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The Role of Company Size in Moderating the Effect of Profitability, Profit Growth, Leverage, and Liquidity on Earnings Quality

Siska Puji Lestari *[1] and Muhammad Khafid [2]

[1,2]Department of Accounting, Faculty of Economics, Universitas Negeri Semarang

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ABSTRACT

This study aims to determine the effect of profitability, earnings growth, leverage, and liquidity on earnings quality with company size as a moderating variable. The population in this study was 65 property and real estate sector companies listed on the Indonesia Stock Exchange (BEI) in 2016-2018. The sample selection used a purposive sampling technique and selected 44 companies with 132 units of analysis. The analysis techniques used descriptive statistical analysis, inferential analysis, and moderated regression analysis. The results showed that leverage and liquidity had a positive effect on earnings quality. While profitability and earnings growth have no effect on earnings quality. Company size is able to weaken the effect of profitability, leverage, and liquidity on earnings quality. The conclusion of this study is that the quality of the company's earnings will increase if the company can maintain the level of leverage and the level of company liquidity. However, the quality of company earnings will decrease when the size of the company is large and affects the company's leverage and liquidity on the quality of the company's earnings.

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INTRODUCTION

Financial statements are the outputs of accounting procedures which is useful for management's accountability to the owners of the company. Financial statements are made and published in order to convey news about the company's economic condition to internal and external parties of the company as an economic decision making. In financial statements, earnings information plays an important role in decision-making. Earning becomes a measure of the achievement of a management's performance in managing company resources. Earnings that do not reflect real information regarding management's performance can mislead report users (Khafid, 2012). The earnings information is important so the earnings presented must be high quality so that the users of financial statements do not get the wrong information (Ma & Ma, 2017). Earnings quality is very paid attention to by managers and investors because it conveys information about the operational and financial status of the company. Penman (2001) stated that qualified earnings are earnings that describe the continuation of future earnings and are determined by the accrual and cash flow elements. Corporate earnings reporting is carried out transparently not the result of manipulating to make earnings quality good.

One of the earnings quality cases was carried out by PT Tiga Pilar Sejahtera Food Tbk (AISA) in the 2017 financial statements (Arief, 2019). On March 12, 2019, IDX asked for further information on the result of an investigation conducted by PT Ernst & Young Indonesia (EY) based on AISA's 2017 financial statements. There was a finding of the allegation of accounting post inflation of Rp 4 trillion and income inflation of Rp 662 billion as well as another inflation of Rp 329 billion in EBITDA (earnings before interest, tax, depreciation, and amortization). AISA's 2017 financial statements were previously audited by the Amir Abadi Jusuf, Aryanto, Mawar & Partners Public Accounting Firms which are connected with well-known audit, tax, and consulting firms, namely RSM International.

The existence of an indication of inflation in the accounting post indicates that the company reports financial information that is different from the actual condition of the company. Low-quality financial information makes the company's earnings quality also decline. Earnings information that should be able to be

* *E-mail: siskapl070499@gmail.com*
Address: L2 Building, 2nd Floor FE FE UNNES, Sekaran Campus, Gunungpati, Semarang, Indonesia 50229

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a measure in making the right decisions gives a bias and can lead to mistakes. Therefore, the companies need to evaluate and improve these conditions so that the quality of the company's earnings remains stable and can even increase.

Previous research shows various results from each independent variable. Based on the previous research, four variables that could affect earnings quality were taken. The four variables give inconsistent results, among others, profitability affects earnings quality (Gunarianto et al., 2014; Ma & Ma, 2017), profitability does not affect earnings quality (Afni et al., 2014; Ginting, 2017). Profit growth has a positive effect on earnings quality (Zein et al., 2016; Afni et al., 2014), profit growth does not affect earnings quality (Septiyani et al., 2017; Silfi, 2016). Leverage has a negative effect on earnings quality (Valipour & Moradbeygi, 2011; Moradi et al., 2010) leverage does not affect earnings quality (Marliyana & Khafid, 2017). Liquidity has a positive effect on earnings quality (Ramadan, 2015; Silfi, 2016), liquidity does not affect earnings quality (Marliyana & Khafid, 2017).

