

The Effect of Accrual and Real Earnings Management on Financial Reporting Quality with Corporate Governance as a Moderating Variable

Sarifa aini^{1*}, Puji Harto²

¹Economics and Busines Faculty, Diponegoro Univeristy, Semarang, Indonesia,
sarifaaini308@gmail.com

² Economics and Busines Faculty, Diponegoro Univeristy, Semarang, Indonesia,,
pujiharto@lecturer.undip.ac.id

ABSTRACT

This study examines the effect of accrual and real earnings management on financial reporting quality, as well as the moderating role of Good Corporate Governance (GCG). Using data from transportation, logistics, and consumer non-cyclical companies listed on the Indonesia Stock Exchange (IDX) during 2020–2023, the analysis was conducted through moderated regression using SPSS 24. The results indicate that accrual earnings management has a significant negative effect on financial reporting quality, while real earnings management shows no significant impact. GCG effectively moderates the relationship between accrual earnings management and reporting quality but not for real earnings management. These findings highlight the importance of effective corporate governance in maintaining high-quality financial reporting. Future research is recommended to expand the industrial scope, observation period, and the comprehensiveness of GCG measurement.

Keywords: GCG, Accrual Earning Management, Real Earning Management,

INTRODUCTION

Financial reporting quality represents the extent to which financial statements provide comprehensive, reliable, and relevant information reflecting an entity's actual economic condition. High-quality reporting not only complies with applicable accounting standards but also supports transparency, accountability, and decision usefulness for stakeholders (Beest et al., 2009). The Indonesian Financial Accounting Standards (SAK) emphasize that compliance alone is insufficient to ensure high-quality reporting, as managerial discretion in accounting methods may affect the reliability and comparability of information. Hence, financial reports must fulfill two fundamental qualitative characteristics—relevance and faithful representation—along with enhancing attributes such as understandability, comparability, verifiability, and timeliness (IASB, 2018).

In practice, however, the quality of financial reporting is often undermined by earnings management—managerial intervention in the reporting process to influence perceived performance or meet specific contractual targets (Leuz et al., 2003). Earnings management may occur through accrual-based manipulations (adjusting accounting estimates and discretionary accruals) or real activities management, which alters operational decisions such as sales discounts or expense reductions (Kaldonksi et al., 2019). Both forms can distort reported earnings and mislead stakeholders, thereby reducing the credibility and decision usefulness of financial reports.

Several cases in Indonesia illustrate these issues. In 2018, PT Garuda Indonesia Tbk was reported to have prematurely recognized revenue from a partnership agreement with PT Mahata Aero, resulting in an artificial profit despite the absence of cash inflows (CNN Indonesia, 2019). Similarly, PT Tiga Pilar

Sejahtera Food Tbk (AISA) in 2017 was found to have overstated assets and receivables by trillions of rupiah, indicating deliberate manipulation in financial reporting (EY, 2019). These cases highlight how managerial discretion, when inadequately controlled, can severely compromise reporting quality and investor trust,

To mitigate such practices, Good Corporate Governance (GCG) plays a crucial role as an internal control and monitoring mechanism. Effective governance promotes transparency, accountability, and fairness in financial reporting, thereby limiting opportunistic behavior by management. Empirical studies (Klai & Omri, 2011; Nasiri & Sofian, 2018) demonstrate that GCG can moderate the negative relationship between earnings management and financial reporting quality, strengthening the integrity of financial disclosures. However, the effectiveness of GCG mechanisms in emerging markets like Indonesia remains debated, especially given varying enforcement levels and ownership structures dominated by controlling shareholders (Panda & Leepsa, 2017).

Prior studies have predominantly assessed financial reporting quality indirectly, using proxies such as earnings management, timeliness, value relevance, or conservatism (Fanani, 2009; Tariverdi et al., 2012; Sari et al., 2023). While informative, these approaches often overlook multidimensional aspects of reporting quality as conceptualized by Beest et al. (2009), which integrates both fundamental and enhancing qualitative characteristics. This gap indicates the need for a more holistic assessment framework that better captures the overall integrity and usefulness of financial information.

