

The Influence of Audit Opinion and Managerial Ownership on Income Smoothing in Banking Companies

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ARTICLE INFO

Keywords:
Audit opinions,
managerial ownership,
income smoothing

Kata Kunci:
Opini audit,
Kepemilikan manajerial,
Perataan laba

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ABSTRACT

This research was conducted on banking companies that are included in the top 30 in Indonesia. Data analysis method used in this study is to use a descriptive statistical analysis and logistic regression method with data processing using SPSS 21. The results of this study indicate that audit opinion has a negative but not significant effect on income smoothing. This indicates that with a low audit opinion does not indicate the company is making income smoothing. Managerial ownership shows the results have a significant negative effect on income smoothing, this indicates that the ownership of shares in the company can reduce the actions of managers to make income smoothing.

SARI PATI

Penelitian ini dilakukan pada perusahaan perbankan yang termasuk dalam 30 besar di Indonesia. Metode analisis data yang digunakan dalam penelitian ini adalah dengan menggunakan analisis statistik deskriptif dan metode regresi logistik dengan pengolahan data menggunakan SPSS 21. Hasil penelitian ini menunjukkan bahwa opini audit memiliki pengaruh negatif tetapi tidak signifikan terhadap perataan laba. Hal ini menunjukkan bahwa opini audit yang rendah tidak mengindikasikan perusahaan melakukan perataan laba. Kepemilikan manajerial menunjukkan hasil memiliki pengaruh negatif yang signifikan terhadap perataan laba, yang menunjukkan bahwa kepemilikan saham di perusahaan dapat mengurangi tindakan manajer untuk melakukan perataan laba.

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INTRODUCTION

The financial report is a company facility to convey financial information that contains the accountability of management to fulfill the needs of external parties, namely information on company performance. According to the Statement of Financial Accounting Concept (SFAC) No. 1, earnings information is the main concern to assess performance or accountability of management. Besides that, earnings information also helps the owner or other parties in estimating the company's earnings power in the future. The existence of a tendency to pay more attention to this profit is realized by management, especially managers whose performance is measured based on earnings information, thus encouraging the emergence of deviant behavior, one of which is earnings management (Putri et al, 2014).

The issue of information disclosure has received global attention from various parties due to its importance to investors in making investment decisions. The information asymmetry that exists between the managers and shareholders has positioned the managers above the shareholders in terms of information advantage about the firm. Managers have exclusive access to operational information about firms' actions and future prospects, which causes them to have compelling reasons to ensure confidentiality of the information. Therefore, firms with a weak practice of information disclosure policy could cause managers to take advantage in pursuing their self-interests at the expense of their shareholders (Ghani et al, 2016). Strategy alignment between organization objectives and business unit and support functions become crucial for organization successful. Organization is able to execute its strategy well to compete with its rivals if organizational strategies are linked to business units and support functions within organization (Yuliansyah, 2015).

Earnings management actions have led to several cases of accounting reporting scandals, including

Japanese financial supervisors planning to punish Toshiba Corp., a technology company for allegedly forging financial statements. The independent committee announced its findings regarding intentions to exaggerate the company's revenues made by officials. On November 10, 2017, Kobe Steel Ltd., forged metal product data for years. The data forgery that has hit the company is due to a lack of quality control and the company is only focused on making a profit. Another interesting case is the case of Kimia Farma Company and Lippo Bank. The case of Kimia Farma company happened a mark up on profit in 2001. While at Bank Lippo there was double bookkeeping in 2002. In that year, Bapepam discovered three versions of Bank Lippo's financial statements. As a result of these manipulations, Bapepam imposed penalties on PT Kimia Farma and Bank Lippo along with auditors who conducted audits on the company. Another case happened to a banking company, namely PT Bank Bukopin Tbk, revising the 2015, 2016 and 2017 financial statements. The revised financial report was precisely appeared on April 25, 2018. A number of variables in the report also changed significantly. Bukopin management revealed that these changes were triggered by abnormal records from the credit card business revenue. Data on revenue from credit cards at Bank Bukopin differs from the reality (kompas.com). This event passed through various layers of supervision and auditing over the years, ranging from Bukopin's internal audit, the Public Accountant Office (KAP) as an independent auditor, Bank Indonesia as the payment system authority that handles credit cards, and the OJK as the institution responsible for banking supervision .

Banking companies do more income smoothing than non-banking companies (Indriastuti, 2012). The larger the size of the bank, the more likely to have more information than the smaller banks. Information related to decision making will also increase. Bank size can be an indicator of the assessment of investors to assess the performance of the bank. Large banks generate relatively large

profits. This is what can make large banks to make enough earnings management because one of the main reasons is to meet expectations from investors or shareholders (Agusti and Tyas, 2009). Financial details reported by a company are important information for investors. Investors make decisions partly because the total earnings show the company's financial performance (Makhsun et al, 2018).

