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The Influence of Independent Commissioners, Islamic Social Reporting, and Sharia Supervisory Board on Earning Management with Firm Size as a Moderating Variable in Sharia Commercial Banks in Indonesia

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ABSTRACT

This study aims to determine whether independent commissioners, Islamic social reporting and sharia supervisory boards affect earnings management. This study also aims to determine whether firm size can moderate the relationship between independent commissioners, Islamic social reporting, and sharia supervisory boards on earnings management. The population used in this study are Islamic Commercial Banks registered with the OJK from 2013-2021. The sample selection was carried out using the purposive sampling method. The number of samples in this study was 14 Islamic Commercial Banks, so a total of 126 research observations could be obtained. Data processing was carried out using the EViews version 10 program. The results showed that: (1) Independent commissioners partially have no effect on earnings management, (2) Islamic social reporting partially influences earnings management, (3) Sharia supervisory board partially influences earnings management, (4) Firm size partially moderates the relationship between independent commissioners, Islamic social reporting, and sharia supervisory boards.

Keywords: Independent Commissioner, Islamic Social Reporting, Sharia Supervisory Board, Firm size, Profit Management.

INTRODUCTION

Financial reports are goods needed by investors to see the performance of a company. Investors need the information contained in the financial statements to establish communication with stakeholders. Still, a company's management can use its position to manipulate the information in the financial statements to make it bigger or smaller than it is without violating generally accepted accounting principles.

According to Habbash & Haddad (2019), the accounting scandals of several well-known large companies in the world, such as Enron, Xerox, WorldCom, and Parmalat, have created a public perception that earnings management is used opportunistically by managers for their benefit rather than for the benefit of shareholders. If this happens, then the stakeholders in the company must create a program so that managers cannot be free to manage earnings.

In Indonesia, there are cases involving a company's management in managing earnings, such as the Garuda Indonesia case in 2019. Management behaviours that tend to be opportunistic in maximising their interests motivated researchers to learn more about what happened to public companies in Indonesia (Mentari, 2020).

External shareholders (outside equity) are aware of the possibility of a decrease in the company’s value due to the manager's non-productive actions. Therefore, investors will only want to buy shares at a lower price than if there is no non-productive manager action (Suryanto, 2017).

In this study, researchers will look at the variables that allow for reduced earnings management in a company. External control and corporate social responsibility may reduce companies' earnings management. In this study, researchers want to see whether these factors can affect earnings management in an Islamic banking company in Indonesia. Islamic banking was chosen because of the rapid development of Islamic banking in Indonesia. It is because Indonesia is a country with the largest Muslim population in the world. However, if we look further, the brand name of Islamic banking has only changed its name, but operations are still using a conventional approach (Syarif et al., 2021). Under its functions and duties, an Islamic bank should be a bank that runs its business by Islamic law, which refers to the Al-Quran and Hadith. In carrying out their business, Islamic banks must run a business to seek profit and advance the ummah's economy. But in fact, studies conducted by several previous researchers show that there are still problems in managing Islamic banks, such as earnings management in their financial reports. Research conducted by Quittaniah (2013), Ugbede (2013), and Zainuddin & Lui (2018) found that there is profit management in Islamic banks. However, Syarif et al., (2021) research found that banking in Indonesia during the 2013-2019 research period found that profit management did not occur much in Islamic banks in Indonesia.

Islamic banks, as sharia-compliant institutions, are not permitted to manipulate or engineer profits in making financial reports. It can mislead users of financial reports as information on a company's performance (Faradila & Cahyati, 2013). But in practice, management supervision takes work. The management who directly interacts with the company's business environment is the party that knows everything about the company's performance which causes them to be able to predict the company's future performance. Agency theory recognises that with the power granted by management, company stakeholders must also be aware of company developments so that management acts do not only benefit management but also must benefit other stakeholders in the company, especially shareholders. This must be implemented by placing parties trusted by shareholders to oversee management performance. The board of commissioners in the company can carry this out.

Prior (2008) explains that managers who engage in earnings management practices can use Corporate Social Responsibility (CSR) activities to divert stakeholder attention from monitoring their opportunistic behaviours, thereby protecting their position. CSR refers to society's economic, legal, ethical, and discretionary expectations of an organisation. Companies that carry out CSR give a positive impression to various stakeholder groups.