This study aims to analyze the effect of profitability, earnings growth, leverage, and liquidity on earnings quality using company size as a moderating variable. The existence of different research results on variables that affect earnings quality indicates the need to present other variables that can moderate. The originality of this study is to present company size as a moderating variable. Large-scale companies have assets with a sufficiently large number and a wide enough range of information so that the presence of company size as a moderating variable is expected to contribute to improving the quality of company earnings.

This study uses agency theory and signal theory. Agency theory states that agency relationships arise when the principal hires the agent to provide services and then entrusts the decision-making to the agent (Jensen & Meckling, 1976). Signal theory arises because there is information asymmetry between agents and principals (Ross (1977). Information asymmetry is caused by a mismatch of information from each related party. Therefore, to overcome the existence of information asymmetry, the company must provide a signal to investors.

Return On Asset is a financial ratio that is useful in assessing profitability. ROA is useful in measuring the effectiveness of the company in obtaining profits and using corporate assets. In signal theory, financial information is an important signal issued by the company to parties who have an interest in the good and bad performance of the company according to the perception of the readers of financial statements. A high level of profit gives a signal that the condition of the company is good and has good business opportunities in the future will show the good quality of the company's earnings. Research conducted by Gunarianto et al., (2014) and Hasanzade et al., (2013) show that profitability has a positive effect on earnings quality.

H_1: Profitability has a positive effect on earnings quality

Profit growth is an increase or decrease in company profits per year. In signal theory, a positive profit growth signal gives a positive signal to the market. Profit growth which has increased from year to year is good news for investors which indicates the company has good performance. Profit growth is likely to affect earnings quality. The earnings of a company that has the opportunity to grow indicate that the company's financial performance is good so that it has the opportunity to grow on the quality of its earnings (Silfi, 2016). Increasingly corporate earnings make financial statements better so that it is easier for companies to get investors without manipulating company earnings. This makes the quality of the company's earnings better. The research result of Zein et al., (2016) and Sari & Rokhmania (2020) show profit growth has a positive effect on earnings quality.

H_2: Profit growth has a positive effect on earnings quality

Leverage calculates the amount of debt to finance the company's operations. In agency theory, management is an agent who is given authority from the lender (principal) to fulfill obligations as a borrower by managing loan funds properly. Leverage affects earnings quality. This is because if more assets are funded by debt, the investor's position will decrease. It drives management to manipulate earnings to attract investors so that the financial condition of the company that has been manipulated does not show the proper financial condition which results in a decrease in the quality of the company's earnings. High debt levels can have a negative impact on earnings quality (Ghosh & Moon, 2010). According to the research of Alves (2014) and Dhaliwal et al., (1991) that leverage has a negative effect on earnings quality.

H_3: Leverage has a negative effect on earnings quality

Liquidity is a financial ratio that describes the company's ability to pay all short-term debt (Kurniawan & Khafid, 2016). In signal theory, a company with good financial capability illustrates that the company has good business opportunities in the future. Companies that have the ability to finance short-term debt show that they have good financial performance so that business continuity also improves and gives a signal positive for the market. Therefore, companies do not need earnings management practices. This makes the quality of the company's earnings increase. Research conducted by Ramadan, (2015) and Zein et al., (2016) state that liquidity has a positive effect on earnings quality.

