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Good Corporate Governance to Financial Performance: Earnings Management Moderation

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ABSTRACT: The aim of this study is to examine the impact of Good Corporate Governance (GCG) on financial performance and analyze whether earnings management affects the financial performance of mining companies listed on the Indonesia Stock Exchange (BEI) during the period 2018-2022. The research adopts a quantitative approach using Structural Equation Modeling (SEM) based on Partial Least Square (PLS). The population and sample consist of 47 mining companies listed on BEI from 2018 to 2022. The results indicate that GCG has a significant and positive influence on financial performance, while earnings management does not significantly affect financial performance. Furthermore, earnings management moderates the impact of GCG on financial performance.

KEYWORDS*:* Good Corporate Governance; Earnings Management; Financial Performance

I. INTRODUCTION

Earnings management is a financial reporting practice that involves management's involvement with the aim of maximizing personal gains (Hele 2019). Managers execute earnings management by intervening in the preparation of financial reports based on accrual accounting principles (Majid, Sari, and Purnomo 2020). The company's performance is then evaluated by shareholders based on these financial reports, reflecting in stock performance. Setiawan (2022) found that corporate governance practices influence the reduction of discretionary accruals, a measure of earnings management, positively affecting Cash Flow Return on Assets (CFROA).

In the mining sector, phenomena affecting stock performance occurred in 2019 with a decline attributed to falling coal prices, impacting sales and profit margins (Suryahadi, Izzati, and Suryadarma 2020). Another case in 2015 saw a decline in commodity prices due to a slowdown in coal and oil industries, affecting mining production (Hijriyani, Zulfah, and Setiawan 2017). Various negative news, such as the falsification of sales data by PT Bumi Resources, adds complexity (Nasution 2021).

Financial performance represents a company's ability in resource management, crucial for achieving goals (Pribadi and Diyah, 2022). Good corporate governance influences managerial decisions regarding cost of equity and debt, enhancing overall company performance (Sugiyanto 2019). However, the individual interests of managers may conflict with corporate goals, leading to earnings management practices (Siagian 2020).

Research on corporate governance and firm performance in Hong Kong (Leung et al., 2018) and Malaysia (Zabri, Halim, and Abdullah 2018) yielded positive impacts of independent commissioners on financial indicators. However, results from India suggested negative effects (Salim 2017). This study aims to contribute to understanding the influence of corporate governance on financial performance, particularly in the mining sector, incorporating earnings management as a moderating variable. The research addresses gaps in previous studies, providing insights into the impact of these variables on mining companies listed on the Indonesia Stock Exchange (BEI) from 2018 to 2022.

II. LITERATURE REVIEW

A. Influence of Audit Committee on Financial Performance

The audit committee is a corporate body responsible for overseeing internal and external audit processes. It plays a crucial role in ensuring that the company's financial statements are presented fairly and not misleading. Effective financial performance indicates efficient and effective management, benefiting stakeholders such as shareholders, employees, and the community (Tri,

A. I., & Lilis, A. 2018). The committee oversees internal and external audit processes, ensuring independence, objectivity, and professionalism. Effective audits improve financial statement quality and prevent errors (Haniifah, M. N., & Pramudyastuti, O. L. 2021). The committee also ensures compliance with applicable regulations, mitigating legal risks and building stakeholder trust.
Research indicates that an effective audit committee positively influences financial performance. Studies by Yuliani and Sukirno (2018) and Shanti (2020) found a significant impact on financial performance. Therefore, the hypothesis developed is:

H1 = The Audit Committee significantly influences Financial Performance

B. Influence of Board of Commissioners on Financial Performance

The board of commissioners oversees and advises the board of directors in running the company, playing a vital role in ensuring adherence to good corporate governance principles. It monitors financial performance, crucial for efficient management and optimal benefits to stakeholders (Tri, A. I., & Lilis, A. 2018). The board oversees the board of directors, reviews financial reports, corporate policies, and operational activities, ensuring effective supervision, ethical management, and compliance with regulations (Julythiawati, N. P. M., & Ardiana, P. A. 2023). Research suggests that independent commissioners have a positive and significant impact on financial performance (Saifi, 2019; Intia, L. C., & Azizah, S. N. 2021). However, contrary findings exist, highlighting the complexity of the relationship. Therefore, the hypothesis developed is:

