

The Influence of Corporate Governance Mechanisms and Investment Opportunity Set on Earnings Management

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ABSTRACT

The aim of this study was to analyze the influence of corporate governance mechanisms and investment opportunity set on earnings management practices in Indonesia. This study used a sample of 20 manufacturing companies listed in the Indonesia Stock Exchange (IDX) in 2010-2014 and the sample selection is based on judgment sampling. Results from this study showed corporate governance mechanisms has no affect on earnings management practices and investment opportunity set negatively affect earnings management practices. This is because the implementation of corporate governance is still relatively new in Indonesia so the goal has not been effectively felt. In addition, the corporate governance implementation has started being applied in the business world, but implementation still not fulfilled either. Earnings management practices cannot be fully carried out by only having a great number of investment opportunity set. Companies that have the auditor from the Big 5 will have lower possibility of discretionary accruals actions undertaken by management.

Key Words: Corporate Governance Mechanisms, Investment Opportunity Set, Earnings Management.

BACKGROUND

Earnings management is often perceived negatively by peoples because in general the earnings management causes the appearance of financial statement information (financial reporting) does not reflect the real situation. Earnings management has always been considered as an opportunistic behavior, which in this case the management to act for their own interests (Wibisono, 2004).

In the agency theory, principal and agent are rational actors where each party wants to maximize his utility. Principal in this case is the owner of the company or shareholders who have an interest to increase the value of the firm, while the manager who acts as the agent concerned to increase the compensation received from managing the company, either in the form of salaries, bonuses or other incentives. The interests of both sides can be aligned, if the conditions are good company, perceived well by investors, shareholder wealth increases,

managers prosperous and value of the firm increases. But in reality, the interests of both sides are not parallel that cause information asymmetry, so that differences in the interests of both parties need to be arranged in a compensation contract. Findings Richardson (1998) in Rahmawati (2006) states that the information asymmetry leads to earnings management.

Earnings management problems can be minimized by monitoring themselves through good corporate governance (GCG). This earnings management practices minimized through a monitoring mechanism to harmonize different interests as the owner and manager of the company management (Herawaty, 2008).

Supervisory capital markets need to improve the supervision of offenders in the stock investment to ensure the sustainability of capital market transactions and maintain balance in it. Control can be done by applying good corporate governance or good corporate governance. Watts (in Ujiyantho) states that one of the means used to monitor the issue of contracts and restrict opportunistic behavior management is corporate governance. Corporate Governance Task Force of the National Committee on Corporate Governance Chapter II: is a process and structure used by the company to provide additional value to the company on an ongoing basis to the shareholders in the long term, to keep watching the interests of shareholders, based on the regulations and norms applicable. The concept of corporate governance is proposed in order to achieve a more transparent management of the company for all users of financial statements (Sam'ani, 2008). Corporate governance practices can be run either when applying the principles which consisted of transparency, accountability, findependency, fairness, and responsibility.

Investment Opportunity Set shows the company's investment or growth options. The growth in the value of the option depends on the discretionary expenditure manager. Gaver and Gaver (1993) states that the investment value of these options depend on discretionary expenditures incurred by the manager in the future. The choices of investments made in the future the company then known as the investment opportunity set or investment opportunity set (IOS) (Kallapur and Trombley, 2001). Results of research Wah (2002) states that companies with high investment opportunity are more likely to have discretionary accrual (accrual under management) is high. In addition, research Rachmawati and Triatmoko (2007) states that the variables that affect the Discretionary Accruals (DA) only Investment Opportunity Set (IOS). Results were consistent with the view that the greater the investment opportunity set (IOS) an enterprise the greater the opportunity to perform management through the opportunistic nature of earnings management practices that affect the quality of the company's profit generated.

The aim of this research is to analyze the influence of Corporate Governance mechanisms and Investment Opportunity Set on Earnings Management practices.

