

Effect of Deferred Tax Expense, Current Tax Expense, Accrual Basis, and Audit Quality on Earnings Management

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Abstract

This study aims to analyse the impact of deferred expense, current tax expense, accrual basis, and audit quality on earnings management. The object of this research is a manufacturing company listed on the IDX for period of 2019-2021. Purposive sampling was employed in the research sample selection method to collect data from up to 30 manufacturing companies. The binary logistic regression test with SPSS assistance was used to examine the hypotheses. The examination of the data reveals that the management of company earnings is significantly impacted by deferred expense, current tax expense, accrual basis, and audit quality.

Keywords: Deferred Expense, Current Tax Expense, Accrual Basis, Audit Quality, Earnings Management.

1. INTRODUCTION

It is quite intriguing to examine the financial statements of Indonesian companies. The primary information source for the organization, which is crucial for both internal and external parties, includes financial statements. Accounting records are used to evaluate a company's performance [1]. Financial statements are used by both internal and external stakeholders when making choices. Information about profit is one of the things a company's financial statements include. High profits, which result in sales, profit, and cash flow, show that the business is performing well [2]. The income statement gives details on the company's performance indicators, which are shown as profit or loss. In order for management to benefit from what has been implemented, profit is tied to the distribution of dividends to the company's shareholders.

Earnings management is a deliberate intervention in the external financial reporting process with the intention of obtaining some personal gain [3]. The term "earnings management" is used to characterize management who is thought to have altered the financial statistics of the firm for certain purposes. By introducing bias in financial statements, earnings management can decrease the credibility of a company's financial statements [4].

Large corporations frequently employ earnings management techniques to increase profits for the business or the management. In order to conduct profits management operations in the organization, managers will attempt to take advantage of numerous chances that exist in various activities or occurrences. In order to affect the outcomes of various choices, many managers take use of the possibility to manipulate profit statistics in businesses through accrual engineering [5].

Several factors that influence management affect earnings management including deferred tax expense, deferred tax assets, and free cash flow [6]. Sutadipraja stated that the factors that affect earnings management are current tax expense, deferred tax expense, and deferred tax assets [7]. Deferred tax expense and accrual basis have a significant effect on earnings management [1]. Deferred tax expenses are expenses that exist as a result of temporary differences between accounting profit and fiscal profit.

Companies in Indonesia generate financial reports for implementation based on PSAK and Tax Regulations. Due to disparities between how PSAK operates and the applicable tax legislation, corporations are required under existing tax regulations to make

fiscal repairs. If there is a discrepancy between commercial and fiscal profit, management's decision-making during the accrual process can be informed [8].

The amount of income tax that must be paid on taxable income for a time period is known as current tax cost. According to prior studies, the accrual basis can have an impact on earnings management in addition to deferred tax expenditure and current tax expense. In the sense that revenue is recognized when it is received and costs are recognized when they are due, the accrual basis is a way of assessing income and expenses. It is thought that accrual-based accounting methods can result in financial statements that are more trustworthy [1].

The caliber of the audits performed has an impact on earnings management in addition to taxes. Investor trust is anticipated to rise as a result of improved financial reporting due to better audit quality [9]. Auditors that are qualified will be able to identify client earnings management actions. The size of the KAP performing the audit serves as a proxy for the quality of audits performed by public accountants. Compared to other KAPs, the financial statements audited by major four large KAPs are regarded as reliable. Large KAPs are superior than smaller KAPs in terms of expertise, technical experience, capability, and reputation [10].

The researcher is interested in researching the impact of deferred expense, current tax expense, accrual basis, and audit quality on earnings management in manufacturing businesses listed on the IDX for the period of 2019–2021 based on the explanation of the existing concerns. The year 2022 was chosen as the range's middle point since it contains the most recent financial statement data sources.

Manufacturing businesses employ a lot of fixed assets, such as inventory, as a source of accruals, which enables earnings management in a manufacturing business [1]. Manufacturing firms are more appealing to investors than other types of businesses, thus the researcher was also motivated to select one for this study. As a result, the company must actively promote the publication of its financial statements to keep investors confident.

2. Methods

This study uses a quantitative approach with the type of *expost facto* research. *Expost facto* is a type of research in which all data are obtained after all the problem events take place [11]. The aims of this study is to investigate the impact of deferred expense, current tax expense, accrual basis, and audit quality on earnings management using manufacturing businesses listed on the IDX as the subject and object of research for the 2019–2021 period as the subject and object of study.