H2 = The Board of Commissioners significantly influences Financial Performance

C. Influence of Managerial Ownership on Financial Performance

Managerial ownership represents the proportion of company shares owned by managers. High managerial ownership can positively or negatively impact financial performance, depending on factors such as ownership structure and corporate policies. High managerial ownership can reduce agency problems, aligning manager and shareholder interests. Managers with significant ownership have a motivation to improve company performance, fostering management cohesion and cooperation (Anggraini, R., & Fidiana, F. 2021; Saifi, M. 2019).
Research supports the positive influence of managerial ownership on financial performance (Holly & Lukman, 2021; Saifi, M. 2019). Therefore, the hypothesis developed is:

H3 = Managerial Ownership significantly influences Financial Performance

D. Influence of Earnings Management on Financial Performance

Earnings management involves manipulating financial reports for personal gain or increasing company value. The phenomenon raises concerns about the reliability of financial information. Good financial performance is crucial for stakeholder trust and decision-making. Previous research indicates mixed results on the impact of earnings management on financial performance (Lestari, N., & Ningrum, S. A. 2018; Adryanti, 2019). Considering Indonesia's unique context and prevalent earnings management practices, the hypothesis developed is:

H4 = Earnings Management significantly influences Financial Performance

E. Moderating Effect of Good Corporate Governance on Earnings Management

Good corporate governance is crucial for minimizing agency problems and ensuring transparency. The research hypothesis suggests that good corporate governance moderates the relationship between earnings management and financial performance (Santoso, L., & Bimo, I. D. 2023). This hypothesis is developed as follows:

H5 = Earnings Management moderates the influence of Good Corporate Governance on Financial Performance

III. METHODOLOGY

The research method employed is quantitative, utilizing Structural Equation Modeling (SEM) with a foundation in Partial Least Square (PLS) approach. SEM is a statistical analysis technique used to test the relationships between variables. Based on the hypotheses presented in the research, the research model will be further analyzed through SEM analysis. To examine the structural relationships between latent variables, hypothesis testing on the path coefficients between variables is conducted by comparing the p-value with alpha (0.005) or t-statistic (>1.96). The population for this study consists of 47 mining companies listed on the Indonesia Stock Exchange (BEI) from 2018 to 2022. The sample size used is 47 mining companies listed on the Indonesia Stock Exchange (BEI). The sample selection in this study is determined based on the saturation sampling method.