H_4: Liquidity has a positive effect on earnings quality

A high level of profit indicates that the company is in good condition and has good business opportunities in the future. It indicates that the quality of the company's earnings is good. Agency theory regulates the bond between the principal and the agent, in which the principal entrusts the work to the agent (Wahyudin & Solikhah, 2017). Good corporate profitability indicates that the company has good prospects in the future so that it indicates good earnings quality. For large com-

panies, there is a mechanism related to internal control which tends to be better than small companies. It will encourage the company to always operate properly and optimally in order to meet the needs of various interested parties, one of which is the owner. Large companies will try to maintain good business practices so that the profits generated are maximized and in accordance with applicable accounting provisions. Therefore, company size can strengthen the effect of profitability on earnings quality.

H_5: Company size moderates the effect of profitability on earnings quality

Profit growth is an increase or decrease in profit, an increase in company profits will affect an increase in profit growth. In signal theory, an increasing company profit will give a positive signal to the market and can describe the prospect of the company's growth in the future. Especially in large-scale companies can increase profit growth to be higher. This is since the company's total assets are larger so that the company's business continuity is more secure and the opportunity to earn profits is greater. The increasingly growing level of company profits will make earnings information more attractive for investors to invest their capital. Therefore, an increasingly growing profit rate will improve the quality of the company's earnings.

H_6: Company size moderates the effect of earnings growth on earnings quality

If a lot of wealth is funded by liabilities, the position of investors will decrease. This drives management to manipulate earnings to attract investors so that the company's financial condition is different from the actual financial condition, which results in a decrease in the quality of the company's earnings. Based on signal theory, large companies can signal external parties to submit additional capital which makes the capital structure to be bigger (Sawitri & Lestari, 2015). Company size is an important indicator of capital structure. Many studies state that large-sized companies will be greater in the use of debt than small-scale companies. Large companies are able to manage debt neatly because the larger the size of the company, the more visible its performance to the public so that companies will report financial conditions and tend to be more alert and transparent which will produce optimal profits. This optimal profit can attract a positive response from investors. Thus, funding problems are not constrained, there will be no practice of earnings manipulation and making the company's earnings quality better.

H_7: Company size moderates the effect of leverage on earnings quality

Companies that can fulfill their short-term obligations show that their financial performance is unquestionable so that business continuity is also good. Therefore, there will be no earnings management practice. Then, the quality of the company's earnings will increase. In agency theory, the party responsible for managing the condition of the company is the agent (manager). Large-scale companies have larger total assets, including current assets related to liquidity. Large-sized companies also have a fairly large business risk, because operating costs and company liabilities are also larger. Liquidity is measured by comparing current assets to current liabilities. Current assets are useful for funding the company's current liabilities, if current liabilities are too large and the results of current asset management are not proportional to current liabilities, it illustrates the company's low ability to finance current liabilities. Then there is a fraud committed by managers to beautify the company's financial condition to attract investors so that the quality of the company's earnings became low.

H_8: Company size moderates the effect of liquidity on earnings quality

RESEARCH METHODS

The type of this study describes quantitative research using secondary data with a population of 65 companies in the property and real estate sectors for the 2016-2018 period. There were 44 sample companies with 132 analysis units in three years, then subtracted from outlier data of 25 analysis units. Sampling provisions in the study are presented in table 1.

Earnings quality was the dependent variable in this study, the independent variables included profitability, profit growth, leverage, and liquidity. Meanwhile, the moderating variable was company size. The operational definition of research variables is presented in table 2.

The data collection technique was a documentary technique in the form of annual reports of the property and real estate sector companies listed on the IDX during 2016-2018 which were accessed using the www.idx.co.id page. The analytical methods used in this study were descriptive statistical analysis, classical assumption test, and moderating regression analysis (MRA) using IBM SPSS 21. The basis for making the decision was to accept the hypothesis if the significance level was below 5%. The moderation regression model was expressed in equation 1.

$$QE = \alpha+\beta_1ROA+\beta_2Yit+\beta_3DER+\beta_4CR+\beta_5|ROA_SIZE| +\beta_6|Yit_SIZE|+\beta_7|DER_SIZE|+\beta_8|CR_SIZE|+e \quad (1)$$

RESULTS AND DISCUSSIONS

The results of descriptive statistical tests regarding the minimum value, maximum value, mean, and standard deviation are presented in table 3.