LITERATURE REVIEW

Agency Theory

According to Anthony and Govindarajan (2005: 269), agency theory is the relationship between principal and agent. Principal employs an agent to

perform tasks for the benefit of the principal including the delegation of decision-making authorization from the principal to the agent. At companies whose capital is composed of shares, acts as the principal shareholder and CEO (Chief Executive Officer) as their agent. Shareholders hires CEO to act in accordance with the interest of the principal.

Agency theory assumes that every individual is motivated by self-interest that can lead to conflict between principal and agent. The principals are motivated to contract for the welfare of her with ever-increasing profitability. Instead, the agent is motivated to maximize the economic needs and psychology.

In the agency theory, shareholders and managers are rational actors because each party wants to maximize his utility. The interests of both parties can be aligned. If the company condition is good, the investors will perceive the company well , the shareholders' prosperity increase, manager is welfare, and the value of the firm increases. However, in reality, the interests of both sides are not parallel that cause assymetry information so that differences in the interests of both parties need to be regulated in a contract compensation.

Corporate Governance

Corporate governance is the principle of the management company that aims to encourage the performance of the company as well as provide economic value for shareholders. Corporate governance is basically a system and a set of rules that govern the relationship between the various interested parties, especially in the narrow sense of the relationship between shareholders, board of directors, and the board of directors for the achievement of company objectives (Zarkasyi, 2008: 36). Forum for Corporate Governance in Indonesia (2003) stated that beneficial application of corporate governance as follows:

1. Improve the performance of companies through the creation of a decision-making process better, including the operational efficiency of the company, and as an effort to improve service to stakeholders.
2. Simplify obtaining more financing funds in order to increase corporate value.
3. Especially for companies, will be able to help reception for the state budget mainly from privatization proceeds.
4. Minimize management capabilities perform actions that may be detrimental to shareholders.
5. Reduce the high cost economy especially at the corporate level.
6. Attract foreign investors to invest in Indonesia.

According to the Forum For Corporate Governance In Indonesia (FCGI, 2003) in corporate governance must address: (a). Fairness; (b). Transparency; (c). Accountability; (d). Responsibility; (e). Independency.

The essence of corporate governance is improving corporate performance through supervision or monitoring the performance of management and the accountability of management to other stakeholders, based on the framework of rules and regulations (Kaihatu, 2009). In FCGI (2003) corporate governance mechanisms include the board of directors, audit committee, managerial ownership and institutional ownership.

Corporate Governance Mechanisms

As for the corporate governance mechanism is a proxy of the study, among others:

1. Board of Independent Commissioner

Basically, all the commissioners are independent, meaning that they were expected to perform his duties independently, solely in the interest of the company, without influence from other parties. The existence of independent directors is intended to create a climate that is more objective and put fairness among the various interests of the company and the interests of stakeholders as a key principle in decision making by the board of commissioners. To further strengthen the effectiveness of independent directors, the number of independent directors at least 30% of the total number of directors or at least 1 (one) person (indicated on the letter of the rules of directors of a number Kep-305 / BEJ / 07/2004).

2. Audit Committee

In accordance with Kep. 29/PM/2004, the audit committee is a committee established by the board of directors to carry out the task of supervision of the management of the company. In the framework of the implementation of good corporate governance (GCG), BEI require listed firms are required to have independent directors and audit committee. Membership of the audit committee of at least three members, one of them independent directors listed companies as well as a chairman of the committee, while the other party is external parties that are independent and minimal one has the ability in the fields of accounting and finance (listed on the provisions of the letter of directors numbers kep-305 / BEJ / 07/2004).

3. Managerial Ownership

Jensen and Meckling found that managerial ownership manages to be a mechanism to reduce agency problems of managers by aligning the interests of managers and shareholders. Their study found that the interests of managers with external shareholders can be put together if the ownership of shares by managers is enlarged so that the manager would not manipulate earnings to their interests (Herawaty, 2007).

4. Institutional Ownership

Institutional investors often referred to as a sophisticated investor that should be able to use the current period information in predicting future earnings than non institutional investors. The results of the research results Jambavo et al described in Vinola study states that there is a feedback effect of ownership institutional which can reduce the profits of the company management. If the efficient management of such profits, the high institutional ownership will improve the management of return but if management of the company profits are opportunists so that high institutional ownership will reduce earnings management (Herawaty, 2007).