Given this context, the present study aims to analyze the effect of accrual and real earnings management on financial reporting quality, while examining the moderating role of Good Corporate Governance in mitigating earnings manipulation. The study focuses on companies in the transportation, logistics, and consumer non-cyclical sectors listed on the Indonesia Stock Exchange (IDX) during 2020–2023. These sectors are particularly relevant due to their complex operations, high fixed costs, and exposure to external pressures, which may intensify managerial incentives to engage in earnings management (Yusri, 2020).

This research contributes to the literature by employing a NiCE-based measurement framework that captures multiple qualitative attributes of reporting quality—relevance, faithful representation, understandability, comparability, and timeliness—and by providing empirical evidence on the moderating effectiveness of GCG in the Indonesian context. The findings are expected to enrich academic understanding of financial reporting dynamics and offer practical implications for regulators, investors, and corporate governance practitioners.

RESEARCH METHOD

3.1 Research Design

This study employs a quantitative research approach with a hypothesis-testing design aimed at analyzing the effect of accrual and real earnings management on financial reporting quality, and examining the moderating role of Good Corporate Governance (GCG). The study utilizes secondary data obtained from audited annual reports of companies in the transportation, logistics, and consumer non-cyclical sectors listed on the Indonesia Stock Exchange (IDX) for the period 2020–2023. Data were analyzed using Moderated Regression Analysis (MRA) through IBM SPSS Statistics version 26.

3.2 Population and Sampling

The population comprises all transportation, logistics, and consumer non-cyclical companies listed on the IDX between 2020 and 2023. Samples were determined using a purposive sampling technique based on the following criteria:

1. The company was continuously listed on the IDX during 2020–2023.
2. The company published audited annual financial reports within the observation period.
3. The report contained complete data relevant to the research variables.

This sampling method ensures that selected firms consistently meet data and disclosure requirements, thus enhancing comparability and data validity.

3.3 Variable Measurement

Dependent Variable – Financial Reporting Quality (FRQ)

Financial reporting quality was measured using the NiCE Framework developed by Beest et al. (2009), which evaluates five qualitative characteristics of financial information: relevance, faithful representation, understandability, comparability, and timeliness. The framework includes 21 indicators, each rated on a five-point scale, allowing a multidimensional assessment of reporting quality.

Independent Variables

- Accrual Earnings Management (AEM): measured using the Kothari et al. (2005) discretionary accrual model, which adjusts total accruals for performance (ROA).
- Real Earnings Management (REM): measured following Roychowdhury (2006) using three abnormal components Abnormal Cash Flow from Operations (ABCFO), Abnormal Production Costs (ABPROD), Abnormal Discretionary Expenses (ABDISX)

The comprehensive REM score was derived as:

$$R E M = A B C F O + A B P R O D + A B D I S X$$

Moderating Variable – Good Corporate Governance (GCG)

GCG was measured using a Corporate Governance Index adapted from Solikhah & Maulina (2021), based on the OECD principles (transparency, accountability, responsibility, independency, fairness). The index includes 20 criteria, each rated on a binary or ordinal scale, reflecting a firm's adherence to governance best practices.

Control Variables

Two control variables were included to minimize potential bias:

- Firm Size (SIZE): measured as the natural logarithm of total assets.
- Leverage (LEV): measured by the ratio of total liabilities to total assets.

3.4 Data Collection Procedure

Data were collected using documentation and literature study methods. Financial data were obtained from official company websites and the IDX portal (www.idx.co.id), while theoretical references were gathered from relevant journals, books, and research reports. Only audited and publicly available financial statements were used to ensure reliability and data integrity.

