Analysis of firm size, leverage, corporate governance on earnings management practices (Indonesian evidence)

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ABSTRACT

The inconsistency of the results in previous studies related to the relationship of firm size and leverage on earnings management practices is still interesting. In contrast to the previous studies, this study is not merely to determine the effect of firm size, leverage, and corporate governance on earnings management practices partially but also to include the variable corporate governance (CG) is also thought to be able to moderate the effect of firm size and leverage variables on earnings management practices. Discretionary accruals as proxy for earnings management and are also measured using Performance-Matched Discretionary Accruals Model. Using Moderated Regression Analysis (MRA) and Residual Test, the result shows that firm size and corporate governance have a significant effect on earnings management, whereas the leverage was not found to have a significant effect. In addition, the results of this study indicate that corporate governance is able to moderate the relationship firm size and leverage on earnings management practices.

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1. INTRODUCTION

The practice of earnings management implemented by management has various purposes. One of them is an opportunistic behavior that can maximize its own utility by using judgment to accelerate or decelerate revenue recognition and expense. This kind of measure will directly affect the profit information presented in a financial report. As stated by Wirama (2002), earnings management that is done repeatedly by management in the long-time impacts companies because financial report released by companies does not fully represent the companies’ actual condition.

Realizing the importance of the public and stake holder’s trust in supporting the survival of a company, regulators in Indonesia such as Otoritas Jasa Keuangan (Financial Service Authority) and Bursa Efek Indonesia (Indonesia Stock Exchange) have tried to protect the activities of corporations from the management’s opportunistic behavior by implementing the concept of good corporate governance (GCG). Cornett et al. (2006) along with Gulzar &
Zongjun (2011); Murhadi (2009); Chung and Hsiang (2007) in their research, discovered the negative impact of corporate governance mechanism on discretionary accruals as a measurement of earnings management. The implementation of CG concept is expected to raise oversight and transparency in a company, so that CG acts as a factor, which influences the behavior of management regarding the conduct of earnings management as mentioned by Watts (2003) which stated the implementation of corporate governance (CG) as one of the ways to monitor contract issues and reduce the management’s opportunistic behavior.

This research tries to figure out the effect of company size, leverage and corporate governance implementation on earnings management. Even though previous research on the impact of company size on earnings management has been widely studied, many of its finding are on the contrary, such as the study of Alviantini (2013), Nassirzadeh et al. (2012), Kouki et al. (2011), Halim et al. (2006) and Kim et al. (2003) which discovered that the firm size have positive impact on earnings management. However, on the contrary, other research such as Swastika (2013), Tangjiprom (2013), Rezaei and Roshani (2012), and Wuryani (2012) discovered a negative relation between the firm size and earnings management.

Previous studies on the influence of leverage on earnings management also produced contrary results, such as the research of Shiri et al. (2012), Roodposhti and Chashmi (2011), and Bekiris and Doukakis (2011) which revealed that leverage has positive impacts towards earnings management, while a study by Nejad et al. (2012), and Wasimullah (2010) found negative results between leverage and earnings management.

In contrast to previous research (Alviantini 2013; Nazzizadeh et al. 2012; Nejad et al. 2012; Bekiris and Doukakis 2011; Gulzar and Zongjun 2011; Kouki et al. 2011; Wasimullah 2010; Murhadi 2009; Chung and Hsiang 2007; Halim 2006), this research is not only to examine the influence of firm size, leverage or CG on the practice of earnings management partially. This research will also examine the effect of CG as a moderating influence of firm size and leverage on earnings management. The implementation of CG in a company functions as a supervising factor on the entire course of a company’s activities that can pressure various acts of opportunistic behavior in a company, hence a good implementation of CG can strengthen or weaken the effect of firm size and leverage towards the conduct of earnings management. Hence, the addition purpose of this research is figure out the influence of CG towards the relation of firm size and leverage towards earnings management.