Earnings management arises as the impact of agency theory that occurs due to an inconsistency of interests between shareholders (principal) and company management (agent). Income smoothing is a management intervention in external financial reporting with the aim of benefiting itself (the manager). This conflict arises due to the emergence of information gaps provided, therefore it requires the existence of financial statement audits by competent and independent third parties (Lin and Mark, 2010). Company share ownership by management aims to align various interests between the principal and agent. By giving the manager the opportunity to be involved in the shareholding aims to align the interests of the manager with the shareholders, so that the greater the proportion of ownership by the managerial management will be more active for the benefit of the shareholders which includes themselves.

LITERATURE OF REVIEW AND DEVELOPMENT OF HYPOTHESIS

Agency Theory

Agency theory is a theory that addresses differences in interests between agents and principals (Jensen & Meckling, 1976). Scott (2012) argues that agency theory is the most appropriate form of contract design to integrate principal and agent interests in the event of a conflict of interest. The company has many contracts, for example a work contract between the company and its managers and a loan contract between the company and its creditors. The employment contract which mention here is a work contract between the owner of the capital and the manager of the company. There

is interest between the agent and the principal want to maximize their utility with the information they have, the agent has more information than the principal (full of information), so that cause asymmetry of information. Information that is more owned by managers can encourage managers to take actions in accordance with their wishes and interests. As for capital owners, it will be difficult to effectively control the actions taken by managers because they only have little information available. Therefore, sometimes there are certain policies carried out by company managers without the knowledge of the capital owners or investors.

Auditing

Auditing is a critical and systematic examination by an independent party of the financial statements prepared by management along with accounting records and supporting evidence in order to be able to provide an opinion on the fairness of the financial statements. Auditor quality is needed in determining good financial statements with high-quality auditors that are expected to increase investor confidence (Agoes, 2007).

According to Mulyadi (2002) there are five types of accountant opinions:

1. Unqualified opinion.
Unqualified opinion is provided by the auditor if there are no restrictions in the scope of the audit and there are no significant exceptions regarding the fairness and application of accounting principles generally accepted in the preparation of financial statements, consistency in the application of generally accepted accounting principles, and adequate disclosures in financial statements.
2. Unqualified opinion with explanatory language
This opinion is given if the audit has been carried out or completed in accordance with auditing standards, the presentation of financial statements in accordance with generally accepted accounting principles, but there are certain circumstances or conditions

that require an explanatory language.

3. Reasonable opinions with qualified opinions
According to IAI (2002), this type of opinion is given if:
 - a. There is no sufficient competent evidence or limitation on the scope of the material audit but does not affect the financial statements as a whole,
 - b. The auditor believes that the financial statements contain deviations from generally accepted accounting principles that have a material effect but do not affect the financial statements as a whole. The deviation can be in the form of inadequate disclosure, or changes in accounting principles.
4. Adverse opinion
This opinion is given to state that the financial statements do not present fairly the financial position, results of operations and cash flows in accordance with generally accepted accounting principles. If the financial statements are given an unfair opinion by the auditor, then the information presented by the client in the financial statements is totally untrustworthy, so that it cannot be used by users of financial information for decision making. The auditor must explain the reasons for supporting the opinion that is not fair and the main impact of things that cause the opinion to be given to the financial statements.
5. Statement of not giving opinions (disclaimer opinion)
This statement is feasible if there are restrictions on the scope of the audit that are very material both by the client and because of certain conditions and the auditor is not independent of the client.

Managerial ownership

According to Sugiarto (2009) managerial ownership

is ownership of shares by the management of the company. The greater the managerial ownership in the company, the managerial party will try to improve its performance for the benefit of shareholders, so as to avoid the existence of earnings management carried out by company managers.

Earnings management

Earnings management is one of the factors that can reduce the credibility of financial statements, and add bias in financial statements and disrupt financial statement users who believe the profit figures from the engineering as profit numbers without engineering (Wiryadi and Sebrina, 2013). Schipper (1989) defines earnings management as intentional management intervention in the process of determining earnings, usually to fulfill personal goals.