During the three research periods, earnings quality has an average of 0.259, profitability HAS an average of 0.047, and earnings growth has an average of 0.60 is low. Meanwhile, the level of leverage with an average of 3.24, liquidity with 3.24, and company size with an average of 29,348 are highly classified. The average values of the variables of profitability, profit growth, and company size are greater than the standard deviation value, meaning that the data distribution has low data variability. Meanwhile, the average values of earnings quality, leverage, and liquidity variables are smaller than the standard deviation value, meaning that the data spread

Table 1. Sampling Criteria

No	Sample Criteria	Beyond Criteria	Included Criteria
1	Property and real estate sector companies listed on the IDX in 2019.		64
2	Property and real estate sector companies listed on the IDX during the 2016-2018 period.	(18)	47
3	Companies that publish financial statements consistently during 2016-2018.	(2)	45
4	Companies that provide complete data information on variables.	(1)	44
5	Companies present financial statements using rupiah currency.	0	44
	Total sample companies		44
	Total analysis units (2016-2018)		132
	Data outlier	(25)	107
	Final total		107

Source: Processed Secondary Data, 2020

has a high data variability.

Classical assumption tests include normality test, multicollinearity test, autocorrelation test, and heteroscedasticity test. The normality test gives the data results which are normally distributed with a significance of 0.120 > 0.5. The multicollinearity test produces a VIF value < 10 and tolerance> 0.01 means that there is no multicollinearity symptom. The autocorrelation test using Durbin-Watson shows a d value of 2.083. The value of the autocorrelation test was 1.608 <2.083<2.392, meaning that this study is free from autocorrelation. The heteroscedasticity test on each variable shows a significance value >0.05, meaning that it is free from heteroscedasticity. Based on hypothesis testing, it can be written in the form of equation 2.

$$QE = -0.781 - 174.212ROA + 0.495Yit + 3.279DER + 3.789CR + 6.239|ROA_SIZE| - 0.019|Yit_SIZE| - 0.094|DER_SIZE| - 0.127|CR_SIZE| \quad \text{...........................(2)}$$

The adjusted R^2 value is 0.017, this value shows that both the independent variable and the moderating variable are able to predict 1.7% of the dependent variable. The remaining percentage of 98.3% is explained by variables outside the research model. The summary of hypothesis testing is presented in table 4.

The Effect of Profitability on Earnings Quality

Profitability does not affect earnings quality. The level of high or low profitability does not affect the quality of earnings. The research result indicates a discrepancy with the signal theory, which states how companies should convey signals to users of financial statements (Ross, 1977). The signal given is a statement of profit. The company's earnings still contain accruals, if the receivables have not been collected, the earning has not shown the actual financial condition. Thus, pro-

Table 2. Operational Definition of Research Variables

No	Variables	Definition	Measurement
1	Earnings Quality (QE)	The ability of reported earnings to predict future earnings (Sepe & Spiceland, 2015).	QE= Operating Cash Flow/ Net Profit (Septiyani et al., 2017)
2	Profitability (ROA)	The company's ability to make a profit (Murhadi, 2013).	ROA= Net Profit After Tax/ Total Assets (Soly & Wijaya, 2018)
3	Profit Growth (Yit)	Variables that explain the prospect of the company's growth in the future (Reyhan et al., 2014).	$Yit= (Yit-Yit_{-1})/(Yit_{-1})$ (Zein et al., 2016)
4	Leverage (DER)	The composition between debt and own capital used in financing company assets (Hossain & Ali, 2012).	DER= Total Debt /Total Equity (Septiyani et al., 2017)
5	Liquidity (CR)	The company's ability to follow up on its short-term obligations (Moghaddam & Abbaspour, 2017).	CR= Current Assets/ Current Liabilities (Soly & Wijaya, 2018)
6	Company size (SIZE)	The scale of the company as seen from the total assets of the company at the end of the year (Sekartaji, 2017)	*Size = Ln. Total Asset* (Jaya & Wirama, 2017)

