

## A Review of Income Smoothing through Company Size, Profitability, and Managerial Ownership

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### Abstract

*This study was conducted to test empirically the effect of firm size, profitability, and managerial ownership on income smoothing with firm age and leverage as control variables. Income smoothing is proxied using the Eckel index. This research is a quantitative research and the objects in this research are manufacturing sector companies listed on the Indonesia Stock Exchange (IDX) for the 2019-2021 period. Selection of sample criteria was carried out by purposive sampling technique with predetermined criteria and obtained data of 282 samples obtained from 94 companies. Testing the hypothesis in this study used multiple linear regression analysis with the help of STATA software version 16. The results of this study indicate that 1) company size has no effect on income smoothing; 2) profitability has no effect on income smoothing; and 3) managerial ownership has no effect on income smoothing.*

**Keywords:** income smoothing; Company Size; Profitability; Managerial ownership.

### Introduction

Financial statements are a financial description of a company that has the objective of presenting information to shareholders and investors. Financial statements are the results of business activities that are reported by the company periodically, where it is management's obligation to the owner for performance during a certain period. In the financial statements, one of the information is information related to profit. Profit is one of the most important information and measures to measure performance in company management. The importance of the information generated by the company regarding profits, then becomes the basis for the management side to carry out inappropriate practices (dysfunctional behavior).

*Income smoothing* is one of the earnings management techniques that companies do. Income smoothing is a deliberate action taken by managers by applying accounting policies by avoiding fluctuations in profits (Rosalie et al., 2019). In general, management takes steps when the profits generated are relatively low and takes steps to reduce profits when the profits generated are relatively high, because if there is a decrease in profits that are not directly sourced from a decrease in assets, it will have a negative impact on the company. Financial Accounting Standards provide leeway for management in terms of choosing an accounting method that better reflects the actual condition of the company. This flexibility is usually for the purpose of managing earnings (earnings management) by management.

*Income smoothing* often said whether good or not. The implementation of income smoothing is said to be good if there is no element of fraud in it (Wijoyo, 2014). Management performs income smoothing actions generally based on a variety of good reasons, namely to satisfy company owners, for example to make the company a good value, so that there is an assumption that by increasing the stock price, the company has a low risk and to provide satisfaction for its own interests, for example maintaining its position. and get bonuses or rewards (Maotama & Astika, 2020). Even though the income smoothing action is carried out with a purpose and reason, it makes the presentation of the financial statements inadequate because the management itself makes changes to the information contained in the financial statements. so that the information to be used by users of financial statements becomes

inaccurate. Therefore, users of financial statements are expected to be aware of the information presented in financial reports (Juniarti & Carolina, 2005).

The phenomena that occur regarding income smoothing, which motivated the authors to conduct this research, such as at PT Toshiba, where the company made a deviation, namely the company increased its profits or inflated profits for seven years to reach US \$ 1.2 billion because of the desire to get high achievements before the end. years which caused the head of the business unit to have his financial reports manipulated by continuously abusing accounting procedures (Judge, 2015). Then in 2016, PT. Sepatu Bata Tbk recorded poor performance with a decrease in net profit of 67.70% from the initial Rp. 129.52 billion for 2015 to Rp. 42.23 billion. However, in 2017 PT Sepatu Bata Tbk recorded a profit that experienced a significant increase with an increase in the number of sales. PT Sepatu Bata Tbk managed to report sales of IDR 514.7 billion in the first half of 2017 by making the company's domestic sales increase which was IDR 468.43 billion to IDR 512.04 billion. However, export sales have decreased, from Rp. 4.14 billion until June 30 2016 to Rp. 2.66 billion in the first six months of 2017 (Rahman, 2017).

Furthermore, at PT Garuda Indonesia Tbk where in 2018 the company experienced a profit by earning a net profit of US \$ 809.4 thousand. This is surprising because PT Garuda Indonesia Tbk should have experienced no profits. In the first nine months of 2018 the company continued to make losses of US\$114.08 million. At the end of 2018 it was surprising that the profit reported by PT Garuda Indonesia Tbk experienced a profit. (Pratwi, 2019). Then PT Akasha Wira International Tbk (ADES), namely in 2020, earned a profit for the year of Rp. 135.78 billion, which experienced an increase of 62.65% when compared to 2019 of Rp. 83.885 billion. Meanwhile, net sales in that year decreased by 11.91% from Rp 764.70 billion to Rp 673.36 billion. (Aziz, 2021).