Investment Opportunity Set

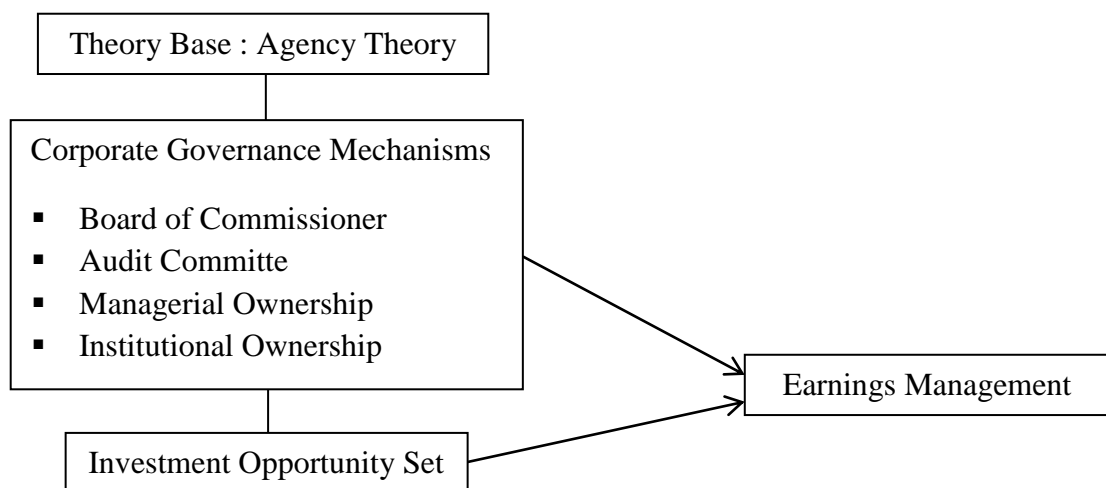
Term investment opportunity set (IOS) is first raised by Myers (1977) which is a picture of the extent or magnitude of investment opportunities so that high or low levels of the value of the company depends on spending decisions, such advertising is used to guarantee the sustainability of the company. IOS is an unobservable variable is therefore necessary to use a proxy (Kallapur and Trombley, 2001). IOS proxies that have been used by researchers in Kallapur and Trombley (1999) can generally be classified into three types, namely: proxy based on prices, proxied by the investment, and proxies based measurement variants.

Earnings Management

Earnings management is an action taken by management to raise or lower the reported income of the unit under his responsibility that does not correspond with the increase or decrease in the company's profitability in the long term. Thus, earnings management can be interpreted as a measure of earnings management that affect reported earnings and provide economic benefits to the company wrong, so that in the long term it will be very annoying and even harmful to the company. Earnings management is driven by Several motivations. Scott (2003: 377) argued that there are several factors that can motivate managers perform earnings management, namely: the bonus scheme (bonus plan), debt covenant (contract long-term debt), political motivations, taxation motivations, chief executive officer (CEO turnover), and the initial public offering (IPO).

Research Framework

Based on the description of the theory and the result of previous studies, research framework in this study as follows:



Note : —————> = Affects

Hypothesis

H14: Corporate Governance Mechanisms negatively affects on Earnings Management Practices

H2: Investment Opportunity Set negatively ~~positively~~ affects on Earnings Management Practices

RESEARCH METHODOLOGY

Population and Sample

The population of the study is manufacturing companies listed in Indonesian Stock Exchange (BEI) during 2010-2014. The basic considerations for selecting companies listed on the Stock Exchange is that this sector has a relatively large and complex accounts which allow managers to perform earnings management practices. The sample selection is based on judgment sampling, the sampling is based on “consideration” researchers regarding manufacturing companies which are appropriate (meets requirements) to be sampled. The judgment of sampling is not random, but it is selected based on the information obtained by using certain considerations (Indriantoro and Supomo, 2002:131).