Source: Processed secondary data, 2020

Table 3. Descriptive Statistics Test Result

	N	Minimum	Maximum	Mean	Std. Deviation
Earnings Quality	107	-5.2594051	5.4195523	.258992428	1.5616052346
Profitability	107	-.0477884	.2585293	.046943342	.0467169099
Profit Growth	107	-3.1628872	59.2736402	.597323594	5.8773489605
Leverage	107	.0356874	3.7009605	.784500111	.6669785493
Liquidity	107	.2077274	59.5727387	3.238105836	5.9574741006
Company Size	107	25.8725810	31.6700664	29.348214060	1.2892335445
Valid N (listwise)	107				

Source: Processed secondary data, 2020

fitability cannot determine the earnings quality better. The result of this study is in line with the research of Afni et al., (2014), Sukmawati et al., (2014), Anjelica & Prasetyawan (2014) and Ginting(2017).

The Effect of Profit Growth on Earnings Quality

Earnings growth does not affect earnings quality. This study is not in line with signal theory, the disclosure of company earnings information is a signal from the company to investors in order to minimize uncertainty about the company's prospects in the future. The disclosure of this information is in the form of the company's profit growth. In table 3, the profit growth carried out during the three research periods shows a low value. It shows the poor financial performance of the company so that the increase in company profits has not been maximized. Therefore, the role of earnings growth cannot affect earnings quality. This study is in line with the research of Silfi (2016) and Septiyani et al., (2017).

The Effect of Leverage on Earnings Quality

Leverage has a positive effect on earnings quality. The result of this study is not in line with agency theory. Jensen & Meckling (1976) stated that agency theory is a theory of differences in interests between principal and agent. The principal wants agents to report financial information in accordance with company circumstances. As seen in Table 3, this study has a high average level of leverage. If the company's debt is used effectively and efficiently, it is possible to get greater profits and be able to pay obligations from the profits obtained. Thus, the reported earnings have higher quality without any earnings manipulation. This study is in accordance with the research of Septiyani et al., (2017), Silfi (2016), Risdawaty & Subowo, (2015), and Ahmad & Alrabba, (2017).

The Effect of Liquidity on Earnings Quality

Liquidity has a positive effect on earnings quality. According to signal theory, Leland & Pyle (1977) stated that signal is a step by someone who has authority to convey company information to shareholders. A high level of liquidity provides a small possibility of corporate earnings manipulation. The absence of earnings manipulation and stable earnings will improve the quality of earnings, it will give a positive signal to the market. If the company has a good level of liquidity, it presents earnings information more widely to show the credibility of the company. (Ginting, 2017). That is why the company's financial performance is guaranteed to be better and avoid earnings management practices so that the quality of the company's earnings is getting better. The result of this study strengthens the research of Zein et al., (2016), and Silfi (2016).

Table 4. Summary of Hypothesis Testing Results

Hypothesis	Hypothesis Statement	β	Sig.	Results
H_1	Profitability has a positive effect on earnings quality.	-174.212	0.061	Rejected
H_2	Profit growth has a positive effect on earnings quality.	0.495	0.774	Rejected
H_3	Leverage has a negative effect on earnings quality.	3.279	0.000	Rejected
H_4	Liquidity has a positive effect on earnings quality.	3.789	0.019	Accepted
H_5	Company size moderates the effect of profitability on earnings quality.	6.239	0.049	Accepted
H_6	Company size moderates the effect of earnings growth on earnings quality.	-0.019	0.748	Rejected
H_7	Firm size moderates the effect of leverage on earnings quality.	-0.094	0.001	Accepted
H_8	Firm size moderates the effect of liquidity on earnings quality.	-0.127	0.020	Accepted