2. THEORETICAL FRAMEWORK AND HYPOTHESIS

Earnings management is a phenomenon, which cannot be avoided due to the management’s discretion in the use of accrual basis when preparing financial statements. This accrual principle is agreed upon as a basis for financial statements preparation due to the fact that the basis of accrual is indeed more rational and fair in comparison to cash basis (Setiawati 2002). However the discretion possessed by management can create various motivations that can push managers to perform earnings management. For instance, manager becomes motivated to report lower profit, one of them being to reduce political cost, among others to reduce workers unions demand, minimize company income tax or avoid other government regulations that reduce company income. Thus, the total accruals can be differed to two different parts of accrual: accruals that are naturally present in the process of preparing a financial statement (nondiscretionary accruals) and discretionary accruals that includes estimation, the selection of accounting policies, allocation, as well as decision that includes management’s policy that is subjective.

Numerous motivations can push managers to perform earnings management. For example, managers can attain a number of reasons to lower the report of earnings. One of them is lowering political cost, an example of a reaction towards the demands of workers union, to avoid other government relations that can reduce company’s revenue which is known as political cost hypothesis or size hypothesis (Watts and Zimmerman (1986). The size hypothesis shows that the larger the company is, the larger the probability of the company to choose an accounting method that will lower earnings, with the purpose to reduce the political cost, in order to avoid government actions of implementing more regulations that can lower the company’s revenue. This condition shows that firm size can motive management to practice earnings management. However, previous research is not always in line with that hypothesis. Alviantini (2013), Nassirzadeh et al. (2012), Kouki et al. (2011) and Halim et al. (2005) in their researches attained results that firm size impacts positively on earnings management. Firm size is a scale where the size of the companies can be classified from a number of methods or standpoints: its total assets, total sales, the market value of the stock and others. In this research the firm size is proxied by using the total asset logs.
H1: Firm size has an effect on earnings management.

The management can also be motivated to choose an accounting method, which can impact on the increase of earnings. Companies sometimes have debts that contain specific covenants based on accounting numbers, usually in a form of money ratio. Leverage ration can picture how large the operations of a company are being funded by debt. Companies with high leverage level can be motivated to perform earnings management so that they will be spared from debt covenant violation. The violation of such violations can have a huge impact towards the company’s reputation from the external’s parties perspective, because companies that have high debt ratio will find difficulties additional funds from creditors, as a matter of fact such companies are threatened in violating debt covenant, as mentioned in the debt covenant hypothesis (Watts and Zimmerman, 1986). Research conducted by Shiri et al. (2012), Roodposhti and Chashmi (2011), and Bekiris and Doukakis (2011) showed that leverage influences earning management. In this case, earnings will usually be reported higher. This is done to maintain the company’s reputation from the external parties perspective, because companies that have high debt ratio will find difficulties additional funds from creditors, as a matter of fact such companies are threatened in violating debt covenant violation. The violation of such violations can have a huge impact towards the company’s reputation from the external’s parties perspective, because companies that have high debt ratio will find difficulties additional funds from creditors, as a matter of fact such companies are threatened in violating debt covenant, as mentioned in the debt covenant hypothesis (Watts and Zimmerman, 1986). Research conducted by Shiri et al. (2012), Roodposhti and Chashmi (2011), and Bekiris and Doukakis (2011) showed that leverage influences earning management. In line with the debt covenant hypothesis, the high level of leverage attained by a company can motivate the management to perform earnings management so that they can avoid the violation of debt covenant.

H2: Leverage has a positive effect on earnings management.

CG concept is basically a matter of controlling and directing the activities of corporations, in order to achieve harmony between major parties such as are shareholders, management, board of directors along with stakeholders, including employees, suppliers, customers, bank and other creditors, regulators, environment and the general public, so that the corporation provides benefit as a whole (Kaen 2003:17).

According to the National Committee of Governance Policy—KNKG (2006), the implementation of CG can be pushed from two drives: ethics and regulation. The ethical driven push comes from the awareness of businesses to practice their business in a way that prioritize the survival of the company, stakeholders’ interest, and evade ways that create short-term gains. On the other hand, regulatory driven push forces companies to obey the existing laws and regulation.

There are five existing CG (TARIF) which are formulated by the Organization for Economic Corporate Governance and Development—OECD (2004), these five existing CGs are: (1) Transparency (includes the release of adequate information, accurate and timely towards company’s stakeholders); (2) accountability (emphasizes on clear function, structure, system and accountability, so that company management is performed effectively; (3) responsibility (demand companies in performing their business activities with full responsibility); (4) independency (demand company managers to act independently and professionally based on their role and functions without any pressure from parties that are not in accordance to the company’s existing operating system); and (5) fairness (fair and equal treatment in both service and information in order to fulfill the rights of stakeholder which arises based on existing agreements and regulations).