Apart from being a form of supervision, social responsibility also plays an essential role in the company’s continuity. Disclosure of a company's corporate social responsibility can be an obstacle in carrying out earnings management practices because corporate social responsibility emphasises business practices that are carried out in a transparent, accountable, and socially acceptable manner so that the resulting financial reports are reliable and the quality of the information presented can be increased (Rich & Yazan, 2019). Socially responsible companies aim to foster long-term relationships with stakeholders rather than increase the company's short-term profits (GrasGil et al., 2016).

In the business activities of Islamic banks, the government has regulated forms of oversight of products and services offered to the public by adding supervisors to the management of Islamic banks, namely the Islamic supervisory board. The sharia supervisory board is expected to be the party that oversees the course of Islamic bank activities from products and services that Islam prohibits. The sharia supervisory board is also expected to play an essential role in operational activities to ensure that the business activities of the sharia bank comply with sharia principles as determined by fatwas and Islamic sharia.

In this study, researchers also used firm size as a moderating variable. The size of large companies is felt to tend to do earnings management more often than small companies. This is because large companies want to display the condition of companies that are performing well and have a good image to get investors to invest capital in the company. Meanwhile, small companies are usually more vigilant when presenting financial reports because small companies are more observed by external parties (Medyawati & Dayanti, 2016). Therefore, the researcher wants to see whether the firm size in Islamic banking in Indonesia can moderate the relationship between Independent Commissioners, Islamic Social Reporting, and the Sharia Supervisory Board on earnings management.

Based on the explanation above, the authors are interested in researching earnings management in Islamic banks with the title "The Influence of Independent Commissioners, Islamic Social Reporting, and Sharia Supervisory Boards on Profit Management with Firm size as a Moderating Variable in Islamic Banks in Indonesia in 2013-2021".

LITERATURE REVIEW

Earning Management

Scott in Setyani (2020), earnings management as an action that is carried out by choosing an accounting policy method that aims for certain interests. Earnings management can be interpreted as interference in the external financial reporting process that aims to benefit oneself.

Earnings management is one of the negative impacts of using accrual-based accounting. This is because accrual-based accounting will record all the financial effects that occur during transactions and events recognised and experienced by the company, with cash consequences that occur during a specific period, regardless of whether cash is received directly in cash or not by the company. Accrual accounting also recognises allocating the cost of assets for specific periods. This can lead to the emergence of accounts payable, such as payables, unearned income, receivables, prepaid expenses, depreciation expenses, etc. This method also uses accruals, deferrals, and allocation procedures that describe the company's performance during the current period, even though cash has not been received and issued. So, the recognition of income, costs, and profits, as well as the increase and decrease in assets, including profit, is a measurement of a company's performance.

The decision that has been chosen is the best decision from several existing alternatives to achieve the desired goal. According to Zulaikhah (2014), some factors influence a person in making decisions, including problem factors, situation factors and condition factors.

According to Setyani (2020), earnings management is measured through discretionary accruals (DA), where the accruals used to detect earnings management carried out by management in financial reports are total accruals consisting of:

$$\mathbf{TAC} = \textit{Net Income - Cash Flow From Operations}$$
$$\mathbf{NDA} = \text{TAC / Total Assets}$$
$$\mathbf{DA} = \text{TAC} - \text{NDA}$$

Information:
TAC = Total Accruals period t
NDA = Estimated Non-Discretionary Accruals
DA = Discretionary Accruals

Independent Commissioner

The Independent Commissioner is an internal Corporate Governance mechanism that guarantees the discipline of company managers. Corporate Governance aims to create added value for stakeholders. An Independent Commissioner is a member of the Board of Commissioners who comes from outside the Issuer or Public Company, does not own shares either directly or indirectly in the Issuer or Public Company, has no affiliation with the Issuer or Public Company, Commissioners, Directors or Major Shareholders of the Issuer or Public Company, and has no direct or indirect business relationship with the business activities of the Issuer or Public Company. The function of the board of commissioners, including independent commissioners, includes the following two roles:

a. Supervise the company's directors in achieving performance in the Business Plan and provide advice to the board of directors regarding deviations in business management that need to follow the direction intended by the company.
b. Monitor the implementation and effectiveness of Good Corporate Governance practices.

A group of people appoints the board of commissioners through the General Meeting of Shareholders and acts as a liaison between shareholders and management. The board of commissioners has the task of supervising management behaviours and the quality of financial reports to limit the tendency of managers to manage earnings. The existence of the board of commissioners is expected to be able to protect the interests of the shareholders. The larger the size of the board of commissioners in the company is expected to be able to increase supervision to reduce earnings management (Dwiharyadi, 2017).