Table 3.1
Sample Selection Procedure

No.	Sample Criteria	Amount
1.	Companies are listed on the Indonesian Stock Exchange in 2010-2014 which publish its financial statements not more than December 31 st .	141
2.	Companies do not generate consecutive profit during the observation period.	(79)
3.	Companies do not have complete data on managerial ownership in a row during the observation period.	(42)
	Number of samples	20
	Total sample data during the period (2010-2014)	100

Source: Capital Market Directory Appendix 1

Type and Source of Data

The quantitative data is data in the form of numbers and can be analyzed systematically (Sugiyono, 2005:131). Quantitative data in this study is the annual financial statement data manufacturing companies listed on the Indonesian Stock Exchange in 2010-2014.

Source of data captured by researchers in the study came from the Indonesian Stock Exchange (IDX) in Jakarta obtained from ICMD (Indonesian Capital Market Directory) and www.idx.co.id.

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Variable and Hypothesis

Exogenous Latent Variable

Exogenous latent variables in this study includes Corporate Governance mechanisms and the Investment Opportunity Set. The following will explain how to measure both the exogenous variables.

1. Corporate Governance Mechanisms

There are four proxy for corporate governance mechanisms used in this study, namely:

a. Independent Commissioner

Independent Commissioner is measured by counting the number of independent commissioner divided by the total number of commissioners present in the composition of the board of commissioners.

b. Independent Audit Committee

Understanding the Audit Committee in the decision of the Chairman of Bapepam Number: Kep-29/PM/2004, dated 24th September 2004 number IX.1.5 Regulation on the Establishment and Implementation of the Audit Committee. It is a committee established by the board of commissioners to carry out the task of monitoring the processing companies. Independent audit committee is measured by dividing the number of independent audit committee (independent commissioner who became chairman of audit committee) with a total number of audit committee in the composition of audit committee.

c. Managerial Ownership

Managerial ownership is the number of stock own by management of the entire share capital being managed. Managerial ownership is measured by counting the shares owned by management and actively participate in corporate decision (commissioners and directors) divided by number of shares outstanding.

d. Institutional Ownership

Institutional ownership, the shares are held by institutional investors. Institutional ownership is measured by counting the number of shares owned by institutional investors divided by the total number of shares outstanding.

2. Investment Opportunity Set

There are three measurements IOS latent variables in this study, namely:

a. Market Value of Assets ratio to the Book Value of Assets (MVA/BVA)

This proxy states that the greater this ratio, the lower the ratio of assets in place to firm value and the greater the value of the company's growth opportunities. Researcher also measures the growth variables using the

market value of the company divided by the company's assets as defined as follows:

$$\text{MVA/BVA} = \frac{[\text{Total assets} - \text{Total ordinary equity} + (\text{Shares outstanding} \times \text{Closing price})]}{\text{Total assets}}$$

- b. Ratio of market value of equity to the Book value of equity (MVE/BVE)
This proxy is used because there is a difference between market value and book value of equity which are included in the company's value investment opportunities in the future. The higher this ratio, the greater the value of the company's growth opportunities are defined as follows:

$$\text{MVE/BVE} = \frac{\text{Number of shares outstanding} \times \text{Closing price}}{\text{Total equity}}$$

- c. Ratio Capital Additions to Book Asset Value (CAP/BVA)
Ratio CAP/BVA shows the flow of additional share capital of the company which shows the ratio is positively correlated to the assets and equity of the company, which is formulated as follows:

$$\text{CAP/BVA} = \frac{\text{Additional capital in one year}}{\text{Total assets}}$$

Endogenous Latent Variable

Endogenous latent variable in this study is Earnings Management. Discretionary Accrual (DA) as a proxy of earnings management.

Modified Jones Model (1995) is used to detect the presence of earnings management practices because this model is considered as the best model in detecting earnings management compared to other models as well as provides results of the most powerful (Dechow et al., 1995; Sutrisno, 2002). This model uses Total Accrual (TA) that is classified into Discretionary Accrual (DA) and Non Discretionary Accrual (NDA).