3.5 Data Analysis Technique

Data were analyzed through several stages:

1. Descriptive Statistics: to summarize the mean, median, minimum, maximum, and standard deviation of each variable.
2. Classical Assumption Tests: including tests of normality, multicollinearity, autocorrelation, and heteroskedasticity to validate regression requirements.
3. Moderated Regression Analysis (MRA): used to examine the moderating effect of GCG on the relationship between earnings management and financial reporting quality, with the regression model formulated as:

$$FRQ = \alpha + \beta_1 AEM + \beta_2 REM + \beta_3 (AEM \times GCG) + \beta_4 (REM \times GCG) + \varepsilon$$

4. Goodness-of-Fit Tests: including the coefficient of determination (R^2), F-test, and t-test, to evaluate model significance and explanatory power.

RESULTS AND DISCUSSIONS

Result

4.1 Descriptive Statistics

The descriptive analysis provides an overview of the characteristics of each research variable. The results show that **accrual earnings management (AEM)** has a mean value of -0.0365 , indicating that accrual-based manipulation among sampled firms is relatively low, although the standard deviation (1.687) suggests notable variation. **Real earnings management (REM)** shows a mean of 0.904 with a higher deviation (1.980), implying broader heterogeneity in real activity manipulation practices.

4.2 Regression Analysis

Prior to regression testing, all classical assumption tests were satisfied. The Kolmogorov-Smirnov normality test ($p = 0.276$) confirmed normal distribution. Multicollinearity was absent ($VIF < 10$, tolerance > 0.1), residuals were random (Runs Test $p = 0.424$), and no heteroskedasticity was detected (Glejser test $p > 0.05$).

4.3 Hypothesis Testing

The t-test results reveal that AEM ($\beta = -0.468$, $p < 0.001$) significantly and negatively affects FRQ, suggesting that higher accrual manipulation deteriorates reporting quality. In contrast, REM ($\beta = -0.035$, $p = 0.386$) is not significant, indicating operational-based manipulation has limited statistical impact on reporting quality. Among control variables, firm size ($\beta = -0.335$, $p = 0.001$) and GCG ($\beta = -0.079$, $p = 0.002$) show negative effects, while leverage ($\beta = 0.169$, $p < 0.001$) positively affects FRQ.

4.4 Moderating Effect of GCG

The moderated regression analysis (MRA) shows that GCG significantly moderates the relationship between AEM and FRQ ($R^2 = 0.898$, $p < 0.001$). The interaction term AEM×GCG ($\beta = -0.081$, $p < 0.001$) indicates that effective governance mitigates the negative effect of accrual manipulation on reporting quality.

However, the interaction REM×GCG ($R^2 = 0.042$, $p = 0.577$) is not significant, suggesting that GCG does not moderate the link between real earnings management and reporting quality. These results imply that while governance mechanisms are effective in constraining accounting-based manipulation, they are less effective in detecting real operational interventions.

Discussion

Effect of Accrual Earnings Management on Financial Reporting Quality

The significant negative relationship between AEM and FRQ supports the Agency Theory (Jensen & Meckling, 1976), which posits that managers engage in discretionary accounting choices to meet personal or contractual objectives. This finding aligns with Burlacu et al. (2024) and Khelil-Rhouma & Hamed-Sidhom (2021), who found that accrual-based manipulation erodes transparency and reliability. It also echoes results from Cohen et al. (2008) and Nugrahanti & Nugroho (2022) showing that accrual adjustments distort true firm performance, reducing the credibility of reported earnings.

Practically, this suggests that Indonesian firms still face challenges in maintaining faithful representation due to managerial discretion. Strengthening audit quality and governance enforcement can help mitigate such manipulative tendencies.

Effect of Real Earnings Management on Financial Reporting Quality

REM shows an insignificant negative impact on FRQ, consistent with Zang (2011) and Amelia Sari (2022), who argue that real activity manipulation is more subtle and less detectable in the short term. While it may not immediately distort reporting quality, REM can impair firm performance and stakeholder trust over time.

The insignificance observed may reflect Indonesia's disclosure environment, where operational decisions (e.g., pricing or production adjustments) are harder to monitor externally. Thus, future studies should integrate panel or sectoral analysis to capture long-term REM effects.