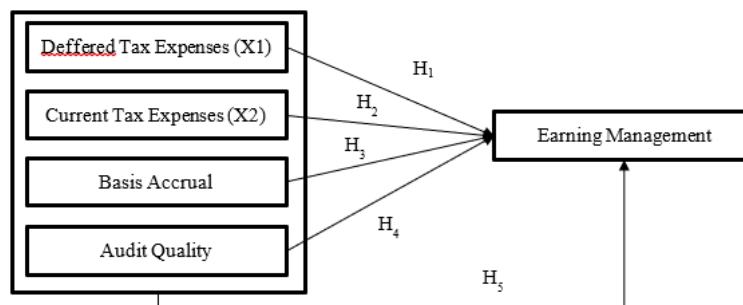


Figure 1. Research Framework

The sampling technique used is purposive sampling. This technique will take samples based on certain criteria. The criteria for determining the companies used as samples for this study can be seen in Table 1.

Table 1. Research Sample Selection Procedure

No	Criteria	Amount
1	Manufacturing company listed on IDX 2019-2021	201
2	Manufacturing company has been registered on IDX before 2019	166
3	Financial reporting company is published in full 2019-2021	151
4	The issuance of financial statements has been audited by independent auditors as of desember 31 from 2019-2021	148
5	Financial statements have all information related to research variable	30
Research Sample		30
Years		3
Data		90

Source: Data Processed by the Author

Secondary data is obtained through intermediaries which are generally in the form of published or unpublished historical records, documents or reports. The data collected in this study are in the form of complete annual financial reports of manufacturing companies listed on the IDX mainly in 2019-2021 and obtained through the IDX Capital Market Reference Center and related website pages that provide data on public financial statements, namely [www.idx.co .id](http://www.idx.co.id).

Data collecting techniques, such as library research and documentation pertaining to the research variables raised, were employed to gather the data. Binary logistic regression (binary logistic regression) is used to analyze the data and test the study's hypothesis. SPSS is used to help combine metric and non-metric statistical programs for the independent variables.

The dependent variable for the study includes the earnings management variable. If a company is included in the category of small profit enterprises, earnings management will be assigned a value of 1, and if it is not, it will be assigned a value of 0. According to Amanda's study, the criteria in this classification state that small profit enterprises fall into the category of small loss firms if their company's revenue is between zero and six dollars [12]. When categorizing data for the audit quality variable, if the audit was conducted by a KPA that is one of the "big four," it is given a value of 1, and if not, it is given a value of 0.

Utilizing binary logistic regression analysis, this hypothesis is tested on research data (binary logistic regression). Assessment of model fit, Hosmer & Lameshows Goodnes chi-square test, Cox & Snell R Square and Nagelkerke coefficients, classification tables, Wald Statistic Test, and parameter estimates are things that need to be taken into account in the analysis utilizing this test. The SPSS program was used for the analysis of the research data.

3. Results and Discussion

3.1 Data Analysis Results

The test was carried out with a significance level of 0.05. In this study, the amount of data processed was 90. Research data obtained from manufacturing companies listed on the IDX in accordance with research provisions.

3.1.1 Testing of Model Fit and Overall Model Fit

This data analysis is carried out by comparing the value of -2 Log Likelihood on Block Number = 0 with -2 Log Likelihood on Block Number = 1. The hypothesis to determine the model fit is H0 which states that the hypothesized model fits the data.

Table 2. Value -2 Initial Likelihood Log

Iteration History^{a,b,c}			
		-2 Log	Coefficients
Iteration		likelihood	Constant
Step 0	1	118.292	-.533
	2	118.288	-.547
	3	118.288	-.547

a. Constant is included in the model.

b. Initial -2 Log Likelihood: 118,288

c. Estimation terminated at iteration number 3 because parameter estimates changed by less than ,001.

Table 3. Rating -2 Log Likelihood Final

Iteration History^{a,b,c,d}							
		-2 Log	Coefficients				
		likelih	Cons				
Iteration		ood	tant	X1	X2	X3	X4
Step	1	96.674	-.682	5.095	3.628	5.482	-.843
1	2	94.693	-.771	8.003	4.913	7.111	-1.185
	3	94.608	-.788	8.826	5.274	7.447	-1.267
	4	94.607	-.789	8.871	5.294	7.460	-1.271
	5	94.607	-.789	8.871	5.294	7.460	-1.271

a. Method: Enter

b. Constant is included in the model.

c. Initial -2 Log Likelihood: 118,288

d. Estimation terminated at iteration number 5 because parameter estimates changed by less than ,001

Based on the results of the analysis, the value of -2 Log Likelihood is 118,292 which can be seen in Iteration History on Block Number 0 and the results of the calculation of the value of -2 Log Likelihood setp 1 show a value of 96,674 which can be seen in Iteration History on Block Number 1. These results prove that there is a decrease in the value of -2 Log Likelihood which means that the second regression model is better and H0 is accepted or the hypothesized model fits the data.