- a. Total Accrual

$$\text{TA (Total Accrual)} = \text{Net Income} - \text{Cash Flow From Operation}$$

$$\text{TA}_{it}/\text{A}_{it-1} = \alpha_1 (1/\text{A}_{it-1}) + \alpha_2 (\Delta \text{REV}_{it}/\text{A}_{it-1}) + \alpha_3 (\text{PPE}_{it}/\text{A}_{it-1}) + \varepsilon$$

Description:

- T_{ait} : Total accruals for manufacture i in year t
A_{it-1} : Total assets for sample manufacture i at the end of the year t-1
ΔREV_{it} : Changes in income of manufacture i in year t-1
PPE_{it} : The fixed assets of the manufacture i in year t
α₁, α₂, α₃ : Regression coefficients
ε : error

The above equation regressed to get the value of α_1 , α_2 , and α_3 . This value is then incorporated into the calculation of the value of NDA to get the Modified Jones Model (1995).

b. Accrual normal levels (Non Discretionary Accruals)

$$NDA_{it} = \alpha_1 (1/A_{it-1}) + \alpha_2 (\Delta REV_{it} - \Delta REC_{it})/A_{it-1} + \alpha_3 (PPE_{it}/A_{it-1})$$

Description:

NDA_{it} : Non Discretionary Accruals of manufacture i in year t

ΔREC_{it} : Changes in the manufacture's net receivables i in period t

The value of α_1 , α_2 , and α_3 obtained from the equation TA are included in the calculation of the value of NDA and NDA then is manually counted without regression.

c. Accrual level is not normal (Discretionary Accruals)

Total accruals consist of discretionary and non discretionary accruals, then discretionary accruals can be formulated as follows:

$$DA_{it} = TA_{it}/A_{it-1} - NDA_{it}$$

Description:

DA_{it} : Discretionary accrual of manufacture i in year t

TA_{it} : Total accruals for manufacture i in year t

A_{it-1} : Total assets of the manufacture i in year $t-1$

NDA_{it} : Non discretionary accruals in year t (Modified Jones Model: 1995)

Data Analysis Method

This study uses a partial least squares analysis (PLS) to test the hypothesis. PLS is a statistical method based SEM variant that is designed to complete multiple regression when there is a specific problem in the data, such as the sample size is small, the data is lost (missing values), and multicollinearity (Hartono, 2001: 55)

Evaluation Model

Partial Least Square (PLS) models consist of outer and inner models. According to Sholihin (2013: 16) outer model is a measurement model to assess the significance of weights and multicollinearity of the model, while the inner model is a structural model to predict the quality of the relationship between the latent variables (constructs).

Measurement Model (Outer Model)

According to Hartono (2011: 69) the measurement model (outer model) is used to test the indicator weight of the instrument. The criteria are:

1. The indicator weight must be statistically significant ($\alpha < 0.05$)
2. Multicollinearity: Variance Inflation Factor (VIF) smaller than 3.3

Structural Model Evaluation (Inner Model)