Based on the phenomena that exist in some of these companies, it proves that there are still many companies that carry out income smoothing. It can be seen that companies carry out income smoothing with the intention of manipulating their profits with the intention to change or even increase profits in a current period so that the profits generated in that period look good and the wishes of the management and company owners will be appropriate. So there are several factors that can influence the occurrence of income smoothing in the company. These factors were examined in this study regarding income smoothing, namely company size, profitability, and managerial ownership with the control variables used, namely company age and leverage.

Based on this background, the formulation of the problem in this study is:

1. Does company size affect income smoothing?
2. Does profitability affect income smoothing?
3. Does managerial ownership affect income smoothing?

In connection with the formulation of the problem above, the research objectives to be achieved are to prove empirically the effect of company size, profitability, and managerial ownership on income smoothing

## **2.Literature Review**

### **Agency Theory**

According to Jensen & Meckling (1976) Agency theory is a contract between the manager (agent) and the owner (principal). In order to expedite the contractual relationship, then in a company there is a division of tasks between the principal and the agent. Agency relationships arise when selecting someone to offer a service and then delegating decision-making power to that person creates an agency relationship. Both agents and principals want to increase the value of the company through increasing shareholder profits. *Principal* want

management to act in the interest of the principal. However, agents often do not always act for the needs of the principal or carry out behavior that is contrary to the interests of shareholders so that conflicts between shareholders and managers occur.

### **Profit management**

According to Scott (2015 p.445), earnings management is a real action or policy that management chooses where affect profit so that the reported profit goal is achieved. Earnings management also means behavior that is deliberately carried out by management by reducing or increasing profits, causing the credibility of financial statements to decrease and mislead stakeholders in terms of assessing company performance and will affect the results of reported accounting numbers. Management will be compelled to report the results of financial statements in proportion to what is desired and not in proportion to the proper conditions. This actually creates a negative impact where the quality of earnings will decrease as well as in terms of making decisions based on information about profits or the overall financial statements. (Panjaitan & Muslih, 2019).

### **Income Smoothing**

*Income smoothing* is a form of earnings management (Cahan et al., 2008). Income smoothing actions are carried out to obtain the expected profit post on profit and loss reporting so that the market shows interest in investing, investors often only focus on the rules that have been set by the company to obtain information related to profits. (Subekti, 2005). According to Koch (1981) in Kamaruddin et al. (2003) said where income smoothing is an effort to exercise control to reduce the variation contained in the income statement within a period of time which can be done through manipulated accounting transactions that occur within the company.

### **Company Size**

In research Suwardika & Mustanda (2017), Company size is the size of the company whose measurement can be through the size of the company's capital, sales and total assets. The company is in the maturity stage when the company's total assets are getting bigger and the mature company is expected to have positive cash flow and provide profit over a long period of time. Medium and large companies are under more pressure from their stakeholders, so that compared to small companies, companies must have performance that is in line with investor expectations. Larger companies also serve as wider stakeholders. As a result, if large companies take different actions it has a significant impact on the public interest compared to small companies.

### **Profitability**

The ratio used in terms of measuring a company's capability in which it generates profits from normal business activities is the definition of a profitability ratio (Hery, 2018 p.191). The profitability ratio is the ratio to determine the company's ability to earn profits. This ratio is also a measure of how effective corporate governance is. This can be seen by the profits derived from sales and investment income. Where it can be said, using this ratio shows how efficient a company is (Kasmere, 2018 p.196).

### **Managerial ownership**

Managerial ownership is the percentage of shares owned by management. This ownership will affect the performance of a management. Management's responsibility to try to maximize its performance and meet management's wishes is getting bigger because of large managerial ownership. Agency conflict can be minimized by managerial ownership in firms (Jensen and Meckling, 1976). Management who owns shares will certainly better understand the situation that occurs in the company where he works so that the management who owns

shares will work as much as possible so that the benefits of his position can be owned by the ranks of managers and his position as the owner of the company.