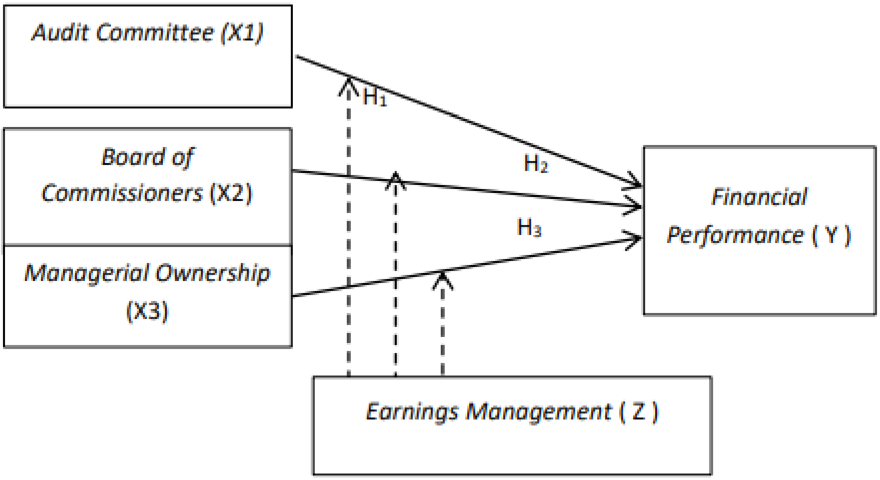

Figure 1. Research Model

IV. RESULTS AND DISCUSSION"

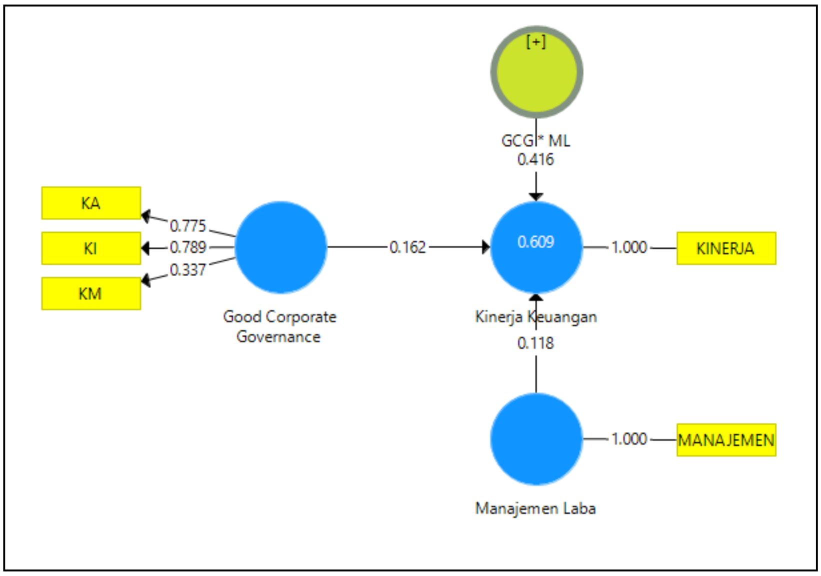

Figure 2. Hypothesis Testing and MRA Results

Source: Processed by the Researcher (2023)

Based on Figure 2, the following Hypothesis Testing and MRA table, which will be explained further, will provide empirical evidence regarding the influence of Good Corporate Governance on financial performance with earnings management as a moderating variable. The table is as follows:

Table 3: Hypothesis Testing and MRA Results

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
GCG * ML -> FP	0.416	0.494	0.187	2.222	0.027
GCG -> FP	0.162	0.146	0.073	2.204	0.028
EM -> FP	0.118	0.049	0.264	0.447	0.655

Source: Data processed in 2023

The table shows the results of hypothesis testing and Multiple Regression Analysis (MRA) to examine the relationship between Good Corporate Governance (GCG), Earnings Management (ML), and Financial Performance (KK) in Indonesian companies. In the context of the relationship between GCG and ML with financial performance, a p-value less than 0.05 indicates sufficient evidence to support the hypothesis that GCG and ML have a positive relationship with financial performance. Based on Table 3 and Figure 2 above, the research findings are as follows:

1. **Audit Committee has a significant and positive influence on Financial Performance**

Hypothesis 1 proposed in this study is that the Audit Committee has a significant and positive influence on Financial Performance. This finding is supported by the coefficient sig = 0.028 < 0.05 and the original sample of 0.162. The audit committee variable has an influence on the financial performance variable of 0.775 or 75.5%. Based on these research results, H1 is accepted. The research results indicate that there is a positive and significant influence of the Audit Committee on Financial Performance. Based on the research results, the audit committee is a very important factor in influencing Financial Performance. The audit committee plays a crucial role in ensuring the integrity and quality of financial reporting. By closely monitoring accounting practices and financial reporting, the audit committee helps reduce the risk of fraud or manipulation of financial information. Trust of shareholders and the overall capital market can be enhanced through transparency and reliability of financial information generated. The audit committee plays a vital role in maintaining the financial integrity of the company. The audit committee is responsible for ensuring that the company's financial statements are prepared accurately and in accordance with applicable accounting standards. The audit committee is also responsible for overseeing the company's internal and external audit activities. The audit committee can help the company improve the quality of financial reporting. Accurate and reliable financial statements are a crucial factor in gaining the trust of investors and creditors in the company. The audit committee can help the company reduce the risk of fraud. Fraud can cause significant financial losses to the company. The audit committee can also help the company prevent fraud by effectively overseeing the company's operational activities. The audit committee can help the company improve efficiency and effectiveness. The audit committee can provide advice and recommendations to the company's management to improve operational efficiency and effectiveness.

