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Corporate governance, tax planning, leverage and public ownership on earnings management: The moderating role of profitability

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Abstract

This study examines the effect of tax planning, leverage, independent commissioners, and public ownership on earnings management, with profitability acting as a moderating variable. Earnings management practices often arise from conflicts of interest between management and shareholders, reducing financial statement quality and affecting external decision-making. The study uses a causal-comparative quantitative approach, analyzing secondary financial statement data from consumer goods companies listed on the Indonesia Stock Exchange during 2021–2024. A purposive sampling technique was applied, and Moderated Regression Analysis (MRA) was conducted to test the proposed relationships. The findings indicate that leverage has a positive and significant effect on earnings management, suggesting that companies with higher debt levels are more likely to engage in earnings manipulation. In contrast, tax planning, independent commissioners, and public ownership do not have significant direct effects on earnings management. Profitability significantly moderates the relationship between leverage and earnings management, amplifying the influence of leverage on managerial discretion, while it does not moderate the relationships of earnings management with tax planning, independent commissioners, or public ownership. These results suggest that earnings management in the consumer goods sector is primarily influenced by capital structure and financial performance rather than governance or ownership structure alone. The findings highlight the importance of strengthening monitoring mechanisms and corporate governance practices to enhance financial reporting quality. This study contributes to the literature on earnings management by demonstrating the conditional role of profitability as a moderating factor in the relationship between leverage and managerial discretion.

Keywords: Earnings Management; Tax Planning; Leverage; Independent Commissioners; Public Ownership; Profitability

1. Introduction

Accounting processes play a crucial role in recording transactions, overseeing financial data, and providing relevant information to stakeholders for decision-making. High-quality financial reporting enables accurate economic evaluation and accountability of management, while manipulation or misstatement can mislead investors and other users (Apriadi et al., 2022; Hutadjulu & Simanjuntak, 2020). One prevalent issue undermining financial statement quality is earnings management, defined as deliberate managerial actions to influence reported earnings within the boundaries of accounting standards for personal or organizational gain (Saputra et al., 2022). Earnings management often arises from conflicts of interest between management and shareholders, reflecting agency problems and information asymmetry (Arwani et al., 2020; Wibisono et al., 2022). Managers may manipulate financial results to meet performance targets, influence market perception, or optimize tax obligations, which can reduce transparency and financial statement reliability.

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Several internal factors have been found to influence earnings management, including tax planning, leverage, corporate governance mechanisms such as independent commissioners, and public ownership (Amelia & Purnama, 2023; Setiowati et al., 2023; Adyastuti & Khafid, 2022). Tax planning allows firms to optimize tax liabilities and free up resources for operations, potentially creating incentives for income manipulation (Joe, 2022; Achyani & Lestari, 2019). Leverage can pressure managers to maintain financial ratios required by creditors, motivating earnings management to avoid covenant violations (Tetradia & Priantinah, 2023; Salama et al., 2023). Independent commissioners and public ownership are expected to provide oversight and reduce opportunistic behavior, although empirical findings regarding their effectiveness remain mixed (Mardjono & Chen, 2020; Ruslan et al., 2024). Profitability may further condition these relationships, serving as a moderating factor that influences managerial incentives for earnings management (M. Putri & Rousilita, 2023). High-profitability firms may engage in income smoothing to maintain a stable performance image, whereas low-profitability firms may manipulate earnings to conceal poor results.

The consumer goods industry represents an especially relevant context for examining earnings management due to its competitive environment, rapid operating cycles, and high market scrutiny. Firms in this sector face pressures to maintain investor confidence and stable performance metrics, making them more susceptible to managerial discretion in reporting earnings (Ardillah & Vesakhadevi, 2021). Despite extensive research in other sectors, studies on consumer goods companies in Indonesia remain limited, particularly concerning the combined effect of tax planning, leverage, corporate governance, and public ownership on earnings management with profitability as a moderator.