Referring to the agency theory, companies with large-scale companies have a high tendency to carry out income smoothing when compared to smaller-scale companies, because large-sized companies receive more attention and supervision from investors, which causes managers to tend to determine accounting methods with deferrals. reported current period profits to future periods which will make reported profits smaller (Setyaningsih et al., 2021). The bigger a company is, the attention it gets from investors, analysts and the government also increases because the company is considered to be earning more profit so that this can affect the imposition of higher costs such as tax costs. Therefore, the company maximizes efforts to avoid high profit fluctuations, if the recorded profit is large enough it will have an impact on the taxes paid, namely the tax is getting bigger. In research conducted by Maotama & Astika (2020) and Andini & Agustina (2020) concluded the results that company size has a positive influence on income smoothing.

**H1: Firm size has a positive influence and significant to income smoothing.**

Referring to agency theory, agency problems that arise between principals and agents are mainly caused by differences in goals between the two. There are different goals illustrated by profitability where each individual wants to fulfill their respective expectations for their own personal prosperity. Profitability itself is an important benchmark in assessing whether a company is healthy or not affect investors to make decisions (Winarti et al., 2020). Investors often focus their attention on the profitability of a company that has become a target in terms of investment, companies that obtain positive and high profitability will have a desire to invest in the funds owned by the company because investors think the company has good skills in earning profits. Obtained profitability stability affect investors' confidence in the investment they will make because the company is seen as good at earning profits. A high return on investment in a very profitable company is a good performance or success in operating its business. The results of research previously conducted by David & Fauzan (2017) and Fauzan & Sari (2018) concluded that the effect on profitability *income smoothing*.

**H2: Profitability own positive and significant influence on income smoothing.**

Managerial ownership is the amount of shares owned by management who are also shareholders of the company. Shares owned by managers can balance the interests of shareholders and management, because the benefits of decisions made by management are immediately felt, and management bears the risk if a loss occurs due to an incorrect decision. The majority of shares managers own influence decision making and company success. Based on agency theory according to Jensen & Meckling (1976) explained that creating monitoring costs for behavior and performance can be carried out by company owners called agency costs. In order to reduce these costs, the company can through increased managerial ownership in the company where every policy contained in the company is well researched so as not to cause harm to the company owner. If the ownership is increasing owned by the managerial side, the decision making will have a greater tendency to benefit himself and as a whole will be detrimental to the company. The results of research previously conducted by Andini & Agustina (2020) and Maotama & Astika (2020) concluded that managerial ownership has an influence on income smoothing.

**H3: Managerial ownership has a positive and significant effect on income smoothing.**

### 3. Research Methodology

#### Research Variable Measurement

Table 1. Variable Measurement

No	Variable Name	Symbol	Measurement
<b>Dependent Variable</b>			
1	Income Smoothing	IS	$\frac{CVAI}{CV\Delta S}$
<b>Independent Variable</b>			
2	Company Size	SIZE	ln Total Sales
3	Profitability	PB	$\frac{\text{Operational profit}}{\text{Net sales}}$
<b>Control Variables</b>			
4	Company Age	AGE	Year of Research - Year Listed on IDX
5	<i>leverage</i>	Lev	$\frac{\text{Total Debt}}{\text{Total Assets}}$

#### Types of research

Quantitative data method is the analysis of the data used. The quantitative method is a method in which the data search is in the form of numerical data and is examined using statistical data.

#### Population, Sample, and Sampling Technique

This study uses the population, namely manufacturing sector companies that are listed and publish financial reports published on the Indonesia Stock Exchange for the reporting periods of 2019, 2020 and 2021. Apart from the many companies in the manufacturing sector that carry out income smoothing as in the phenomenon that has been described Previously, the reason researchers determined manufacturing sector companies was because manufacturing companies were a business sector consisting of the largest industrial sub-sectors, so it was hoped that they would produce a diversity of data to obtain accurate results. In addition, based on data obtained from the Ministry of Industry, the level of investment in manufacturing sector companies will continue to increase in 2019-2021.

The sample is part of the population which is taken by sampling technique(Hardani et al., 2020 p.362).Purposive sampling technique was used in this study where the selection of this sample was determined specifically based on the objectives of the study by applying several criteria.

**Table 2. Number of Samples Based on Criteria**

No	Criteria	Amount
1.	Manufacturing sector companies that have gone public and are officially listed on the Indonesia Stock Exchange between 2019 and 2021	183
2.	Manufacturing sector companies that do not publish annual financial reports for the 2019-2021 period	-12
3.	Manufacturing sector companies whose financial reports are from 2019-2021 do not earn profits every year	-77
	<b>Number of Samples</b>	94
	<b>Observation Year</b>	3
	<b>Total Samples During the Observation Period</b>	282

Source: Data processed by researchers (2022)

### Data collection technique

Secondary data is the type of data in this study. Secondary data is data that is already available or data that is no longer needed to be collected by researchers. Sources of secondary data include statistical bulletins, library documents, company websites, government publications, company records or documentation presented by media such as the web and so on. (Sekaran & Bougie, 2017 p. 41).