The pattern of earnings management according to Scott (2012) can be done by:

1. Taking a bath
This pattern occurs during reorganization, including the appointment of a new CEO, by reporting large losses. This action is expected to increase profits in the future because the burden of future periods is reduced.
2. Income minimization
Income minimization is done when the company experiences a high level of profitability, so that if the profit in the next period is expected to drop dramatically, it can be overcome by taking the previous profit. This action was carried out with the aim of not getting political attention.
3. Income maximization
This pattern aims to report high net income for the purpose of greater bonuses, motivation to avoid violations of debt agreements, or to avoid a sharp drop in stock prices. Income maximization is applied when profit decreases. This pattern is carried out by taking the previous period's profit deposits or withdrawing profits

for the future period, for example by delaying the charging of costs.

4. Income smoothing

This pattern is carried out by the company by leveling the reported earnings, so as to reduce the fluctuations in profit that are too large, because investors generally prefer relatively stable profits.

Income smoothing

According to Belkoui (2000) income smoothing is defined as reducing fluctuations in earnings from year to year by moving income from high years of income to less favorable periods. Income smoothing is a general form of earnings management. In this strategy managers increase or decrease reported earnings to reduce fluctuations. Income smoothing also includes not reporting current earnings in bad periods (Subramanyam and John, 2010)

The purpose of the accounting method in question is as follows (Suryandari, 2012):

1. Achieve tax benefits
2. Giving good impression from the owner and creditor to the management performance.
3. Reducing fluctuations in earnings reporting and reducing risk.
4. Produce stable profit growth.
5. Maintain their position / position in the company

Eckel (1981) divides two types of income smoothing, namely:

1. Naturally Smooth (natural leveling)
This alignment has the implication that the nature of the income smoothing process itself produces a flat flow of profit. We can find this in the acquisition of income from public needs / services, where the flow of existing profits will be flattened by itself without interference from other parties.
2. Intentionally Being Smoothed by Management
In designed smoothing, the leveling that

occurs is due to intervention or interference from other parties, in this case management. Designed smoothing can be divided into 2 types, namely:

- a. Artificial smoothing (accounting smoothing), is an accounting manipulation carried out by management to spread profits.
- b. Real smoothing (transactional or economic smoothing), is a management action to control economic events. Management can flatten income by changing the company's production decisions and / or the company's investment decisions at the end of the year based on how the company improves its performance at that time.

Hypothesis Development

Influence of Audit Opinion on Income Smoothing

De Angelo (1981) mentions that audit quality is the probability that an auditor finds and reports about a violation in the audit accounting system. The role of the auditor in producing audit reports is very important by providing opinions or opinions on a company's financial statements. Auditing provides added value to the company's financial statements because the public accountant as an independent party at the end of the examination will give an opinion regarding the fairness of the financial position, results of operations, changes in equity, and cash flow statements. If the financial statements have been audited, and received an Unqualified Opinion from KAP, the financial report user can be sure that the financial statements are free from material misstatement and are presented in accordance with generally accepted accounting principles in Indonesia (Agoes, 2007). Guna and Herawaty (2010) show that audit quality influences income smoothing actions. Amijaya, and Andri's (2013) research also shows that auditors influence earnings management.

Based on this explanation, the following hypothesis is proposed:

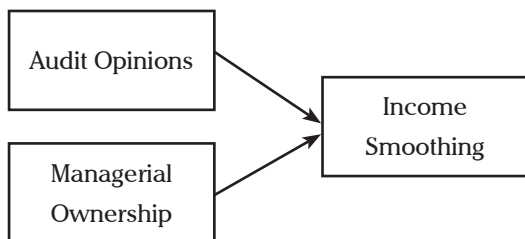
H1: Audit opinion influences income smoothing.

Influence of Managerial Ownership on Income smoothing

Managerial ownership is the number of shares owned by management. In a company, if there is managerial ownership there is more information provided to the public. In research conducted by Agustia (2013) shows that managerial ownership does not have an influence on earnings management. However, Kouki et al (2011) revealed that managerial ownership has a negative effect on earnings management and can improve the quality of the financial reporting process, this is because when managers also have a portion of ownership, they will act the same as common shareholders and ensure that financial statements has been presented fairly and revealed the real condition of the company. Similar to the results of Oktovianti and Agustia (2012), which states that managerial ownership has a significant negative effect on earnings management.

Based on this explanation, the following hypothesis is proposed:

H2: Managerial ownership influences income smoothing.



Picture 1. Framework

METHODS

The population in this research are 30 major banking companies in Indonesia. The sampling technique used is purposive sampling, which is the determination of the sample based on the suitability of certain characteristics and criteria. The number of companies that meet the criteria to be used as research objects is 28 banking companies. The sampling process is described in Table 1 as follows.