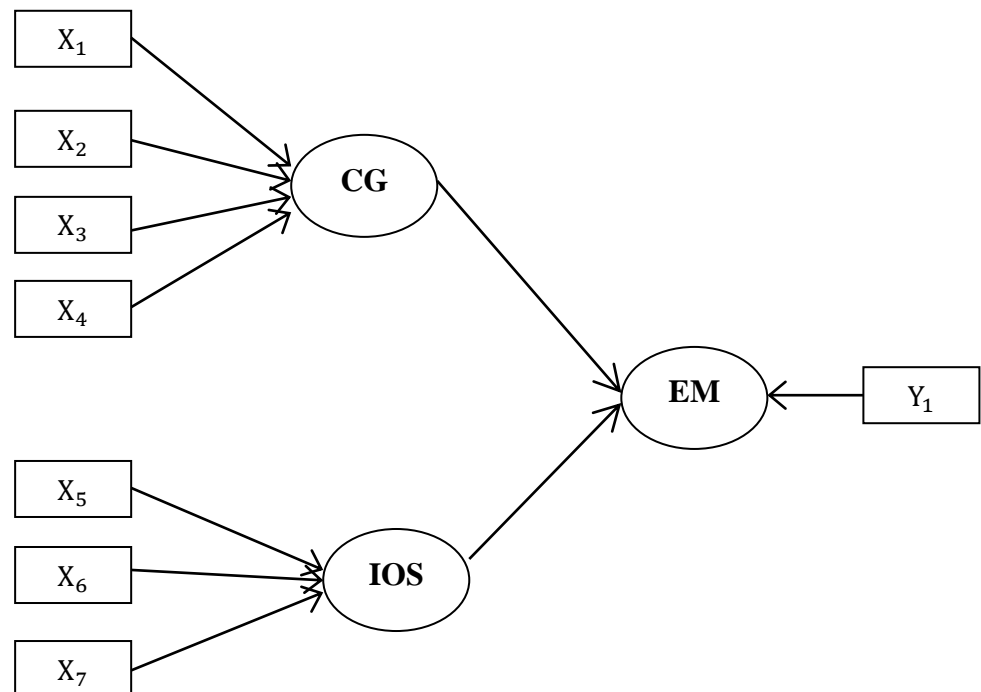
According to Hartono (2011: 69) inner model is a structural model to predict the causal relationship between the latent variables or constructs. Structural models in PLS was evaluated by measuring the value of Q^2 and the path coefficients.

- 1) Q^2 , is used to measure the degree of variation of the change of independent variables on the dependent variable. The higher the value of Q^2 indicates better prediction models of the proposed research model (Hartono, 2011: 72).
- 2) The path coefficient, used to indicate the level of significance in hypothesis testing. Path coefficients value or inner model indicated by the model of the T-statistic values, must be above 1.96 to test the hypothesis on alpha 5 percent (Hair et al., 2008 in Hartono, 2011: 73).

Specification Model

This study aims to explain the influence of corporate governance and the investment opportunity set to earnings management. The structural model shown in Figure 3.1 below.

Figure 3.1
Structural Model



Outer Model

Outer models explaining the relationship between an indicator block with latent variables. Outer equation model in this study can be seen in Table 3.2 below.

Tabel 3.3
Outer Model Equation

Construct	Outer Model Equation
Corporate Governance mechanisms	$CG_1 = \lambda_{x_1}CG + \delta_1$
	$CG_2 = \lambda_{x_2}CG + \delta_2$
	$CG_3 = \lambda_{x_3}CG + \delta_3$
	$CG_4 = \lambda_{x_4}CG + \delta_4$
Investment Opportunity Set (IOS)	$IOS_1 = \lambda_{x_5}IOS + \delta_5$
	$IOS_2 = \lambda_{x_6}IOS + \delta_6$
	$IOS_3 = \lambda_{x_7}IOS + \delta_7$
Earnings Management (EM)	$EM = \lambda_{y_1}EM + \varepsilon_1$

Description: CG_i : exogenous latent variable indicator (corporate governance); IOS_i : exogenous latent variable indicator (investment opportunity set) i ; λ_{x_i} : loading factor on latent variabel indicator i ; Y_1 : endogenous latent variable indicator (earnings management); δ_i : level measurement error exogenous latent variables i ; ε : error

Inner Model

Inner Model describes the relationship of causality between latent constructs are built on the substance of the theory. Inner model equation in this study is:

$$\eta_1 = \beta_1\zeta_1 + \beta_2\zeta_2 + \varepsilon$$

Description:

- η_1 = endogenous latent variable (earnings management)
- β_1 = coefficients influence on GCG
- ζ_1 = GCG construct
- β_2 = coefficients influence on IOS
- ζ_2 = IOS construct
- ε = error

RESULT AND DISCUSSION

Data Analysis Results

This section presents the results of the data analysis. The data has been tabulated then analyzed using regression, descriptive statistics and PLS. The use of descriptive statistics is an attempt to determine the characteristics of the data, while the PLS is used to test hypotheses of the study.