### Data analysis technique

Descriptive statistical analysis and regression analysis are the analytical techniques used, while testing the hypothesis for the regression model is multiple regression analysis. Based on this, an analysis technique was determined using Microsoft Excel and STATA as a computer-assisted tool.

### Panel Data Regression

Combining a series of time data and cross data is a panel data regression (Caraka & Yasin, 2017 p.1). The reason for this panel data regression researcher is because the research year chosen for this research is not just one year, but 3 years starting from 2019-2021 and using more than one company. This study will determine the appropriate model through several tests, namely (1) Chow test, aims to test whether the model is right to determine between the common effect model and the fixed effect. (2) Lagrange Multiplier Test, to test whether the model is right to determine between the common effect and random effect models. (3) Hausman Test, This type of follow-up test aims to determine which model is better, the fixed effect model or the random effect model.

### Classic assumption test

The classical assumption test aims to make the regression equation obtained unbiased and has accuracy in estimating (Ghozali, 2018 p.175). In this classic assumption test there are several tests, namely the normality test which aims to determine whether the distribution of data is normal or not. The distribution of normal residual data is a good regression model. Multicollinearity test where to find the presence of multicollinearity by using the Variance Inflation Factor value and tolerance. If the Variance Inflation Factor does not exceed 10 and the

tolerance value exceeds 0.10, the research model being carried out can be free from multicollinearity and can be used in research.(Ghozali, 2018 p.107).

Autocorrelation test using the Wooldridge Test Autocorrelation with the provision that if the prob > 0.05 it can be interpreted that there is no autocorrelation problem in the regression model but if the prob <0.05 then it can be interpreted that there is an autocorrelation problem. The heteroscedasticity test has the objective of knowing whether the regression model has a difference in variance from one residual observation to another or not. The heteroscedasticity test can be carried out using the Breusch-Pagan. The criterion for this test is if the probability value is > 0.05 which proves that it is free from heteroscedasticity.

#### 4. Results And Discussion

This study uses as many as 94 companies based on the selection results according to the criteria. The results of descriptive statistics are listed in Table 3.

**Table 3. Results of Descriptive Statistical Analysis**

Variables	Obs	Means	std. Dev.	Min	Max
IS	282	2.54838	29.9653	-150.8869	324.2085
SIZE	282	28.7516	1.75518	21,802	33.09978
PB	282	0.12236	0.21837	0.001133	2.71697
km	282	0.06851	0.15503	0	0.739182
AGE	282	19	12.3528	0	44
Lev	282	0.41044	0.2048	0.003453	1.887043

Notes: IS: Income Smoothing, SIZE: Firm Size, PB: Profitability, KM: Managerial Ownership, AGE: Firm Age, LEV: Leverage.

Source: STATA V.16 output processed by researchers (2022)

#### Panel Data Regression

##### Chow test

**Table 4. Chow test results**

<i>Probability Restricted</i>	0.0000
$\alpha$	0.05

Source: STATA V.16 output processed by researchers (2022)

Based on the test results that have been carried out by researchers in table 4, it can be seen that the probability value is smaller when compared to the  $\alpha$  value, which means that H0 is rejected so that the correct model based on the Chow test is the fixed effect model.

#### Lagrange Multiplier Test (LM)

**Table 5. Lagrange Multiplier Test Results**

<i>Probability Restricted</i>	0.0000
$\alpha$	0.05

Source: STATA V.16 output processed by researchers (2022)

Based on the test results that have been carried out by researchers in table 5, it can be interpreted that the probability value has a smaller value than the  $\alpha$  value, which is equal to 0.0000. Therefore, H0 is rejected so that the appropriate model in this study is the random effect model.

### Hausman test

**Table 6. Hausman Test Results**

<i>Probability Restricted</i>	0.1600
$\alpha$	0.05

Source: STATA V.16 output processed by researchers (2022)

Based on the test results that have been carried out by researchers in table 6, it can be interpreted that the probability value has a greater value than the  $\alpha$  value, which is equal to 0.1600. Therefore, H0 is accepted so that the appropriate model is the random effect model. So it can be concluded that of the three tests to determine the best regression model in testing the hypothesis is the random effect model.