The continued development of study and research regarding CG has created a measurement, which represents the implementation level of CG by companies. Such measurements are scores or CG indexes, which is the ranking of companies based on the implementation of CG. In Indonesia index CG can be measured by Indonesian Institute of Corporate Governance (IICG) with its CG index known as Corporate Governance Perception Index (CGPI) and Indonesian Institute for Corporate Directorship (IICD) with its Corporate Governance Scorecard (CGS).

Murhadi (2009) in his research concludes that the practice of CG has a negative impact towards earnings management conducted by a company. Gulzar and Zongjun (2011) their research shows that the characteristics from the corporate governance mechanism play an important role in reducing earnings management. The implementation of corporate governance proves in limiting the tendency of management to perform earnings management and actually directs the presentment of a financial report with higher credibility (Bekiris and Doukakis 2011). The research of Chung and Hsiang (2007) showed that the implementation of CG could reduce the earnings management behavior. Hence, CG can affect earnings management directly and indirectly through firm size and leverage.

Based on such description, therefore the hypotheses proposed in this study are:

H3: Corporate Governance has a negative affect on earnings management

H4: Corporate Governance (CG) weakens the relation of firm size on earnings management.

H5: Corporate Governance (CG) weakens the relation of leverage on earnings management.

The relation of those variables can be explained by the relation of each variable on the Figure 1.
3. RESEARCH METHOD

Data and Sample Selection

This research uses secondary data acquired from the Indonesian Stock Exchange by accessing the official website at www.idx.co.id and also by paying a visit to its Stock Markets Information Center located at PB. Sudirman Street 10X Kav 2 Denpasar-Bali, Phone (0361) 256-701. Data used compromises of company financial report samples, primarily consisting of balance, income statement, and company cash flow reports for the years of 2009-2011. Other than financial data, this research also uses corporate governance index data acquired from IICD, located Jakarta Pusat 10340, Email: info@iicd.or.id and its official website at www.iicd.or.id.

The populations in this research are all companies included in the Indonesia Most Trusted Companies list, based on the Indonesian Institute for Corporate Governance (IICG) research in cooperation with SWA magazine and registered at the Indonesian Stock Exchange from 2009 to 2011, with a total of 79 companies. The selection of such companies as a population in the research is based on its predicate as Indonesia Most Trusted Companies, which is a form of appreciation especially for various companies that display its sincerity in implementing CG as a trusted company. Such appreciation is assessed by independent external parties and is in form of acknowledgement on a company’s commitment and achievement as well as an award for its seriousness and voluntarily willingness in the awareness of the importance of CG implementation.

The procedures of sample selection are done by using a purposive sampling approach, with the following criteria: companies included in the category of Indonesia Most Trusted Companies of 2009-2011 period and listed in the Indonesian Stock Exchange. Companies those are not in the banking and finance industry, due to the fact, such companies have a highly regulated characteristic. Companies that release complete financial reports annually that ends as of 31 December at the time of the observation and 5 years before. It aims to obtain data that supports the calculation of enterprise value and accrual components. Also other criteria are companies that publicize annual financial reports in Indonesian Rupiah. Based on stated criteria a total sample of 47 companies was acquired.

Measurement and Operational Definition of Variables

Dependent Variables

The practice of earnings management in this research is measured by discretionary accrual, which is calculated with the performance-matched discretionary accruals model. This model was developed by Kothari et al. (2005), in which the basic idea is that accruals in a growing company is systematically expected not to be zero, so that the performance of such company is related to accrual. Thus, in order to control the performance that is unusual in estimating discretionary accrual included in performance variables such as the return on assets in calculating non-discretionary accrual (Sulistiawani et al. 2011). Below is a mathematical overview of a performance-matched discretionary accruals model.

\[
\frac{TA_t}{A_{t-1}} = \alpha \left( \frac{1}{A_{t-1}} \right) + \beta_1 \left( \frac{\Delta REV_t - \Delta REC_t}{A_{t-1}} \right) + \beta_2 \left( \frac{PPE_t}{A_{t-1}} \right) + \beta_3 (\Delta ROA_t) + \epsilon_t
\]

\[
TA_t = NI_t - CFO_t
\]
Firm size
darmadji and Sularto 2007). The stocks and sales in measuring the firm size (Sulis relatively stable compared to the market value of a firm size proxy by considering that the total assets by using the total asset logs. Total asset is chosen as total assets, total sales, the market value of the stock from a number of methods or standpoints: its scale where the size of the companies can be classified by a ratio of market value of the firm to its total asset.