In this study, to obtain the ratio of independent commissioners, the following equation can be used:

$$\text{Independent Commissioners} = \frac{\textit{Number of Independent Commissioners}}{\textit{Number of Board of Commissioners}}$$

Anggraini’s (2019) research on Islamic Commercial Banks in Indonesia shows that independent commissioners can influence earnings management. Different results were obtained in a study conducted by Rasyid (2015) that independent commissioners do not affect the profit management of Islamic Commercial Banks.

Disclosure of Islamic Social Reporting

CSR activity is one of the activities carried out by the company to make the company more impactful to society and the environment. The company running its business is not only responsible to the owners but also must be responsible for other business environments, including the government, consumers, and society, both in the national environment and the environment where it runs its business.

I-CSR comes with a sharia concept that is very suitable for countries with a Muslim majority population and allows this concept to be applied. Islamic Social Reporting is another form of the existing CSR concept that follows the standards of the Islamic Social Reporting (ISR) index.

In reporting Islamic Corporate Social Responsibility activities, a standard CSR report is called the Index of Islamic Social Reporting (ISR). ISR is one of the social performance reporting standards for sharia-based companies. Haniffa first initiated ISR in 2002. This index appeared because there were still many limitations in conventional social reporting, so it was hoped that ISR would become a reporting standard for sharia-based companies. With the ISR index, it is expected that companies will make decisions that will help Muslims but also help companies fulfil their obligations to Allah SWT and society.

In this study, ICSR disclosure is measured using the social disclosure index:

$$\mathbf{ISRD}j = \frac{\sum Xij}{nj}$$

Information:
ISRDj = Islamic Social Reporting Disclosure Index company j.
Nj = Number of items for company j, nj = 50
Xi = 1 (if the item i is disclosed); 0 (if the item i is not disclosed. So, $0 \leq I\ j \geq 1$).

Companies that carry out CSR activities and disclose them in annual reports will indirectly get a positive assessment in the eyes of the public and investors, which will benefit the company in managing profits. However, this positive assessment can be misused by management in covering earnings management practices because the public believes that companies with high CSR activities are unlikely to carry out unethical practices such as earnings management, so the higher a company's CSR, the higher earnings management practices will be. (Santi & Wardani, 2018). This is also reinforced by the research conducted by Garfatta (2021), who found a positive relationship between CSR disclosure and earnings management practices, thereby supporting the agency theory perspective. Managers engage in previously socially responsible activities to hide their mistakes and assure stakeholders that the organisation is transparent. They may use the code of ethics to achieve their goals rather than the companies. Tend to cover this up through more CSR disclosure. Meanwhile, Solikhah's (2022) research shows that CSR disclosure does not affect earnings management.

Sharia Supervisory Board

The leading role of the ulama in the Sharia Supervisory Board is to oversee the bank's day-to-day operations so that it always complies with sharia provisions. This is because the transactions that apply in Islamic banks are exceptional compared to conventional banks. Because this is compiled and determined by the National Sharia Council. The Sharia Supervisory Board must make a statement periodically (usually annually) that the bank it supervises has been operating under sharia provisions. This statement is contained in the annual report (Annual Report).

As sharia scholars who understand sharia law and principles, the sharia supervisory board supervises and advises management in carrying out bank operations following sharia principles.

This study measured the sharia supervisory board by the number of Islamic banks supervisory board meetings in a year.

$$\text{DPS} = \sum \text{Sharia Supervisory Board Meeting}$$

The research results by Anggraini (2019) on Islamic Commercial Banks in Indonesia show that the Sharia Supervisory Board positively influences earnings management. Meanwhile, Rasyid (2015) research found that the Sharia Supervisory Board negatively impacts earnings management at Islamic Commercial Banks.

Firm Size

Firm size is a scale or value that the company can classify by size based on total assets, log size, share value, and so on. Firm size can be expressed in total assets, sales, and market capitalization. The greater the total assets, sales, and market capitalisation, the greater the firm size. The greater the market capitalisation, the more widely outsiders recognise the company. The greater the market capitalisation represents the movement of more money, and the greater the assets, the more invested capital. This study uses total assets as a measure of firm size. Determination of the use of total assets because total assets are considered better than other measurements as an assessment of firm size.

$$\textbf{Firm Size} = \text{Ln (Total Assset)}$$

Firm size can affect earnings management in a company. Large companies usually tend to have independent commissioners who are more credible in viewing and supervising the company's running under management. It is expected that with the increasing size of the company, the company also tends to choose good commissioners and can represent stakeholders outside management as big decision-makers.