The data used in this research is secondary data such as financial statements, annual report, and share data. Testing was performed on 100 data taken through judgment sampling.

Coefficients Regression of a1, a2, and a3

In this study, earnings management as endogenous construct was calculated by Jones Model 1995. This model uses Total Accrual (TA) that is classified into Discretionary Accrual (DA) and Non Discretionary Accrual (NDA).

Total Accrual

$$TA_{it}/A_{it-1} = \alpha_1 (1/A_{it-1}) + \alpha_2 (\Delta REV_{it}/A_{it-1}) + \alpha_3 (PPE_{it}/A_{it-1}) + \varepsilon$$

The above equation regressed to get the value of α_1 , α_2 , and α_3 .

Table 4.1
Regression of a1, a2, and a3 result

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
Constant	0.045	0.026		1.686	0.095
a1	-376788.115	351806.678	-0.116	-1.071	0.287
a2	0.102	0.044	0.264	2.310	0.023
a3	-0.076	0.069	-0.125	-1.106	0.272

Source : Appendix 2

The equation regression formula is as follow:

$$TA_{it}/A_{it} = -376788.155 (1/A_{it-1}) + 0.102 (\Delta REV_{it}/A_{it-1}) + -0.076 (PPE_{it}/A_{it-1}) + \varepsilon$$

Description of Data

In order to know the characteristics of the data used in this study, conducted descriptive statistical test results can be seen in Table 4.1 below.

Table 4.2
Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Board of Commissioner (X_1)	100	25,00	75,00	38,00	10,35
Audit Committee (X_2)	100	28,00	66,00	34,75	5,52
Managerial Ownership (X_3)	100	0,00	28,00	7,53	9,09
Institutional Ownership (X_4)	100	12,00	87,00	60,67	17,45
MVA/BVA (X_5)	100	-3,00	9,00	1,26	1,89
MVE/BVE (X_6)	100	0,00	12,00	1,98	2,62
CAP/BVA (X_7)	100	-3,00	1,00	-0,07	0,45
Earnings Management (Y)	100	-12,00	0,00	-1,47	2,23

Source : Appendix 5

Hypothesis Test Results

There are two criteria used in the assessment models:

1. Indicator weight must be statistically significant ($<0,05$).
2. Multicollinearity: Variance Inflation Factor (VIF) is smaller than 3.3.

Table 4.3
Results (Outer Model)

	<i>p-value</i>	<i>Variance Inflation Factor (VIF)</i>
$X_1 \rightarrow CG$	<0.001	1,164
$X_2 \rightarrow CG$	0.004	1,043
$X_3 \rightarrow CG$	<0.001	1,271
$X_4 \rightarrow CG$	<0.001	1,486
$X_5 \rightarrow IOS$	<0.001	1,581
$X_6 \rightarrow IOS$	$<0,001$	1,586
$X_7 \rightarrow IOS$	0,183	1,004
$Y_1 \rightarrow EM$	$<0,001$	0,000

Source : Appendix 6

Description:

CG: Exogenous Construct (Corporate Governance); IOS: Exogenous Construct (Investment Opportunity Set); ML: Endogenous Construct (Earnings Management); X_i : Exogenous Construct indicators i ; Y_i : Endogenous Constructs indicators i

Based Table 4.3 known all the indicator weight statistically significant because all of the p-value $<0,05$, except X_7 . The Variance Inflation Factor (VIF) of indicators are smaller than 3,3. Thus, the indicator X_7 can not qualify, at next stage be re-estimation model by removing indicator X_7 and the results obtained are presented in Table 4.4 as follows.