Independent and Moderating Variables
The independent variables in this research consist of firm size, leverage and CG. CG variables in this research also act as a moderating variable. Firm size is a scale where the size of the companies can be classified from a number of methods or standpoints: its total assets, total sales, the market value of the stock and others. In this research the firm size is proxied by using the total asset logs. Total asset is chosen as a firm size proxy by considering that the total assets is relatively stable compared to the market value of the stocks and sales in measuring the firm size (Sudarmadji and Sularto 2007).

\[ \text{Firm size} = \log (\text{Total Asset}) \] (5)

Leverage is a ratio that measures the size of assets that are financed by debts. This research uses the debt to total assets ratio calculated by using the equation below:

\[ \text{Leverage} = \frac{\text{Total Debt}}{\text{Total Asset}} \] (6)

CG (Corporate Governance) in this research is measured by using score or the CG index provided by IICD’s (Indonesian Institute for Corporate Directors) research. The CG scorecard method refers to the International Standard Code on GCG determined by OECD (Organization of Economic Cooperation and Development). The score is provided in terms of percentage with a 100 % maximum value. Utama (2010) mentioned that the Corporate Governance Scorecard being used as a CG implementation evaluation tool by the IICD can be categorized to a number of scores: excellence (95-100%), good (80-89%), fair (60-79%) and poor (less than 60%). Each score has its own interpretation based on GCG practice assessment criteria determined by the IICD. CG Scorecard provided by IICD’s research is based on a variety of publicly available information, such as annual report and financial reports released by public companies, meeting minutes, records of the general meeting of shareholders, as well as other publicly available information, so that the result of the evaluation in such scorecard can represent the level of CG implementation comprehensively. Such assessment scores are expected to represent the implantation of CG comprehensively in a company.

Data Analysis Technique
Moderated Regression Analysis
The data analysis technique to test hypothesis 1, 2 and 3 on how does size, leverage, and CG influences earnings management in this research uses moderated regression analysis (MRA). But, the CG variable test as a moderating variable for the relation of size and leverage on earnings management with this MRA technique has a likelihood of high multicollinearity among independent variables and this can violate classical assumptions. So as to test hypothesis 5 and 6, namely whether the CG variables affect the relationship of size and leverage on earnings management is to use residual test.

The statistical equations used are as follows

\[ DA_{it} = \alpha_{it} + \beta_1 \text{SIZE}_{it} + \beta_2 \text{LEV}_{it} + \beta_3 \text{CG}_{it} + \beta_4 \text{SIZE}_{it} \times \text{CG}_{it} + \beta_5 \text{LEV}_{it} \times \text{CG}_{it} + \epsilon_{it}. \] (7)

Description:
\( DA = \) Discretionary accruals (Earnings Management)
\( \alpha = \) Constants
\( \text{SIZE} = \) Firm size
\( \text{LEV} = \) Leverage
\( \text{CG} = \) Corporate Governance
\( \text{SIZE} \times \text{CG} = \) Interaction between firm size and corporate governance
\( \text{LEV} \times \text{CG} = \) Interaction between leverage and corporate governance
\( \epsilon = \) error term.
Regression coefficient ($\beta$) shows the magnitude of the changing of dependent variable when the independent variable changes one unit. The relationship direction from such regression coefficient indicates the relationship direction between independent variable and dependent variable. The acceptable level of error in this statistical testing is ($\alpha$) 5%.

Residual Test

Hypothesis 4 and 5 will be tested with residual test. Residual test is used to discover whether corporate governance (CG) can moderate the relation between firm size (SIZE) and leverage (LEV) on earnings management (DA).