Moderating Role of Good Corporate Governance

GCG significantly moderates the effect of AEM on FRQ, demonstrating its ability to constrain opportunistic accrual choices. This finding supports Rahman & Ismail (2011) and Lestari & Yulianawati (2015), emphasizing that governance effectiveness depends on substantive implementation rather than formal compliance.

However, GCG fails to moderate the REM–FRQ relationship, consistent with Iqbal et al. (2023), who noted that board independence and institutional ownership may not always curtail real activity manipulation. This limitation indicates that oversight mechanisms in Indonesia remain more attuned to accounting discretion than operational decisions.

Control Variables: Firm Size and Leverage

Firm size negatively affects FRQ, implying that larger firms may face complex operations and higher pressure to meet earnings targets, which can reduce reporting transparency. This finding contrasts with Aulawy & Utomo (2021), who argued that larger firms usually exhibit better internal control. Leverage shows a positive and significant influence, indicating that higher debt levels may motivate firms to report more transparently under creditor scrutiny — supporting Ahmed & Duellm (2013) and Rahman & Hossain (2020).

CONCLUSION

This study investigates the effect of accrual and real earnings management on financial reporting quality (FRQ), and the moderating role of Good Corporate Governance (GCG) among transportation, logistics, and consumer non-cyclical companies listed on the Indonesia Stock Exchange (IDX) during 2020–2023.

The empirical results reveal that accrual earnings management (AEM) negatively and significantly affects FRQ, indicating that accounting-based manipulations reduce the credibility and reliability of financial statements. Conversely, real earnings management (REM) does not significantly influence FRQ, implying that operational manipulation remains less visible in short-term reporting.

Moreover, GCG significantly moderates the relationship between AEM and FRQ, confirming its role as a monitoring mechanism that constrains discretionary accounting practices. However, GCG fails to moderate the impact of REM on FRQ, suggesting that governance oversight in Indonesia is still limited in detecting real activities manipulation.

Overall, these findings underscore the importance of effective governance mechanisms in maintaining the transparency and integrity of financial reporting, especially in emerging market contexts where regulatory enforcement and ownership concentration may affect monitoring effectiveness.