Companies with a large market capitalisation tend to pay attention to public image and highlight their advantages over competitors, encouraging larger companies to disclose social responsibility reports. This is also a way for management to carry out earnings management.

Islamic banking should apply Islamic principles in running its business. With the existence of a Sharia Supervisory Board in the management of Islamic Banks, it is hoped that there will be no mistakes in running their business and not violating Islamic law in carrying out their business. The increasing size of an Islamic bank will also be followed by the selection of members of the Sharia Supervisory Board who are credible and able to anticipate earnings management in the company.

Framework

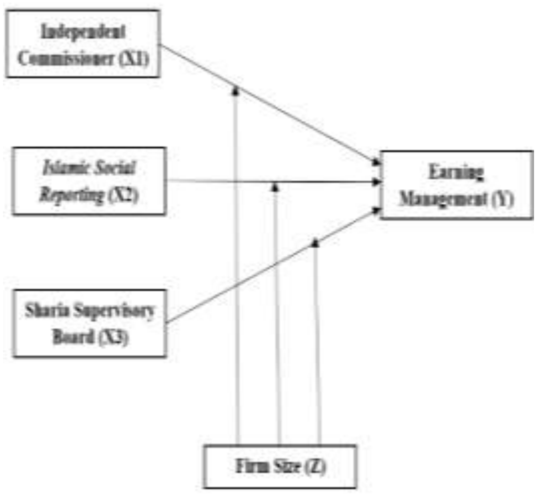


Figure 1. Framework

H1: Independent Commissioners affect earnings management.

H2: Islamic Social Reporting Disclosure affects earnings management.

H3: The Sharia Supervisory Board involves earnings management.

H4: Firm size can moderate the effects of Independent Commissioners on Earnings Management.

H5: Firm size can moderate the effect of Islamic Social Reporting disclosure on Profit Management.

H6: Firm size can moderate the effect of the Sharia Supervisory Board on Profit Management.

MATERIALS & METHODS

This is causal associative research, which aims to analyse the relationship between two or more variables. Based on the type of data used, this research is quantitative because it refers to calculating data in numbers. In this study, the data used is secondary data. Secondary data is a source of research data obtained indirectly or through intermediary media, received and recorded by other parties (Indriantoro, 1999). The data source in this study is the official website of the Indonesia Stock Exchange, www.ojk.co.id. The data taken is the financial report data of Islamic Commercial Banks for 2013-2021.

The population is a generalisation area consisting of objects or subjects that become certain quantities and characteristics set by researchers to study and then draw conclusions (Erlina, 2011). The population in this study are all registered Islamic Commercial Banks and still active in 2013-2020.

The sample is part of the population used to estimate population characteristics (Erlina, 2011). The method used in determining the model is a purposive sampling method which has been carried out based on specific criteria. The sample criteria used in this study are:

1. Sharia Commercial Banks registered with OJK in 2013-2021.

2. Islamic Commercial Banks that issue annual reports for 2013-2021.
3. Have complete data to see data on the number of Independent Commissioners, Corporate Social Disclosure, Number of Sharia Supervisory Boards and Firm size.

Based on the above criteria, the number of samples obtained is 126 (14 Islamic banks x 9 years of research).

Analysis of the data obtained in this study will use computer technology assistance, namely the Econometric Views (EViews) version 10 application program.

RESULT

Results of Descriptive Analysis of Research Variables

Descriptive statistics is the first step before data analysis. The following are the results of the descriptive study that has been carried out:

Table 1. Descriptive Analysis Results

	Minimum	Maximum	Mean	Std. Deviation
X1	0.33	1.00	0.64	0.0965
X2	0.38	0.86	0.59	0.1015
X3	9.00	30.00	14.02	2.9215
Y	-6110398.89	63965361.00	1756243.44	8867915.3351
Z	12.61	18.40	16.12	1.2432

Source: Data processed, 2022

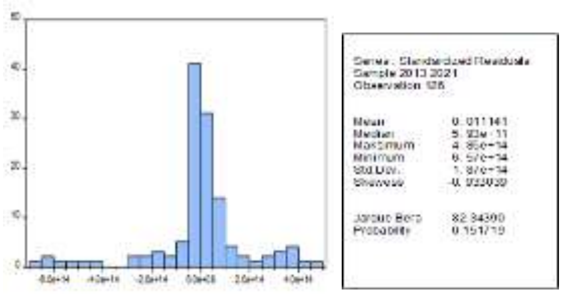
The table above shows the following results:

1. Independent Commissioner Variable (X1) has a minimum value of 0.33 (33%), while the maximum is 1 with an average of 0.64 and a standard deviation of 0.0965. This means that the Islamic Commercial Bank companies in this study have complied with the rules that independent commissioners are at least 30% of the total number of the Board of Commissioners.
2. The Islamic Social Reporting variable (X2) has a minimum value of 0.38, a maximum of 0.86, an average of 0.59 and a standard deviation of 0.1015. Companies have disclosed an average of 59% of the Islamic Social Reporting disclosure index.
3. The Sharia Supervisory Board variable (X3) has a minimum value of 9 and a maximum of 30 meetings in one year with an average number of meetings of 14.0159 or 14 x meetings in a year with a standard deviation of 2.9215.
4. The minimum earning management variable is -6110398.89, the maximum is 63965361.00, and the average is 1756243.44, with a standard deviation of 1.2432. It means that the average earnings management value is positive. The average company manages earnings by increasing its profits.
5. The variable firm size is a minimum of 12.61 and a maximum of 18.40, with an average of 16.12 and a standard deviation of 1.2432. This means that companies in the study have an average firm size of 16.12%.

Classic Assumption Test

Normality Test

The normality test determines whether the model's residuals are normally distributed. The Jarque-Bera Test (JB test) can reach the normality test. The residual is said to be normally distributed if it has a probability above or equal to 0.05. The results of the normality test in this study can be shown as follows



Source: Data processed, 2022
Figure 2. Normality Test Results

The picture above shows that the Jarque-Bera value obtained in this study is 82.34390 with a probability of 0.151719. Because the probability value is 0.151719 > 0.05, it can be said that the residuals in this research model are normally distributed.

Multicollinearity Test

The multicollinearity test is used to see a model's relationship between independent variables by looking at VIF and tolerance. The test results show that all independent variables have a VIF value of less than 10. It can be concluded that there is no multicollinearity between the independent variables in the regression model. Based on the results of the multicollinearity test that has been carried out, a summary of the results is obtained as shown in the table below:

Table 2. Multicollinearity Test Results

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
C	0.000204	15.53448	NA
X1	0.000614	3.944623	**1.072001**
X2	0.000117	6.112528	**1.073695**
X3	0.012851	2.197397	**1.166343**

Source: Results of Data Processing Using EViews 10, 2022

The table above shows that each independent variable has a correlation coefficient below <10 or a tolerance value above 0.1. Thus, it can be concluded that each independent variable used in the study is free from multicollinearity symptoms.

Panel Data Regression Model Selection Results

Chow test

The Chow test is used to determine the panel data analysis model. The Chow test is used to choose between the Fixed Effect model or the Common Effect model, which should be used.
H0: Common Effects
Ha: Fixed Effects
If the results of this specification test show a Chi-Square probability > 0.05, then the Common Effect model is selected. Conversely, if the Chi-square probability <0.05, then the model that should be used is the Fixed Effect. The following are the results of the model specification test in this study:

Table 3. Chow Test Result

Effects Test	Statistic	d.f.	Prob.
Cross-section F	14.368255	(7,61)	0.0000
Cross-section Chi-square	70.136121	7	0.0000

Source: Results of Data Processing Using EViews 10, 2022

The table above shows the Chi-square cross-section probability value of 0.0000 <0.05, so it can be concluded that H0 is rejected and Ha is accepted. Thus, the model that should be used in research is the fixed effect model. Furthermore, because the selected model is a fixed effect, it is necessary to do the Hausman test to find out whether the fixed effect model or random effect model will be used in the study.

Hausman Test

The Hausman test determines which model should be used: the Fixed Effect model or the Random Effect model. The Hausman Test Hypothesis is as follows:
H0: Random Effects
Ha: Fixed Effects
If the results of this specification test show a random cross-section probability of more than 0.05, then the chosen model is a Random Effect. Conversely, if the Chi-square probability is less than 0.05, the Fixed Effect model should be used. Hausman test results are as follows:

Table 4. Hausman Test Result

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	3.430598	3	0.3299

Source: Results of Data Processing Using EViews 10, 2022

The table above shows the test between the random effect model and the fixed effect obtained from the Chi-Square probability value of 0.3299, which is greater than 0.05, so H0 is accepted, and Ha is rejected. Thus, the model that should be used for this research is the random effect model.