Research conducted by Yuliani and Sukirno (2018) found that the audit committee significantly influences financial performance. Companies with an effective audit committee have better financial performance than companies without an audit committee or with an ineffective audit committee. Shanti's research (2020) found that the audit committee significantly influences financial performance. In carrying out its duties effectively, the board of commissioners needs assistance from the audit committee, which is tasked with overseeing and assessing the implementation of activities and the results of audits conducted by internal or external auditors in providing recommendations for improving the management control system.

2. **Board of Commissioners has a significant and positive influence on Financial Performance**

Hypothesis 2 proposed in this study is that the Board of Commissioners has a significant and positive influence on Financial Performance. This finding is supported by the coefficient sig = 0.028 < 0.05 and the original sample of 0.162. The variable of the board of commissioners has an influence on the variable of financial performance by 0.789 or 78.9%. Based on these research results, H2 is accepted. The research results indicate that there is a positive and significant influence of the Board of Commissioners on Financial Performance. Based on the research results, the board of commissioners is a very important factor in influencing Financial Performance. The board of commissioners, as the main supervisory body, plays a role in setting the company's strategic direction and overseeing the performance of executive management. The presence of an effective board of commissioners can increase transparency, accountability, and protect the interests of shareholders. A board of commissioners with adequate competence and experience can provide valuable advice and recommendations to the board of directors in decision-making. This can help ensure that the decisions made by the board of directors are the right decisions and are beneficial to the company. The board of commissioners can oversee the implementation of good corporate governance, making the company more transparent and accountable in its management. This can increase the trust of investors and creditors in the company, ultimately improving the company's financial performance.

Research conducted by Kartika (2017) found that the board of commissioners significantly influences financial performance. The board of commissioners can provide input and recommendations to the board of directors to improve the operational efficiency of the company. This can help the company reduce costs and increase profits. Research by Harmaen et al (2022) also found that the board of commissioners significantly influences financial performance. A larger board of commissioners can provide more effective oversight of the board of directors. This can help ensure that the board of directors acts in the best interests of the company.

3. **Managerial Ownership has a significant and positive influence on Financial Performance**

Hypothesis 3 proposed in this study is that Managerial Ownership has a significant and positive influence on Financial Performance. This finding is supported by the coefficient sig = 0.028 < 0.05 and the original sample of 0.162. The variable of managerial ownership has an influence on the variable of financial performance by 0.337 or 33.7%. Based on these research results, it can be concluded that there is a positive and significant influence of Managerial Ownership on Financial Performance. Based on the research results, it shows indicators that managerial leadership is a very important factor in influencing Financial Performance. Managerial leadership is also an essential element in achieving optimal financial performance. Effective management can manage company resources wisely, design and implement the right business strategies, and maintain operational efficiency. Leadership focused on integrity, ethics, and accountability can shape a corporate culture that supports long-term growth and sustainability. Managerial ownership can reduce agency problems. Agency problems occur when managers act in their own interest, which can harm shareholders. High managerial ownership can reduce agency problems because managers will have the same interests as shareholders. Managerial ownership can increase manager motivation. Managers who own company shares will be more motivated to improve the company's performance because the company's performance will directly impact their wealth. Managerial ownership can enhance manager supervision. Managers who own company shares will be more driven to supervise the company's performance because they have the same interests as shareholders. However, excessively high managerial ownership can also have negative effects on financial performance. This is because managers with excessively high share ownership can act opportunistically for their personal gain.

Research by Holly & Lukman (2021) found that managerial ownership significantly influences financial performance. Managers who own company shares will be more driven to supervise the company's performance because they have the same interests as shareholders. Research by Romadoni & Pradita (2022) also found that managerial ownership significantly influences financial performance. Managers who own company shares will be more likely to make decisions that benefit the company in the long run because they have a long-term interest in the company.