### Classic assumption test

#### Normality test

The normality test has the objective of deciding whether the data distribution is running normally or not. The distribution of normal residual data is a good regression model. The research data is said to be normal if the skewness value is  $< 3$  and the kurtosis value is  $< 10$ .

**Table 7. Normality Test Results After Winsorized**

Variables	Skewness	kurtosis
IS_w	-1.528866	8.302808
SIZE	-0.2468169	4.032246
PB_w	1.213153	4.04084
KM_w	2.166131	6.313514
AGE	-0.1904102	1.587278
LEV_w	-0.0867241	1.993021

Note: IS\_w: Income Smoothing, SIZE: Company Size, PB\_w: Profitability, KM\_w: Managerial Ownership, AGE: Firm Age, LEV\_w: Leverage.

Source: STATA V.16 output processed by researchers (2022)

Based on the results in table 7, it can be seen that the skewness and kurtosis values after winsorized show that each variable is in accordance with the provisions where the skewness value  $< 3$  and kurtosis  $< 10$ , which means that the research data is normally distributed.

### Multicollinearity Test

Multicollinearity test was conducted to see whether there is a relationship between independent variables (Ghozali, 2018 p.107). In this test, look at the Variance Inflation Factor (VIF) and the Tolerance value (1/VIF) of less than 10 and more than 0.10. In the initial data in the VIF study, the value was  $> 10$ . This problem can be overcome by centering variables with VIF values  $> 10$ . (Wasilaine et al., 2014).



**Table 8. Multicollinearity Test Results After Centering**

Variables	VIF	1/VIF
AGE	3.16	0.316251
LEV_w	2.7	0.369768
PB_w	2.12	0.471329
KM_w	1.23	0.810747
centered_SE	1.14	0.880402
<b>VIF means</b>	2.07	

Notes: Centered\_SIZE: Firm Size, PB: Profitability, KM: Managerial Ownership, AGE: Firm Age, LEV: Leverage.

Source: STATA V.16 output processed by researchers (2022)

Based on the results in table 8, after centering it can be seen that the company size variable has  $VIF < 10$  and  $1/VIF > 0.10$ . So it can be concluded that the data for this research variable do not have multicollinearity problems, or there is no attachment between all independent variables so that the regression model can be said to be good.

#### Autocorrelation Test and Heteroscedasticity Test

In this research, the better model is *random effect model* where this model is also known as the Generalized Least Square (GLS) where the assumption of homoscedasticity is definitely fulfilled or it can be said that the data used in the study sample is free from autocorrelation and heteroscedasticity problems so that there is no need for autocorrelation and heteroscedasticity tests (Melati & Suryowati, 2018).

#### Determination Coefficient Test

According to Lestari & Setiawan (2017), said that the test of a coefficient of determination was tested to see how big the percentage of the effect of the independent (free) variable on changes in a dependent variable. The results of the R<sup>2</sup> test in this study are shown in the following table:

**Table 9. Test Results for the Coefficient of Determination**

<i>R-square</i>	0.0289
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Source: STATA V.16 output processed by researchers (2022)

Based on the results in table 9, it can be seen that the value resulting from the R<sup>2</sup> test has equivalent results 0.0289 or equivalent to 2.89%. Therefore it shows that all the independent variables selected by the researcher, namely company size, profitability, and managerial ownership found in manufacturing companies from 2019 to 2021 can provide an explanation for income smoothing of 2.89%. While the rest, which is worth 97.11%, can be explained by other variables or factors outside of this study.

#### Partial Regression Test (t test)

According to Ghozali (2018 pp. 98-99), Partial regression test shows the magnitude of the influence partially independent variables in describing the variation of the dependent variable. If the significance level shows the results of  $t \leq \alpha$  and the value of  $t_{count} > t_{table}$ ,

then the hypothesis can be accepted. The ttable value is known from the statistical table at 5% significance where the degrees of freedom (df) = nk-1 or 282-5-1 = 276 (n is the number of samples and the notation k is the number of variables used). Therefore, based on the statistical table, the ttable value where the significance of 5% is 1.968596. The resulting output is:

**Table 10. Partial Regression Results (t test)**

Variable	Regression Models		
	Random Effects Model		
	Coef.	Q	Probability
(Constant)	1.245498	1.01	0.310
centered_SIZE	0.3277634	1.45	0.147
PB_w	1.872365	0.54	0.589
KM_w	0.2461712	0.08	0.938
AGE	-0.0523488	-1.67	0.094
LEV_w	-1.105101	-0.56	0.575

Notes: Centered\_SIZE: Company Size, PB\_w: Profitability, KM\_w: Managerial Ownership, AGE: Company Age, LEV\_w: Leverage.