The steps of residual examinations are as follow.
1. Regressing between CG towards SIZE as well as LEV to gain residual value ($e$). The statistical equation, which can be used, is as follow.
   \[
   CG_{it} = \alpha_{it} + \beta_6 SIZE_{it} + \epsilon_{it}.
   \] (8)
   \[
   CG_{it} = \alpha_{it} + \beta_7 LEV_{it} + \epsilon_{it}.
   \] (9)
2. Finding the absolute value of residuals ($|e|$).
3. Regressing the absolute value of residuals gained from equation 8 and 9 with DA variable as its independent variables. If the coefficient parameter value is negative and significant, then the CG variable is a moderating variable. The statistical equation used is as follow.
   \[
   |e| = \alpha + \beta_8 DA.
   \] (10)
   \[
   |e| = \alpha + \beta_9 DA.
   \] (11)

Description:
- $DA = $ Discretionary accrual
- $\alpha = $ Constants
- $SIZE = $ Firm size
- $LEV = $ Leverage
- $CG = $ Corporate Governance
- $e = $ lack of fit residual
- $\beta_8 - \beta_9 = $ Coefficients of regression
- $i = $ Industry
- $t = $ Year

The residual analysis testing the deviation effect (absolute residual value) of a particular model is a lack of fit resulted from the deviation of the linear relationship between the independent variable. Lack of fit is indicated by the residual value in a regression (Ghozali 2011: 207). The coefficient value of $\beta_8$ and $\beta_9$ on the regression equation of (10) and (11) pictures whether CG variable is a moderating variable can be seen on its significant and negative results (which means the presence of lack of fit between firm size and CG as well as between leverage and CG results the decrease of DA or negatively effecting).

4. DATA ANALYSIS AND DISCUSSION

Based on the results of interaction tests (MRA), the conclusion of interaction tests (MRA) is shown at Table 1.

The F test results shows that significant value at 0.000 so that it can be concluded that the regression model can be used to predict the influence of firm size, leverage, as well as CG towards earnings management partially and can be used to discover the effect of CG towards the relationship of firm size and leverage towards earnings management. The determining coefficient ($R^2$) = 0.481 has a meaning that 48.1 percent of the earnings management changes (DA) variable is influenced by firm size, leverage and CG simultaneously while 51.9 percent of the rest is explained by other variables that is not included in this research model.

A partial test performed by a t-test. This t-test is done to find out the effect of independent variable partially towards its dependent variable. The results of the test partially are as follow;

The first hypothesis (H1) states that firm size positively affects earnings management. The purpose of the test is to find out the influence of firm size towards earnings management. Based on the statistical test results are shown in Table 1, that firm size positively affects earnings management; this can be proved by seeing the positive regression coefficient value positive (0.046) as well as the smaller significant value of 0.003, smaller than the significant level of $\alpha = 0.05$. Thus the H1 hypothesis value, which states that firm size positively, effects earnings management can be accepted. In this case firm size can motivate management to perform earnings management. The larger the size of a company means the larger the chance for a company to earn profit from its business activity. The faster the expansion of a company occurs, the more complex its operational activities gets and most certainly the company will be demanded to fulfill its investors expectations, in this case there could be more pressure to perform earnings management. So as the larger the company gets, there would probably be more motivation for larger management to perform earnings management. This research supports previous research of Alviantini (2013), Nassirzadeh et al. (2012), Kouki et al. (2011), Halim et al. (2006) and Kim et al. (2003) Kim et al.(2003), Halim et al. (2005), Koukiet al. (2011), Nassirzadeh et al. (2012), and Alviantini (2013), which states firm size influences positively on earnings management. The results of such statistic test provided findings in contrary with political cost hypothesis (size hypothesis) from Watts and Zimmerman (1986) which shows that the larger
the size of the company, the larger the probability of such company to choose an accounting method that will decrease profits with the purpose to decrease political cost, hence avoiding government action which can decrease company income by implementing more regulation. This research is also in contrary towards the research of Swastika (2013), Tangjit-prom (2013), Rezaei and Roshani (2012), and Wury-ani (2012) which discovers negative effects of firm size towards earnings management.