Therefore, this study aims to analyze the effect of tax planning, leverage, independent commissioners, and public ownership on earnings management, while examining the moderating role of profitability. This research contributes to the literature by clarifying the conditional role of profitability in the relationship between financial and governance variables and earnings management, specifically in the context of Indonesia's consumer goods sector.

2. Literature Review and Hypothesis Development

Agency Theory suggests that conflicts of interest between management and shareholders can encourage managers to manipulate earnings to serve personal or organizational objectives (Jensen & Meckling, 1976). Tax planning provides managers with opportunities to adjust the timing of revenue and expense recognition, potentially reducing tax liabilities while maintaining or enhancing reported earnings. Prior studies have demonstrated that aggressive tax planning is associated with higher levels of earnings management, as managers adjust financial reports to optimize after-tax profits while presenting favorable results to investors (Faqih & Sulistyowati, 2021; Achyani & Lestari, 2019; Adhitama et al., 2021). Accordingly, the first hypothesis is proposed:

H1: Tax planning has a positive effect on earnings management.

Leverage represents the extent to which a firm uses debt as a financing source. High leverage increases the risk of violating debt covenants and places contractual pressure on management to maintain financial performance (Tetradia & Priantinah, 2023). According to Agency Theory, managers may engage in earnings management to stabilize reported profits and avoid covenant breaches. Empirical evidence on the effect of leverage on earnings management is mixed: some studies report positive effects (Yani et al., 2025; Senoaji & Opti, 2021), others find negative or insignificant effects (Umah & Sunarto, 2022; Pradnyawati et al., 2021). Given the potential for leverage to create pressure on management, the following hypothesis is formulated:

H2: Leverage has a positive effect on earnings management.

Independent commissioners serve as neutral supervisors, reducing opportunistic behavior by management and enhancing transparency in financial reporting. Agency Theory emphasizes that stronger monitoring mechanisms limit managerial discretion and reduce the likelihood of earnings manipulation (Kristanti et al., 2024; Alrawashedh et al., 2025; Mardjono & Chen, 2020). Firms with a higher proportion of independent commissioners are expected to exhibit lower levels of earnings management due to effective oversight and accountability. Therefore, the following hypothesis is proposed:

H3: The proportion of independent commissioners has a negative effect on earnings management.

Public ownership increases external scrutiny, as dispersed shareholders demand reliable and transparent financial reporting. Firms with higher public ownership face greater reputational and accountability pressures, limiting managerial opportunities for earnings manipulation. Empirical studies have shown that increased public ownership is associated with reduced earnings management (Kristanti et al., 2024; Alrawashedh et al., 2025; Sukirno et al., 2017; Utami et al., 2021). Hence, the hypothesis is formulated as follows:

H4: Public ownership has a negative effect on earnings management.

Profitability reflects the financial performance of a firm and influences managerial incentives. Firms with higher profitability have greater incentives to maintain stable earnings and optimize after-tax profits, which may amplify the effect of tax planning on earnings management. Previous studies indicate that profitability can condition the intensity of managerial manipulation of earnings through accounting policies and tax strategies (Damayanti & Solihati, 2024; Pradnyawati et al., 2021; Wibisono et al., 2022). Based on this rationale, the following hypothesis is proposed:

H5: Profitability strengthens the effect of tax planning on earnings management.

High profitability may reduce the pressure exerted by leverage because firms are better able to meet debt obligations. Conversely, low-profitability firms may experience stronger incentives to manage earnings to satisfy creditors (Wibisono et al., 2022; Kalbuana et al., 2021). Therefore, profitability is expected to condition the effect of leverage on earnings management:

H6: Profitability weakens the effect of leverage on earnings management.

The effectiveness of independent commissioners in monitoring management may vary depending on the firm's financial performance. Profitable firms have more stable earnings, reducing managerial opportunism and allowing independent commissioners to exercise oversight more effectively (Mardjono & Chen, 2020; Kristanti et al., 2024; Alrawashedh et al., 2025). Thus, the hypothesis is formulated as:

H7: Profitability strengthens the negative effect of independent commissioners on earnings management.