Source: Research summary, 2020

The Effect of Profitability on Earnings Quality with Company Size as Moderating

Company size weakens the effect of profitability on earnings quality. The regression coefficient produces a positive value but the coefficient of the first hypothesis is negative. Agency theory explains that management is an agent appointed by investors (principals) and given the task to manage the company and achieve the set targets. Company size indicates the size of the company's scale. Large-sized companies have reached the maturity stage and companies are relatively more stable so that they can generate larger profits. Investors (principals) believe that large companies tend to have higher profitability presentation capabilities compared to small companies. This is because financial performance tends to be better. Besides that, the company's internal control will also be better so that it can increase company earnings. The higher the company earns profit, it shows the company's success in managing, allocating, and maintaining company assets. The financial performance of a good company without any corporate earnings management practices will certainly improve the quality of the company's earnings.

The Effect of Earnings Growth on Earnings Quality with Company Size as Moderating

The result of the study is not in accordance with the signal theory, that increasing profits will give a positive signal to the market and can describe the prospects of company growth in the future. Company size does not have an interaction effect on the effect of earnings growth on earnings quality. Big companies do not always earn high earnings. However, it is the ability of managers to play an important role in managing the company to generate maximum profit growth. Small companies, if they can manage assets better, have the possibility to earn high earnings. Therefore, company size is not able to moderate the effect of earnings growth on earnings quality.

The Effect of Leverage on Earnings Quality with Company Size As Moderator

Company size weakens the effect of leverage on earnings quality. Based on signal theory, large companies can signal outsiders to provide additional funds. Large companies tend to have a big opportunity to get outside funding because they have a wider information network. Thus, the company's leverage level can become larger. Leverage that is too large is closer to large business risk because the debt owned by the company is too large. Thus, leverage that is too large makes investors not lured to invest. Apart from being afraid of taking risks, investors also assume that the company will be more focused on how to pay these debts rather than giving dividends to investors so that investors are not attracted to investment. One of the solutions taken by the company is to practice earnings manipulation, which results in the low quality of the company's earnings.

The Effect of Liquidity on Earnings Quality with Company Size As Moderating

Company size weakens the effect of liquidity on earnings quality. Brigham & Houston (2006) stated that company size is the proportion of small or big of a company that can be grouped in various ways including the size of income, total assets, and total equity. Large companies have a larger amount of wealth, including current assets related to liquidity. In addition to having large total assets, large companies also have a high business risk because the company's operational costs and liabilities are also higher. Liquidity is measured by comparing current assets and current liabilities. Current assets are useful for financing the company's current liabilities. If the current liabilities are too large and the results of the current asset management are not proportional to the current liabilities, it reflects the company's ability to finance current liabilities is low. This causes fraud by managers to beautify the company's financial condition to attract investors so that the quality of the company's earnings becomes low.

CONCLUSIONS

The conclusion of this study is that high levels of leverage and liquidity can improve earnings quality. A high level of leverage does not indicate that the company is closer to bankruptcy. If funds are managed properly it can generate profits to pay off debt so that earnings management practices do not occur and make the earnings quality becomes good. In addition, a high level of liquidity indicates a liquid company, meaning the company's ability to pay off short-term debt does not need to be doubted. Large companies have a fairly good financial performance, therefore, they are able to earn large profits and report according to the company's conditions. Large companies tend to be easy to get funding from outside but also have a high business risk. The amount of external funding makes investors not interested and current liabilities that are too large make business risks even greater. Thus, managers beautify financial statements to cover these two things. Therefore, the existence of company size can weaken the effect of profitability, leverage, and liquidity on earnings quality. Suggestion for further researchers is to add other variables as independent variables such as corporate governance. The existence of corporate governance is expected to reduce earnings management activities so as to improve the quality of company earnings.

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