The second hypothesis (H2) states that leverage positively affects earnings management. The purpose of this test is to discover the effect of leverage towards earnings management. Based on the statistical test result in Table 1, it shows that leverage does not influence earnings management. Such fact is based can be proved by viewing the negative coefficient regression $b$ value (-0.018) as well as significance level of 0.775 larger than the significant level of $\alpha = 0.05$. Thus, the (H2) hypothesis results which states that leverage positively affects earnings management is rejected.

The lack of influence from the leverage shows that debt covenant agreement done by Indonesia Most Trusted Companies with debt holders is not the only factor that can motivate management to perform earnings management. Management will likely seek to avoid consequences from the violation of debt covenant, due to the fact that managing numbers related to debt transactions will most likely give burden to companies, such as the probability of the acceleration of debt maturities, the increase of interests as well as renegotiation of the debt time length (Beneish and Press 1995 in Herawati and Baridwan 2007). Furthermore, tight monitoring on the company by debt holders exists in Indonesia Most Trusted Companies. Debt holders by themselves will try to supervise the use of funds implanted in such companies; moreover the mandatory implementation of CG concept could influence the behavior of management in providing information related with debt holder. Supporting the research by Mashayeekhi and Bazaz (2008), Azlina (2010), Susilowati et al. (2011) and Ardison et al. (2012) which states that leverage does not influence earnings management.

The third hypothesis (H3) states that CG negatively influences earnings management. The purpose of this research is to figure out the influence of CG towards earnings management. Based on the statistical test with SPSS (Table 1), it shows that CG negatively affects earnings management. Such findings can be proved by looking at the negative regression coefficient value (-0.003) as well as the significance level which is 0.018 smaller than the significance level of $\alpha = 0.05$. Thus the H3 research hypothesis that states that CG negatively affects earnings management can be accepted. The result of this test means that the better the CG concept is implemented in a company, then the smaller the actions of earnings management will be. This means that the Indonesia Most Trusted Companies those implements the CG concept properly is a company that has oversight mechanisms, which most certainly will protect every stockholder’s interest.

Considering how important is public trust or other stockholder’s trust in supporting the survival of a company, the implementation of CG in a com-

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**Table 1**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Regression Coefficient</th>
<th>Statistic t</th>
<th>Significance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size</td>
<td>0.046</td>
<td>3.123</td>
<td>0.003</td>
</tr>
<tr>
<td>Leverage</td>
<td>-0.018</td>
<td>-0.288</td>
<td>0.775</td>
</tr>
<tr>
<td>Corporate Governance</td>
<td>-0.003</td>
<td>-2.472</td>
<td>0.018</td>
</tr>
<tr>
<td>Size*CG</td>
<td>-0.040</td>
<td>-2.707</td>
<td>0.010</td>
</tr>
<tr>
<td>Leverage*CG</td>
<td>0.087</td>
<td>2.378</td>
<td>0.022</td>
</tr>
</tbody>
</table>

Statistic F =0.000  
R²= 0.481

---

**Table 2.**

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstd. Coefficients</th>
<th>Std. Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>5.953</td>
<td>.550</td>
<td>10.823</td>
<td>.000</td>
</tr>
<tr>
<td>Training</td>
<td>-8.824</td>
<td>4.234</td>
<td>-2.084</td>
<td>.043</td>
</tr>
</tbody>
</table>

a. Dependent Variable: AbsRes_Size
pany now has become mandatory for the companies registered in the Indonesian Stock Exchange. This CG concept will give balance in managing a company that harmonizes the management and stakeholders’ interest in achieving the company’s main goal, so that a good business climate will be created as a level of achievement towards a result of efforts in meeting requirements, showing priority and regularity of its operations based on CG concept (FCGI 2001). Referring to the principles developed by OECD by paying attention to the requirements from Financial Service Authority (OJK) as well as Indonesian Stock Exchange (BEI), guidelines are drafted which can be a reference in implementing CG concept in Indonesian which contains the following aspects: (1) the protection of the rights of shareholders, (2) the equitable treatment of shareholders, (3) the role of stakeholders in corporate governance, (4) disclosure and transparency and (5) the responsibilities of the board.