Table 4.4
Results (Outer Loading)
Re-estimation model (After Deletion Indicator X_7)

	<i>p-value</i>	<i>Variance Inflation Factor (VIF)</i>
$X_1 \rightarrow CG$	<0.001	1,164
$X_2 \rightarrow CG$	0.004	1,043
$X_3 \rightarrow CG$	<0.001	1,271
$X_4 \rightarrow CG$	<0.001	1.486
$X_5 \rightarrow IOS$	<0.001	1,581
$X_6 \rightarrow IOS$	<0.001	1,581
$Y_1 \rightarrow EM$	<0.001	0,000

Source : Appendix 7

Table 4.4 shows that for the model after re-estimating the p-value of Corporate Governance construct and IOS construct on Earnings Management has been qualified with the value of p-value <0.001 and VIFs are smaller than 3.3.

Inner Model Test (Structural)

The parameters used to evaluate inner model are goodness of fit model and path coefficients. Goodness of fit model is used to determine the ability of exogenous variables to explain the diversity of endogenous variables, or to determine the contribution of exogenous variables on endogenous variables. Goodness of fit models in PLS analysis performed using Q-Square predictive relevance (Q^2). Following is the results of the goodness of fit models in Table 4.5.

Table 4.5
Goodness of Fit Model Results

Variable (dependen)	$Q^2 = R^2$
Earnings Management	0.420

Source : Appendix 8

Q-Square predictive relevance (Q^2) worth 0.420 or 42%. This may indicate that earnings management practices able to be explained by the Corporate Governance (CG) and the Investment Opportunity Set (IOS) construct by 42%, or in other words the contribution of Corporate Governance (CG) and the Investment Opportunity Set (IOS) on Earnings Management by 42%, while the remaining 58% is contributed by the other constructs that are not addressed in this study.

Path coefficient values indicate the level of significance in hypothesis testing. Testing criteria states that if the p-value \leq level of significance (α) = 5%, or otherwise there is the influence of exogenous variables on endogenous variables. The coefficient of the path are presented in Table 4.6 below.

Table 4.6
Path Coefficients Result

Exogenous	Endogenous	Path Coefficients	p-value	Description
Corporate Governance	Earnings Management	0,110	0,131	Rejected (H_1)
Investment Opportunity Set	Earnings Managements	-0,634	<0,001	Accepted (H_2)

Source : Appendix 9

Based on the Tabel 4.6 above it can be concluded that:

1. Hypothesis H_1 rejected. Hypothesis H_1 states that the mechanisms of good corporate governance affect earnings management practices. Based on the test results in Table 4.5 is obtained p-value of 0.131 (more than α) = <0.05).
2. Hypothesis H_2 accepted. Hypothesis H_2 states that Investment Opportunity Set affected on Earnings Management practices. Based on test results obtained in Table 4.5 p-value of <0.001 (the results of these tests show that the p-value < α) = 5%), while the value of the path coefficient of -0.634 Investment Opportunity Set prove that the negative effects on Earnings Management

practices of -0.634. That is, if the Investment Opportunity Set increased by one unit, Earnings Management practices will be an decrease of -0.634.

CONCLUSIONS AND SUGGESTIONS

1. Earnings Management Practices can not be reduced by implementing Corporate Governance Mechanism. This is because the implementation of corporate governance is still relatively new in Indonesia so the goal has not been effectively felt. In addition, the Corporate Governance implementation has started being applied in the business world, but implementation is still not fulfilled either.
2. Investment opportunity set negatively affected on earnings management practices. Earnings Management practices cannot be fully carried out by only having a great number of investment opportunity set. Companies that have the auditor from the Big 5 will have lower possibility of discretionary accruals actions undertaken by management.

Limitations and Suggestions

This study admittedly has several limitations as elaborated as follow:

1. The minimum number of indicators used for interpretation such as the Investment Opportunity Set construct that only uses two indicators. Hartono and Abdillah (2009: 165) cited by Shomad (2013) stated that the rules of thumbs on the number of indicators used as a justification of the results of PLS is preferably a minimum of three indicators. Further research is expected to use more than three indicators to minimize the deletion indicator so that the minimum number of indicators not less than 3 indicators.
2. Not all the indicators in this research constructs can be used in testing results because some indicators do not fulfill the indicator weight test which should be removed. Further research is expected to identify and analyze the indicator earlier so not too much indicators should be removed.

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