4. Earnings Management does not have a significant influence on Financial Performance

Hypothesis 4 proposed in this study is that Earnings Management has a significant influence on Financial Performance. Based on the research results, Earnings Management does not have a significant influence on Financial Performance, as evidenced by the coefficient sig = 0.655 > 0.05. Based on these research results, H4 is rejected. The finding that Earnings Management does not have a significant influence on the financial performance of companies in this study indicates that, at least in the investigated context, earnings management practices do not directly affect a company's financial results. Other factors are more dominant or have a greater impact on the financial performance of mining companies listed on the Indonesia Stock Exchange (IDX) during the period 2018-2022, making the impact of earnings management practices less apparent. It is important to understand that earnings management involves efforts to manage financial information to appear better than the actual reality. While some companies engage in these practices to influence the perception of external parties, such as shareholders or financial analysts, this research shows that such actions do not directly create a measurable impact on the financial performance of companies. Other factors such as management policies, business strategies, operational efficiency, and market conditions have a stronger influence on financial performance. Therefore, these research findings can provide insight to financial practitioners and decision-makers that in designing strategies and managing company performance, focusing on these aspects is more beneficial than paying too much attention to or avoiding earnings management practices.

These research results align with studies conducted by (Epi, 2017) and (Rahayu and Sari, 2018), which show that earnings management does not affect financial performance. The consistency of these findings in various contexts or time periods may indicate that the relationship between earnings management, GCG, and financial performance is indeed based on a strong and reliable foundation.

5. Earnings Management can moderate Good Corporate Governance on financial performance

Hypothesis 5 proposed in this study is that Earnings Management can moderate Good Corporate Governance on Financial Performance. Based on the research results, earnings management moderates the influence of GCG on financial performance, as evidenced by the coefficient sig = 0.027 < 0.05. Based on these research results, H3 is accepted. This can be interpreted that, although GCG has a positive impact on financial performance in general, this influence can be moderated by earnings management practices.

Based on these research results, companies need to understand the complex dynamics between GCG, earnings management, and financial performance to optimize strategies. This research provides important implications for practitioners and policymakers in managing companies. The role of GCG becomes increasingly crucial in controlling and directing earnings management practices, thereby improving the financial performance of companies. Good earnings management can strengthen the relationship between GCG and company performance. Good earnings management will increase the transparency of the company's financial information. This can help investors assess the company's performance better, thus increasing investor confidence and stock prices. Additionally, good earnings management will increase management accountability to shareholders. This can help prevent corruption and abuse of power, thus increasing efficiency and productivity.

These results indicate that good earnings management can be an important factor in improving the financial performance of companies. Good earnings management can weaken the negative relationship between GCG and company performance, and strengthen the positive relationship between GCG and company performance. Good earnings management can include various strategies, such as income management, creative accounting, and smart cost allocation. If a company can manage earnings well, this can create a positive image in financial reports, which, in turn, can strengthen the company's financial performance. Although earnings management can improve short-term financial performance, it is essential to remember that this strategy can also pose long-term risks. Companies need to ensure that earnings management practices do not create uncertainty that can harm shareholder confidence and the credibility of the company.

This research is in line with Triyani et al (2019), Jjuwita and Febriyanti (2021), Itan (2020), and Abduh & Rusliati (2018), stating that the earnings management variable can moderate GCG with independent commissioner proxies, institutional ownership, and audit quality on financial performance with Tobin's Q proxy. The consistency of findings in various contexts or time periods can indicate that the relationship between earnings management, GCG, and financial performance is indeed a strong and reliable basis.

CONCLUSIONS

Audit Committees, Boards of Commissioners, and Managerial Ownership each play a significant and positive role in the financial performance of a company. The Audit Committee plays a crucial role in ensuring good corporate governance, enhancing investor confidence, while the Board of Commissioners, as the main supervisory body, has a significant impact on setting the strategic direction of the company and overseeing executive management. High managerial ownership is also considered to have a positive influence because it can reduce agency problems by aligning the interests of managers with shareholders. On the other hand, the findings indicate that earnings management does not have a significant impact on financial performance, indicating that this practice is not substantially able to improve the company's performance. However, earnings management plays a moderating role in the influence of Good Corporate Governance (GCG) on financial performance. Specifically, earnings management can influence the positive or negative effects of GCG practices, with the potential to obscure the positive impact of GCG implementation if financial reports are manipulated to show better performance than reality. The implications of these findings are important for companies that want to optimize the benefits of GCG practices. Corporate management not only needs to focus on good GCG implementation but also must pay attention to the potential moderating impact that may arise from earnings management practices. Awareness of the role of earnings management as a moderating variable can help companies optimize the implementation of GCG and improve their financial performance.

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