The results of this research shows that the implementation of CG concept can lower the acts of earnings management, due to the fact that a good CG concept implementation exists will make operational activities of a company to be more controlled, thus it can go in accordance to the expected company’s goal. The result of this research is in line with the findings of Chung and Hsiang (2007), Gulzar and Zongjun (2011), as well Sun and Yong (2012), which shows that the implementation of CG negatively influences earnings management.

Table 2 and 3 explain the hypothesis 4 (H4) and hypothesis 5 (H5) states that the implementation of CG weakens the relationship between firm size and earnings management and the implementation of CG weakens the relationship between leverage and earnings management respectively. Based on the residual test, it shows that CG can moderate relation between firm size and leverage on DA. The results of residual tests by using residual tests shows that CG can moderate firm size as well leverage on earnings management. Results of the residual test for firm size and leverage shows that the sig. value as large as (0.043< 0.05) as well as a negative beta coefficient of (-8.824) for an absolute residual firm size value, while the sig. value of (0.031< 0.05) and its negative beta coefficient of (-9.343) for an absolute residual leverage value. The results of such test is parallel to the requirements in a residual test, where the significant (sig.) value as well as the negative parameter coefficient value (beta value) (which means there is a lack of fit between CG and DA), means that the CG variable can affect the relation of size and leverage on earnings management.

5. CONCLUSION, IMPLICATION, SUGGESTION AND LIMITATIONS
This research examines the influence of firm size, leverage, as well as corporate governance towards the practice of earnings management, by having a moderating CG variable. Based on the results and discussions in this research, we obtained the following conclusions and recommendations.

This research discovered that a positive influence between firm size and earnings management exists. This finding is not in line with one of the hypothesis in the positive accounting theory: political cost hypothesis (size hypothesis) which shows that the larger the size of the company, the greater the likelihood the company will perform earnings management, by selecting accounting methods that will lower profit.

The finding of leverage in this research shows that there is not enough prove to state that the higher the leverage the higher the conduct of earnings management. This finding is not in line with the views of debt covenant hypothesis, which states that the higher the debt/equity, the more likely the manager uses accounting procedures and method in increasing accounting profit.

Corporate Governance (CG) shows negative effects on earnings management. This finding suggests that a negative direction exists between CG and the act of earnings management. This result is in line with the hopes of implementing CG concept on a company, where a company that implements CG principles will become better and most certainly opportunistic behaviors such as earnings management can be suppressed.

This research also proves that CG can moderate

| Table 3
Residual Test Result for Moderation on Leverage

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstd. Coefficients</th>
<th>Std. Coefficients</th>
<th>t</th>
<th>Sig</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 (Constant)</td>
<td>6.153</td>
<td>.547</td>
<td>11.257</td>
<td>.000</td>
</tr>
<tr>
<td>Training</td>
<td>-9.343</td>
<td>4.208</td>
<td>-.314</td>
<td>-2.220</td>
</tr>
</tbody>
</table>

a. Dependent Variable: Commitment
the influence of firm size as well as leverage on earnings management or interaction of CG with firm size as well as leverage in influencing the acts of earnings management. This means that the result of this research explains that the implementations of CG concept can weaken the relationship between firm size and leverage by the conduct of earnings management performed by management. The CG concept has a range of monitoring and control mechanisms that can protect all the interests of the stakeholders, so that it can create an alignment in achieving the intended corporate goals. The road towards the establishment of good corporate governance is not easy, it needs commitment, consistency and sincerity of the various parties involved in it. Companies that have implemented CG concept should fully ensure implementation of CG principles on every business aspect and company ranks not just as a mere adhere to the rules of discourse and legislation in force.

This research only used firm size, leverage and corporate governance variable in its examination. Based on the determinations test’s results (R2), as much as 48,1 % of the earnings management changes variance, it can be explained by the independent variable made up of firm size, leverage and CG, while the remaining 51,9 % is explained by other variables which is not included in this research model. The adding of other variable that are perceived to be related to earnings management can be used, while still including firm size and leverage variable to find out the difference of the results obtained.

This research only uses company that attained the predicate of Indonesia Most Trusted Companies and uses limited sample and population; as a result the results of this research cannot be broadly generalized to every public company in Indonesia. So for future research, it is recommendable to use samples that are more accurate by using all companies listed in the Indonesian Stock Exchange, manufacturing and other industries as well as the adding of annual observation samples.

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