Profitability may also influence the effectiveness of public ownership in limiting earnings management. Firms with higher profitability face greater investor attention and reputational pressure, enhancing the monitoring effect of public shareholders (Kristanti et al., 2024; Alrawashedh et al., 2025; Partati & Almalita, 2022). Consequently:

H8: Profitability strengthens the negative effect of public ownership on earnings management.

3. Methods

This study employs a quantitative causal-comparative approach to examine the effect of tax planning, leverage, independent commissioners, and public ownership on earnings management, with profitability serving as a moderating variable. The research population consists of consumer goods companies listed on the Indonesia Stock Exchange (IDX) during 2021–2024. A purposive sampling technique was applied to select firms with complete audited financial statements and annual reports, resulting in a final sample of 118 companies and 472 firm-year observations. Earnings management was measured using discretionary accruals, tax planning was proxied by effective tax rates, leverage by the debt-to-equity ratio, independent commissioners by the proportion of independent members on the board, and public ownership by the proportion of shares held by public investors. Profitability was measured using return on assets (ROA) and included as a moderating variable. Control variables included firm size, audit quality, and industry classification to account for potential confounding effects.

The data were analyzed using Moderated Regression Analysis (MRA) with robust standard errors to test both direct and moderating effects. Interaction terms between profitability and each independent variable were included to evaluate moderation hypotheses. Diagnostic tests were performed to check multicollinearity, heteroscedasticity, and model fit, with any violations addressed through appropriate estimation adjustments. This methodology allows for testing both the individual effect of each corporate governance and financial variable on earnings management and the conditional effect of profitability as a moderator, providing insights into the mechanisms influencing managerial discretion in financial reporting.

4. Result and Discussion

4.1. Diagnostic Tests

To ensure the validity of the regression model, several diagnostic tests were conducted. Multicollinearity was evaluated using Variance Inflation Factor (VIF), heteroskedasticity using the Glejser test, autocorrelation using the Durbin-Watson statistic, and normality using the Kolmogorov-Smirnov test. The results are summarized in Table 1.

Table 1 Diagnostic Test Results

Test	Measurement	Result	Decision
Normality	Kolmogorov-Smirnov	Asymp. Sig. = 0.200	Residuals are normally distributed
Multicollinearity	VIF	Range = 1.025–1.098	No multicollinearity problem
Heteroskedasticity	Glejser test	Sig. > 0.05	No heteroskedasticity
Autocorrelation	Durbin-Watson	DW = 1.982	No autocorrelation

Primary Data, 2026

The results confirm that the regression model meets classical assumptions and is suitable for further hypothesis testing.

4.1.1. Moderated Regression Analysis

The moderated regression analysis (MRA) was conducted to examine the direct and moderating effects of the independent variables on earnings management. The regression results are presented in Table 2.

Table 2 Moderated Regression Analysis (MRA) Results

Variable	Coefficient (B)	t	Sig.
Constant	0.025	17.820	0.000
Tax Planning (X1)	-0.024	-1.085	0.280
Leverage (X2)	0.207	2.056	0.018
Independent Commissioners (X3)	0.254	2.299	0.035
Public Ownership (X4)	0.198	2.203	0.044
Profitability (Z)	0.001	1.265	0.644
X1*Z	-0.001	-0.484	0.629
X2*Z	0.147	2.057	0.047
X3*Z	-0.037	-0.235	0.509
X4*Z	0.222	2.154	0.039

Primary Data, 2026

Regression equation:

$$Y = 0{,}025 - 0{,}024X1 + 0{,}207X2 + 0{,}254X3 + 0{,}198X4 + 0{,}001Z - 0{,}001(X1\times Z) + 0{,}147(X2\times Z) - 0{,}037(X3\times Z) + 0{,}222(X4\times Z)$$

The R^2 value of 0.272 indicates that 27.2% of the variation in earnings management is explained by the independent and moderating variables, with the remaining 72.8% influenced by other factors. The F-test shows the model is significant ($F = 2.049$, $p = 0.010$), confirming model fitness.