Source: STATA V.16 output processed by researchers (2022)

Based on the results of individual parameter significant tests conducted by researchers in table 10, it shows that the company size variable has a tcount of 1.45 and a ttable value of 1.968596. This means that tcount is smaller than ttable which is  $1.45 < 1.968596$  which indicates that this value indicates that company size has no effect on income smoothing. The significance value of the company size variable is 0.147 which means that the significance value is  $> 0.05$ . So it can be interpreted that the variable company size does not have a significant effect on income smoothing carried out by the manufacturing company tested by the researcher. Meanwhile, the firm size coefficient of 0.3277634 has a positive direction in income smoothing. It can be concluded that H1 is rejected.

Furthermore, the profitability variable produces a tcount value of 0.54 and the ttable value is 1.968596. This means that tcount is smaller than ttable i.e.  $0.54 < 1.968596$  which indicates that this value indicates that profitability has no effect on income smoothing. The significance value of the profitability variable is 0.589 which means that the significance value is  $> 0.05$ . So it can be interpreted that the profitability variable does not have a significant effect on income smoothing carried out by the manufacturing companies tested by researchers. While the profitability coefficient of 1.872365 has a positive direction in income smoothing. It can be concluded that H1 is rejected where the firm size variable has no effect on income smoothing. It can be concluded that H2 is rejected.

Managerial ownership generates a tcount value of 0.08 and the ttable value is 1.968596. This means that tcount is smaller than ttable i.e.  $0.08 < 1.968596$  and the significant value of managerial ownership variable is 0.938 which means that the significance value is  $> 0.05$ . So it can be interpreted that the managerial ownership variable cannot significantly influence income smoothing carried out by manufacturing companies that have been tested by researchers. Then the managerial ownership variable coefficient is 0.2461712 with a positive direction on income smoothing. So that H3 is not appropriate or declared rejected.

Firm age and leverage are the control variables in this study. For the company age variable, it produces a tcount value of -1.67 and the ttable value is 1.968596. This means that tcount is smaller than ttable i.e.  $1.67 < 1.968596$  and the significant value of the company age variable is 0.094 which means that the significance value is  $> 0.05$ . This means that the company age variable cannot significantly influence the income smoothing carried out by the manufacturing companies tested by the researchers. However, the variable coefficient of firm

age is -0.0523488 with a negative direction on income smoothing. It can be concluded that the firm age variable has no effect on income smoothing.

The next control variable is leverage which produces a tcount value of -0.56 and the ttable value is 1.968596. This means that tcount is smaller than ttable i.e.  $-0.56 < 1.968596$  and the significance value of the leverage variable is 0.575 which means that the significance value is  $> 0.05$ . So it means that the leverage variable cannot significantly influence the income smoothing carried out by manufacturing companies that have been tested by researchers. Then the leverage variable coefficient is equal to -1.105101 with a negative direction on income smoothing. It can be concluded that leverage has no significant effect on income smoothing.

### **Effect of Company Size on Income Smoothing**

Based on the tests that have been carried out above, company size does not have a significant effect on income smoothing. This is not in line with agency theory where companies with large company sizes do not have a high tendency to carry out income smoothing. The company has considerations in terms of maintaining the company's image by not carrying out income smoothing and disclosing financial statements fairly, because large companies receive more attention and supervision from investors so that if the company does income smoothing it is likely that the government, analysts and investors will know more so this can make the image and ability of the company's managers bad (Santioso et al., 2019). In addition, the bigger the company, the more the company has the ability to predict and bear the risks that will occur by the company so that the company will have a mature strategy to minimize the occurrence of risks so that it will be more careful in making decisions. The total sales itself shows that the bigger the company, the higher the sales value because the company is growing in running its business. However,

The results of this study are in line with the research conducted by Yunengsih et al. (2018) and Sophian & Atalia (2022) which says that the size of the company has no effect on income smoothing. Because large companies will be the center of attention by various parties such as the government and investors, so these companies will be careful in preparing financial reports in accordance with the actual company conditions.