Hypothesis Test Results

Panel data regression analysis in this study aims to determine the effect of Independent Commissioners, Islamic Social Reporting, and Sharia Supervisory Boards on Earning Management in manufacturing companies listed on the Indonesia Stock Exchange from 2013-2021.

Based on the model selection test, the results show that the model that should be used is the Random Effect.

Table 5. Results of Regression Analysis of Panel Data Model Random Effects Without Moderating Variables

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-1.24E+09	1.52E+09	-0.814465	0.4170
X1	6.74E+08	1.64E+09	0.409963	**0.6826**
X2	2.15E+09	1.59E+09	1.349392	**0.0017**
X3	15518889	61434185	0.252610	**0.0010**

Source: Results of Data Processing Using EViews 10, 2022

Based on the table above the selected estimation model, the panel data regression model equation is obtained as follows:

Y= -1.24E+09+ 6.74E+08X1 + 2.15E+09X2 + 15518889X3 + Ɛ

Based on the equation above, it can be concluded that the independent commissioners partially do not affect earnings management. However, Islamic social reporting and sharia supervisory boards partially affect earnings management.

Table 6. Results of Regression Analysis of Panel Data Model Random Effects with Moderating Variables

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	1.77E+13	1.28E+14	0.533212	0.0041
Z	3.333.21	8798.120	2.629321	0.0097
X1	3.99E+11	1.59E+14	4.320144	0.0220
X2	3.99E+11	1.55E+14	3.932939	0.0040
X3	4.27E+12	5.95E+12	3.918503	0.0047
X1Z	2.61E+11	2.47E+14	4.321147	0.0320
X2Z	3.18E+13	3.33E+12	3.732931	0.0020
X3Z	3.19E+11	3.17E+11	4.132939	0.0000

Source: Results of Data Processing Using EViews 10, 2022

Based on the table above the selected estimation model, the panel data regression model equation is obtained as follows:

Based on the equation above, it can be concluded that:

1. Independent commissioner, Islamic social reporting, and the sharia supervisory board partially influence earnings management.
2. Firm size as a moderating variable partially has a significant effect in moderating and strengthening the relationship of independent commissioners, Islamic social reporting, and the sharia supervisory board on earnings management.

CONCLUSION

The results of this study provide several conclusions that can be drawn based on the discussion of the problems that have been carried out. The following are the conclusions that the author has summarised in this study:

1. There was no significant influence between independent commissioners on earnings management at Islamic Commercial Banks in Indonesia in 2013-2021
2. There is a positive and significant influence between Islamic social reporting on earnings management at Islamic Commercial Banks in Indonesia in 2013-2021.
3. There is a positive and significant influence between the sharia supervisory board on earnings management at Islamic Commercial Banks in Indonesia in 2013-2021.
4. Firm size can moderate the relationship between independent commissioners and earnings management at Islamic Commercial Banks in Indonesia in 2013-2021.
5. Firm size can moderate the relationship between Islamic Social Reporting and earnings management at Islamic Commercial Banks in Indonesia in 2013-2021.
6. Firm size can moderate the relationship of the sharia supervisory board to earnings management at Islamic

Commercial Banks in Indonesia in 2013-2021.

RESEARCH LIMITATIONS

This study has several limitations that future researchers can correct for better results. The limitations of this study are:

1. The researcher only examines some variables that may affect earnings management. Still, other variables, such as company age and profitability, may significantly influence earnings management.
2. The existence of other moderating variables, such as corporate governance, may reduce the limitations of the significance of the moderating variable earnings management.

SUGGESTION

1. In this study, independent commissioners do not affect earnings management, so it is hoped that Islamic Commercial Banks will be able to see the competence of the Sharia Supervisory Board and the Board of Commissioners in to able to supervise financial reports effectively and be able to minimise earnings management.
2. It is believed that large firms tend to carry out earnings management so that Islamic Commercial Banks can still maintain their firm size and continue to improve the quality of management so that they do not carry out earnings management.
3. It is hoped that further research will add new variables such as the frequency of the Sharia Supervisory Board meetings, the educational background of the Sharia Supervisory Board and the Board of Commissioners, audit quality, and managerial ownership.

Declaration by Authors

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