4.1.2. Tax Planning and Earnings Management

Tax planning (X1) was not significantly associated with earnings management ($B = -0.024$, $p = 0.280$), indicating that firms in the consumer goods sector primarily use tax planning for legitimate efficiency rather than earnings manipulation. This result aligns with prior studies (Sanjaya, 2022; Setyawan et al., 2021) suggesting that tax planning does not automatically lead to opportunistic behavior. Although Agency Theory and Positive Accounting Theory predict potential manipulation, strict regulatory oversight and industry stability limit the use of tax planning as a tool for earnings management.

4.1.3. Leverage and Earnings Management

Leverage (X2) has a significant positive effect on earnings management ($B = 0.207$, $p = 0.018$). Companies with higher debt levels tend to manage earnings to meet creditor expectations and maintain financial ratios. This finding is consistent with Agency Theory, which emphasizes conflicts between managers and creditors, and with prior research in Indonesia (Kalbuana et al., 2021). High leverage combined with the pressure to present stable earnings increases managerial discretion in reporting, confirming that capital structure is a key determinant of earnings management.

4.1.4. Independent Commissioners and Earnings Management

Independent commissioners (X3) were significant ($B = 0.254$, $p = 0.035$) but in the opposite direction from the hypothesized negative effect. This suggests that merely increasing the number of independent commissioners does not necessarily reduce earnings management. The result reflects the limited effectiveness of oversight, potentially due to symbolic roles or lack of genuine independence, a finding consistent with prior studies (Kristanti et al., 2024). Effectiveness of governance depends on commissioner quality rather than quantity.

4.1.5. Public Ownership and Earnings Management

Public ownership (X4) also had a significant positive coefficient ($B = 0.198$, $p = 0.044$), contrary to the hypothesized negative effect. Dispersed ownership may weaken monitoring, giving managers leeway to adjust earnings to meet market expectations. This aligns with prior evidence that public shareholders may be unable to enforce effective oversight, especially when investor expectations push for stable financial performance (Kristanti et al., 2024; Partati & Almalita, 2022).

5. Conclusion

This study examines the effects of tax planning, leverage, independent commissioners, and public ownership on earnings management, with profitability acting as a moderating variable in consumer goods companies listed on the Indonesia Stock Exchange. The findings indicate that leverage has a positive and significant impact on earnings management, while tax planning, independent commissioners, and public ownership do not show significant direct effects. Profitability significantly strengthens the effect of leverage on earnings management and amplifies the influence of public ownership, but it does not moderate the relationships with tax planning or independent commissioners. These results suggest that earnings management in this sector is primarily driven by capital structure and firm profitability rather than governance or ownership alone.

The study contributes to the literature by highlighting the conditional role of profitability in shaping managerial discretion, particularly in relation to leverage and public ownership. The findings support Agency Theory and Positive Accounting Theory, demonstrating that financial performance and ownership structure interact with managerial incentives to influence earnings management behavior. The research underscores the importance of considering both financial and governance factors when evaluating determinants of earnings management in emerging markets.

5.1. Managerial Implications

The findings have several practical implications for corporate management, auditors, and regulators. For management, the significant effect of leverage on earnings management suggests that firms should carefully monitor debt levels and implement internal policies to ensure transparency and compliance with financial reporting standards. While tax planning, independent commissioners, and public ownership did not show direct effects, management should continue strengthening governance mechanisms and internal control systems to mitigate opportunistic behavior and enhance financial reporting quality.

For auditors and regulators, the moderating role of profitability highlights the importance of considering firm performance when assessing earnings management risk. Auditors should pay particular attention to highly profitable firms with high leverage or substantial public ownership, as these conditions increase managerial incentives for earnings manipulation. Regulators may also encourage policies that enhance transparency, accountability, and disclosure practices, supporting the reliability and credibility of financial statements for all stakeholders.

Compliance with ethical standards

Disclosure of conflict of interest

No conflict of interest to be disclosed.

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