Secondary data processed by researchers, 2023.

Based on the table above shows that the significance value is 0.200 which is where the value is greater than 0.05. So it can be concluded that the research data is normally distributed.

4.2.2 Multicollinearity Test

Table 3: Multicollinearity Test Results

Model	Collinearity Statistics	
	Tolerance	VIF
DP	0,943	1.060
EC	0,893	1,120
LEV	0,859	1,164
IA	0,903	1,108

Source: Secondary data processed by researchers, 2023.

Based on the table, it shows that the tolerance value of each variable is greater than 0.1 and the VIF value is less than 10, so it can be concluded that all variables have no multicollinearity problems.

4.2.3 Heteroscedasticity Test

Table 4: Heteroscedasticity Test Results

Variable	Sig. (2-tailed)
DP	0,466
EC	0,489
LEV	0,942
IA	0,232

Source: Secondary data processed by researchers, 2023.

Based on the table it can be seen that the significance value is greater than 0.05, so it can be concluded that all variables do not occur heteroscedasticity.

4.2.4 Autocorrelation Test

Table 5: Autocorrelation Test Results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	0,522 ^a	0,273	0,246	0,525704	1,922

Source: Secondary data processed by researchers, 2023.

Based on the table it can be seen that the Durbin-Watson value is 1.922. It means that the DW value is between -2 and +2, or $-2 < 1.922 < +2$, so it can be concluded that there is no autocorrelation.

4.3 Model Accuracy Test

The results of the model accuracy test in this study were processed using multiple linear regression analysis as described below:

4.3.1 Multiple Linear Regression Test

Table 6: Multiple Linear Regression Test Results

Model	Unstandardized Coefficients	
	B	Std. Error
(Constant)	,135	,784
DP	-,445	,112

EC	,025	,033
LEV	-1,268	,322
IA	-,004	,002

Source: Secondary data processed by researchers, 2023.

Based on the table, multiple linear equations can be arranged as follows:

$$PM = 0,135 - 0,445 DP + 0,025 EC - 1,268 LEV - 0,004 IA + \varepsilon$$

4.3.2 Model Fisibility Test (F Test)

Table 7: F Test Results

Model	Sum of Squares	F	Sig.
1	11,302	10,224	,000 ^b

Source: Secondary data processed by researchers, 2023.

Based on the table, it shows a significance level of F of 0.000, which means it is smaller than the significance of α (0.05), so it can be concluded that all independent variables simultaneously affect the dependent variable.

4.3.3 Determination Coefficient Test (R²)

Table 8: Determination Coefficient Test(R²) Results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	,522 ^a	,273	,246	,525704

Source: Secondary data processed by researchers, 2023..

Based on the table, an Adjusted R Square of 0.246 is obtained. This shows that the independent variable used in this study has a simultaneous effect on the dependent variable of 24.6%.

4.3.4 Statistic Test (t test)

Table 9: Statistical Test Results (t test)

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	,135	,784		,172	,864
DP	-,445	,112	-,335	3,981	,000
EC	,025	,033	,066	,759	,449
LEV	-1,268	,322	-,347	3,942	,000
IA	-,004	,002	-,169	-1,960	,053

Source: Secondary data processed by researchers, 2023.

Based on the table above it can be explained as follows:

- 1) Based on the table above, it is known that the significance value of the dividend policy variable is 0.000 < 0.05 and the t value is 3.981 > t table 1.982, so it can be concluded that dividend policy affects earnings management.
- 2) Based on the table above, it is known that the significance value of the executive compensation variable is 0.449 > 0.05 and the t value is 0.759 < t table 1.982, so it can be concluded that executive compensation has no effect on earnings management.
- 3) Based on the table above, it is known that the significance value of the leverage variable is 0.000 < 0.05 and the t value is 3.942 > t table 1.982, so it can be concluded that leverage affects earnings management.
- 4) Based on the table above, it is known that the significance value of the information asymmetry variable is 0.053 > 0.05 and the t value is 1.960 < t table 1.982, so it can be concluded that information asymmetry has no effect on earnings management.

5. Conclusion

Based on the results of the analysis and discussion that has been carried out in the previous chapter, it can be concluded as follows:

1. Dividend Policy has an effect (statistically significant) on earnings management. So that H_1 in this study is accepted.
2. Executive Compensation has no effect (not statistically significant) on earnings management. So that H_2 in this study was rejected.
3. Leverage has an effect (statistically significant) on earnings management. So that H_3 in this study is accepted.
4. Information asymmetry has no effect (statistically not significant) on earnings management. So that H_4 in this study was rejected.

Limitations

This research still has limitations that hinder the course of research, among others:

1. The research sample was only limited to manufacturing companies listed on the Indonesian Stock Exchange in the 2018-2021 period, so this research cannot be generalized to companies other than manufacturing companies. In addition, this study uses secondary data methods, so that the conclusions obtained are only based on data collected and processed through the annual financial report data of companies listed on the Indonesia Stock Exchange.
2. The level of adjusted R square in this study is still low, namely only 24.6%, so other variables are still needed which have a greater possible influence on earnings management actions..

Suggestion

Based on the conclusions and limitations contained in this study, several suggestions can be put forward that can be taken into consideration in further research, namely:

1. It is recommended for future research to take samples from other sectors on the Indonesia Stock Exchange and add a research period, in order to be able to compare the implementation of earnings management measures in other sectors and obtain more accurate and generalizable results.
2. Further research is suggested to add other independent variables to determine the determination of the application of earnings management such as taxes, capital intensity, managerial ownership, audit committee and institutional ownership so that the research results are more varied.

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