REFERENCES

- F. van Beest, G. Braam, and S. Boelens, "Quality of financial reporting: Measuring qualitative characteristics," *NiCE Working Paper 09-108*, 2009. [Online]. Available: <https://repository.ubn.ru.nl/handle/2066/90559>
- C. Leuz, D. Nanda, and P. D. Wysocki, "Earnings management and investor protection: An international comparison," *Journal of Financial Economics*, vol. 69, pp. 505–527, 2003. [Online]. Available: [https://doi.org/10.1016/S0304-405X\(03\)00121-1](https://doi.org/10.1016/S0304-405X(03)00121-1)
- M. C. Jensen and W. H. Meckling, "Theory of the firm: Managerial behavior, agency costs and ownership structure," *Journal of Financial Economics*, vol. 3, no. 4, pp. 305–360, 1976. [Online]. Available: [https://doi.org/10.1016/0304-405X\(76\)90026-X](https://doi.org/10.1016/0304-405X(76)90026-X)
- D. A. Cohen, A. Dey, and T. Z. Lys, "Real and accrual-based earnings management in the pre- and post-Sarbanes-Oxley periods," *The Accounting Review*, vol. 83, no. 3, pp. 757–787, 2008.
- S. Roychowdhury, "Earnings management through real activities manipulation," *Journal of Accounting and Economics*, vol. 42, no. 3, pp. 335–370, 2006. [Online]. Available: <https://doi.org/10.1016/j.jacceco.2006.01.002>
- M. Kałdoński, T. Jewartowski, and J. Mizerka, "Capital market pressure, real earnings management, and institutional ownership stability: Evidence from Poland," *International Review of Financial Analysis*, 2019. [Online]. Available: <https://doi.org/10.1016/j.irfa.2019.01.009>
- N. Klai and A. Omri, "Corporate governance and financial reporting quality: The case of Tunisian firms," *International Business Research*, vol. 4, no. 1, pp. 158–166, 2011. [Online]. Available: <https://doi.org/10.5539/ibr.v4n1p158>
- M. Nasiri and S. Sofian, "Investigating the effects of corporate governance on the relationship between earning management and corporate performance," *International Journal of Engineering and Technology*, vol. 7, no. 4, pp. 254–258, 2018. [Online]. Available: <https://doi.org/10.14419/ijet.v7i4.28.22589>
- Z. Fanani, "Kualitas pelaporan keuangan: Berbagai faktor penentu dan konsekuensi ekonomis," *Jurnal Akuntansi dan Keuangan Indonesia*, vol. 6, no. 1, pp. 20–45, 2009. [Online]. Available: <https://doi.org/10.21002/jaki.2009.02>
- Y. Tariverdi, M. Moradzadehfard, and M. Rostami, "The effect of earnings management on the quality of financial reporting," *African Journal of Business Management*, vol. 6, no. 12, pp. 4603–4611, 2012. [Online]. Available: <https://doi.org/10.5897/AJBM11.3006>
- N. Arthur and H. Chen, "Corporate ownership concentration and financial reporting quality: International evidence," *Journal of Financial Reporting and Accounting*, 2018. [Online]. Available: <https://doi.org/10.1108/JFRA-07-2017-0051>
- C. Chen, S. Huang, and H. Fan, "Complementary association between real activities and accruals-based manipulation in earnings reporting," *Journal of Economic Policy Reform*, pp. 37–41, 2012. [Online]. Available: <https://doi.org/10.1080/17487870.2012.667965>
- Y. Chen, W. Liou, Y. Chen, and J. Wu, "Fraud detection for financial statements of business groups," *International Journal of Accounting Information Systems*, vol. 32, 2019. [Online]. Available: <https://doi.org/10.1016/j.accinf.2018.11.004>
- J. Smith and R. Taylor, "Relevance in financial reporting: A study of investor perceptions," *Journal of Accounting and Finance*, pp. 123–140, 2022.
- M. Jones, L. Brown, and Y. Zhao, "Faithful representation and market efficiency," *International Accounting Review*, vol. 30, no. 2, pp. 78–95, 2021.

- B. Panda and N. Leepsa, "Agency theory: Review of theory and evidence," *Indian Journal of Corporate Governance**, 2017. [Online]. Available: <https://doi.org/10.1177/0974686217701467>
- IAI, **Kerangka Konseptual Pelaporan Keuangan**, 2019.
- IASB, **Conceptual Framework for Financial Reporting**, 2018.
- EY, "Laporan atas investigasi berbasis fakta PT. Tiga Pilar Sejahtera Food Tbk," 2019.
- CNN Indonesia, "Kronologi kisruh laporan keuangan Garuda Indonesia," 2019.
- A. Z. Yusri, **Manajemen Rantai Pasok**, **Jurnal Ilmu Pendidikan**, vol. 7, no. 2, 2020.
- S. Agustinus and S. Noorlailie, "Financial reporting quality: The effectiveness of the corporate governance quality evidence from Indonesia," 2022. [Online]. Available: <https://doi.org/10.32996/jefas>
- E. Arioglu, M. Borak, and M. Ocak, "Hometown religiosity and financial reporting quality: Evidence from chairpersons," **Managerial Auditing Journal**, vol. 39, no. 5, pp. 443–476, 2024. [Online]. Available: <https://doi.org/10.1108/MAJ-12-2023-4143>
- G. Burlacu, I.-B. Robu, and I. Munteanu, "Exploring the influence of earnings management on the value relevance of financial statements: Evidence from the Bucharest Stock Exchange," **International Journal of Financial Studies**, vol. 12, no. 3, p. 72, 2024. [Online]. Available: <https://doi.org/10.3390/ijfs12030072>
- S. Febriansyah, R. Mardiyani, and E. A. Firmansyah, "Analysis determination of firm value: Corporate governance perception index as moderating variable," **The International Journal of Applied Business**, vol. 8, no. 2, pp. 212–225, 2024.