### **Effect of Profitability on Income Smoothing**

Based on the tests that have been carried out above, profitability does not have a significant effect on income smoothing. This is not in accordance with agency theory where agency problems that arise between principals and agents are mainly caused by differences in goals between the two. In this case there is no difference in the goals described by profitability where each individual does not want to fulfill his own desire to prosper himself. The absence of an effect on profitability indicates that the profitability ratio is not one of management's considerations for income smoothing. This study uses operating profit margin as a proxy, which is a comparison of operating profit with net sales. Operating profit margin provides an overview of the pure profit obtained from sales that occur (Fauzan & Sari, 2018). The higher the level of operating profit margin does not really have an impact on the higher fluctuations in the company's ability to earn profits, this is because companies that have reported profits are in accordance with actual conditions, so companies choose not to do income smoothing.

In addition, the insignificant level of the operating profit margin is probably due to the operating profit margin, which is a comparison of operating profit where the operating profit itself cannot be used as a reflection of how successful the company is in obtaining the company's net profit, because there are other components that affect net income, for example other income, namely profit on the difference in transaction value, profit on the sale of investments, interest income and other income. Therefore, the magnitude of the value of the operating profit margin cannot be said that the profit to be generated will be large or vice versa, seen from other income

factors it also earns quite a large amount and can have the nature of adding or subtracting according to the existing value.

The results of this study are in line with research Sophian & Atalia (2022) who said that Companies with low profitability have a tendency to carry out income smoothing because the size of the profitability obtained is not a guarantee for managers to take policies that present the company's condition in good health and avoid reporting fluctuating profits or vice versa.

### **Effect of Managerial Ownership on Income Smoothing**

Based on the results of the tests that have been carried out above, managerial ownership does not have a positive and significant effect on income smoothing. Managerial ownership is the amount of shares owned by management who are also shareholders of the company. Shares owned by managers can balance the interests of shareholders and management, because the benefits of decisions made by management are immediately felt, and management bears the risk if a loss occurs due to an incorrect decision. This is not in line with agency theory whereby share ownership by management will reduce agency costs. Agency costs themselves arise due to agency problems that occur between the principal and the agent (Jensen & Meckling, 1976). The higher the percentage of managerial ownership in a company, the company managers who participate as shareholders can reduce agency problems between shareholders and managers which can equate the desires of managers and shareholders, so that information is likely to be conveyed objectively by managers to shareholders. Although management participates in decision making because of the shares it owns, the small number of shares it owns does not really affect the decision making regarding the company.

The results of this study are in line with research Utami et al. (2020) And Sugiari et al. (2022) that said that rose The decrease in managerial ownership of the company does not motivate management to carry out income smoothing and managers who own shares and share ownership in the company can reduce the actions of managers to carry out income smoothing.

## **5. Conclusion**

From the results of the discussion above, it can be concluded that variable firm size, profitability, and managerial ownership have no effect on *income smoothing*. It can be concluded that large companies receive more attention and supervision from investors so that if these companies carry out income smoothing, it is likely that the government, analysts, and investors will detect it more easily, so this can create a bad image and the ability of these managers. It can also be concluded that profitability has no effect on income smoothing indicating that profitability ratios are not one of management's considerations for income smoothing. And it can be concluded Where management has an average minority shareholding when compared to public or institutional shareholdings although management participates in decision-making because of the shares it owns, the small number of shares it owns does not really affect the voting decisions about the company.

Limitations of this research namely the limitations of the research sample caused by the large number of companies that experienced losses and did not publish financial reports and annual reports in 2019-2021 so that this directly affected this research sample.

Suggestions for further research it is suggested to use other variables that might influence income smoothing such as institutional ownership, bonus plans, auditor reputation, and income tax. To improve research results, researchers can add intervening variables or moderating variables, such as audit quality and stock prices. It is also hoped that future research should use an income smoothing index other than Eckel's (1981) index, such as the modified Jones model. Then, for companies it is hoped that this research can be used to increase awareness of opportunities for income smoothing actions that may occur within the company.

And for investors, it is hoped that the results of this research can be used as a consideration in making decisions.

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