Table 1. The Number of Sample Companies

Criteria	Total
The largest company in Indonesia	30
Banking companies that do not meet the criteria	2
Companies that meet criteria	28
Total sample for 7 years (2011-2017)	196

Source: Secondary data processed, 2018

Data collection methods in this research use secondary data, namely data derived from banking companies in Indonesia in 2011-2017. These data were obtained from the website of the IDX, OJK, and the site of each sample company. Data analysis used in this research is to use logistic regression with SPSS 21 data processing.

RESULTS AND DISCUSSION

Index Eckel Calculation Results

The company is classified as income smoothing if:

- a. Index Eckel value ≥ 1 then the company is classified as not doing income smoothing
- b. and if the Index Eckel < 1 then the company is classified as doing income smoothing.

Table 2. Index Eckel Result

Status	2011	2012	2013	2014	2015	2016	2017
Doing Income Smoothing	17	11	14	10	8	7	7
Not doing Income Smoothing	11	17	14	18	10	21	21
Total	28	28	28	28	28	28	28

Source: Secondary data processed, 2018

From the determination of the Eckel index, table 2 shows the number of companies that make income smoothing and do not make income smoothing.

Descriptive Analysis Results

Table 3. Descriptive Statistical analysis

Descriptive Statistics			
	N	Minimum	Maximum
Income Smoothing	196	,00	1,00
Audit Opinion	196	,00	1,00
Managerial Ownership	196	,00	13,47
Valid N (listwise)	196		

Source: Secondary data processed, 2018

Table 3 shows that: the value of descriptive statistical test for 28 banking companies for 7 years so that the total research observations amounted to 196 sample companies with the average value of companies that do income smoothing is 37.75 percent or as many as 74 samples of the total research sample for the period 2011 to 2017.

The audit opinion variable has a total of 196 samples for 7 years of observation with the period 2011-2017 having a minimum value of 0 and having a maximum value of 1. Variable managerial ownership has a total of 196 samples for 7 years observation with the period 2011 - 2017 has a minimum value of 0 and maximum 13.47.

Logistic Regression Test Results

Logistic regression was used in this study because the dependent variable in the study was a dummy variable. Logistic regression is used to test whether the probability of the occurrence of the dependent variable can be predicted by the independent variable (Ghazali, 2013).

Following are the results of the logistic regression analysis test:

1. Model Feasibility Test

The first step to knowing that a logistic regression model is an appropriate model will first look at the suitability or feasibility of the overall model. In this case the Hosmer and Lameshow Test is used. The following is a Hosmer and Lameshow Test Test table:

Table 4. Hosmer and Lemeshow Test

Step	Chi-square	df	Sig.
1	4,445	4	,349

Source: Secondary data processed, 2018

Based on table 4 above, the Chi-Square test results are 4,445 with a significance value of 0,349. It can be concluded that the model is able to predict the value of its observations.

2. Test Fit Model (-2log likelihood)

Testing is done by comparing values -2log likelihood (block number = 0) with final -2log likelihood (block number = 1). If there is a decline, then the model shows a good regression model. Following are the Fit Model Test tables:

Table 5. Test Fit Model Block 0

Iteration History ^{a,b,c}		
Iteration		-2 Log likelihood
Step 0	1	261,754
	2	261,751
	3	261,751

Source: Secondary data processed, 2018

Table 6. Test Fit Model Block 1

Iteration History ^{a,b,c,d}		
Iteration		-2 Log likelihood
Step 1	1	258,877
	2	258,806
	3	258,805
	4	285,805

Source: Secondary data processed, 2018

From table 5 and table 6, we can see the initial log-likelihood values of 261.754 and after entering the two independent variables, the final log-likelihood

value decreased by 2.949 to 258.805, so it can be concluded that this regression model is feasible to use.

3. Regression Coefficient Testing

Regression coefficient testing is done to test how far all independent variables included in the model have an influence on the dependent variable. Following are the results of data analysis with logistic regression:

Table 7. Regression Logistic Analysis

		Variables in the Equation				
		B	S.E.	Wald	df	Sig.
Step 1 ^a	OA	-,438	,335	1,712	1	,191
	KM	-,099	,090	1,196	1	,043
	Constant	-,093	,290	,102	1	,750

Source: Secondary data processed, 2018

From this logistic regression test the regression equation is obtained as follows:

$$PL = -0,093 - 0,438 OA - 0,099 KM$$

Information :

- P : Income smoothing
- OA : Audit Opinion
- KM : Managerial Ownership

The audit opinion variable has a negative regression coefficient of 0.438. This means that if the company gets a fair audit opinion without exception, the probability of the company to make income smoothing will decrease by 0.438.

Managerial ownership variables have a negative regression coefficient of -0.099, this means that if there is managerial ownership in the company then the probability of the company to make income smoothing will decrease by 0.099.

DISCUSSION OF HYPOTHESIS TESTING RESULTS

The Influence of Audit Opinion on Income Smoothing

The audit opinion variable shows the regression

coefficient of -0.438 with a significance level of 0.191 which means that in this research audit opinion has a negative but not significant effect because the significant value is greater than 0.05. This study proves that the audit opinion in the company is not significant to income smoothing, so the H1 of this research is rejected.

This indicates that with a low audit opinion does not indicate the company is making income smoothing. The results of this research indicate that audit opinion does not affect income smoothing. This may be due to law enforcement in Indonesia that is still weak can make auditors less able to develop the ability to detect earnings management practices. This reason is based on the opinion expressed by Ettredge (in Fitriany, 2012) that one of the things that supports the auditor to develop its capabilities is a fairly good legal environment. The auditor is unable to influence earnings management because management utilizes the accrual accounting system.

According to Bazerman, Morgan and Loewenstein (1997) even though the auditor checks the company's financial statements on behalf of external users, the management of the company that compiles and issues a statement to hire and pay the auditor so that the auditor is less independent in providing audit opinions. Hardiningsih (2010) revealed that auditor independence is related to the auditor's ability to detect earnings management, the possibility that the auditor will find misstatements depends on the auditor's technical capabilities while the act of reporting misstatements depends on the auditor's independence. According to Amijaya and Andri (2013) auditor independence does not affect earnings management due to other factors that can interfere with auditor independence such as audit fees, and non-audit services.

The Influence of Managerial Ownership on Income Smoothing

Managerial ownership variables show a regression coefficient of -0.099 with a significance level of

0.043 which means that in this research managerial ownership has a significant negative effect because the significance value is less than 0.05. This study proves that managerial ownership in a company has a significant influence on income smoothing, so H2 research is accepted. This indicates that the ownership of shares in the company can reduce the actions of managers to make income smoothing. When managers have a share of ownership in the company, they will act the same as their general shareholders and ensure that the financial statements are presented fairly and disclose the real condition of the company. The results of this study agree with agency theory which states that managerial ownership structure is believed to have the ability to influence the course of the company which can affect the company's performance. Agency problems can be reduced by managerial ownership.

According to Sugiarto (2009) the greater the managerial ownership in the company, the managerial party will try to improve its performance for the benefit of shareholders, so as to avoid the existence of earnings management conducted by company managers. Large share ownership in terms of economic value has an incentive to monitor. Theoretically, when managerial ownership is low, the incentives for the possibility of managerial opportunistic behavior will increase. Management ownership of the company's shares is considered to be able to harmonize the potential differences in interests between outside shareholders and management (Jensen and Meckling, 1976). So the agency problem will be lost if a manager is also at the same time as an owner. The greater the proportion of management ownership in the company, the management tends to try harder for the benefit of shareholders who also include themselves.

The results of this research agree with the results of the research by Kouki et al (2011) which revealed that managerial ownership has a negative effect on earnings management and can improve the quality of the financial reporting process. Similar to

the results of Oktovianti and Agustia (2012), which states that managerial ownership has a significant negative effect on earnings management. Pratiwi's research, et al (2015) also shows that there is a significant influence with a negative coefficient between managerial ownership on information asymmetry, this is in accordance with the principle of transparency in the implementation of corporate governance which reveals that the higher managerial ownership in a company, the information disclosure that occurs in the company is getting higher too, so it will reduce the gap of the information contained in it. In addition, the use of professional management will reduce the information gap in the company because professional management will maintain its credibility so that the company that becomes its responsibility will be more transparent.

MANAGERIAL IMPLICATIONS

This research provides empirical evidence that audit opinion does not have a significant effect on income smoothing, while managerial ownership has a significant effect on income smoothing. Subsequent research is expected to add other variables that are predicted to affect income smoothing and can also use a wider sample, not only banking companies but can use companies that have gone public in Indonesia..

CONCLUSION

Based on the results of the research as described, it can be concluded that:

1. Based on the Index Eckel calculation, it is known that in 2011 there were 17 banking companies that made income smoothing; and for 2012 there were 11 banking companies that made income smoothing. Furthermore, in 2013 there were 14 banking companies that made income smoothing, and in 2014 there were 10 companies that made income smoothing. In 2015 there were 8 companies that made income smoothing, for 2016 there were 7 companies that made income smoothing, and in 2017 there were also 7 companies that made income smoothing.

2. Audit Opinion does not affect income smoothing in banking companies in Indonesia for the period 2011-2017.
3. Managerial ownership affects the income smoothing of banking companies in Indonesia for the period 2011-2017. ■

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