3.1.2 Coefficient of Determination Test (Nagelkerke's R2)

The Nagelkerke R2 value is used to measure how far the model's ability to explain the variation of the independent variables. The following is the result of testing the coefficient of determination.

Table 4. Coefficient Determination

Model Summary			
Step	-2 Log	Cox & Snell R	Nagelkerke R
	likelihood	Square	Square
1	94.607 ^a	.231	.316

a. Estimation terminated at iteration number 5 because parameter estimates changed by less than ,001

Based on the results of the analysis, it can be seen that the value of Nagelkerke R2 is 0.316. These results indicate that the four research variables can only explain the earnings management variable by 31.6%. The remaining 68.4% is explained by other variables not tested in this study.

3.1.3 Chi Square Hosmer and Lemeshow Test

The test was carried out in order to test the feasibility of the regression model. If the value of Hosmer and Lemeshow's statistic is more than 0.05, the model is able to predict the value of the observation [13]. The results of the feasibility of the regression model can be seen as follows.

Table 5 Regression Model Feasibility Test

<i>Hosmer and Lemeshow Test</i>			
Step	Chi-square	df	Sig.
1	8.309	8	.404

Table 5 shows a significance value of 0.404. These results indicate that the significance value is greater than 0.05 which means that the model can be accepted because it matches the observation data. In other words, the model is able to predict the value of the observations so that the model can be used for further data analysis.

3.1.4 Classification Table Testing

This test was conducted to evaluate the precision of the observed categorization predictions, which were shown using a table of the dependent variable's anticipated values. The dependent variable's actual observation value is displayed in the row. The categorization table test's findings are listed in table 6.

Table 6. Classification Table Test

Classification Table^a					
Observed		Predicted		Percentage Correct	
		No Earnings Management	Earnings Management Happens		
Step 1	Profit management	No Earnings Management	13	20	39.4
		Earnings Management Happens	6	51	89.5
Overall Percentage					71.1

a. The cut value is .500

Based on the table, it can be seen that the strength of the regression model in predicting the possibility of a company doing earnings management is 89.5%. The company indicated that it did not carry out earnings management was 39.4%. The total percentage of the overall strength of the regression model is 71.1%. Thus, these results prove that the variables of deferred expense, current tax expense, accrual basis, audit quality can be used in predicting a company's earnings management.

3.1.5 Simultaneous Significance Test

The Chi Square model's omnibus test of model coefficients examines all the independent factors that are concurrently influencing the dependent variable in this study. The outcomes of the simultaneous significance test are as follows.

Table 7. Simultaneous Significance Test

Omnibus Tests of Model Coefficients		Chi-square	df	Sig.
Step 1	Step	23.681	4	.000
	Block	23.681	4	.000
	Model	23.681	4	.000

Table 7 can be seen that the significance value of 0.000 is less than 0.05 and the Chi Square value of 23,681 is greater than the Chi Square Table of 9.49. This result indicates that H5 is accepted. In other words, deferred expense, current tax expense, accrual basis, and audit quality have a simultaneous effect on earnings management.

3.1.6 Parameter Estimation and Interpretation

The test is run to determine the extent to which the independent variable partially influences the dependent variable. The variables in the equation table are examined to determine the test outcomes.

Table 8. Parameter Estimation

Variables in the Equation		B	S.E.	Wald	df	Sig.
Step	X1	-8.871	3.766	5.550	1	.018
1 ^a	X2	-5.294	2.694	3.862	1	.049
	X3	-7.460	3.561	4.388	1	.036
	X4	1.271	.530	5.752	1	.016
	Constant	.789	.376	4.391	1	.036

a. Variable(s) entered on step 1: X1, X2, X3, X4.

Table 8 shows the results of data analysis with the acquisition of the regression coefficient value of the deferred expense variable -8.871 with a p-value of 0.018 <0.05, the measured deferred expense variable has an effect on earnings management. The regression coefficient of the current tax expense variable is -5.294 with a p-value of 0.049 <0.05, so the current tax expense variable has an effect on earnings management. The coefficient of the accrual basis variable is -7.460 with a p-value of 0.036 <0.05, so the accrual basis variable has an influence on earnings management. The regression coefficient of the X4 variable is 1.271 with a p-value of 0.016 <0.05, so the audit quality variable has an effect on earnings management.

The form of the regression equation used in this study is as follows.

$$\ln \frac{ML}{1-ML} = 0,789 - 8,871BT - 5,294BPK - 7,460BA + 1,271KA$$

Description

$\ln \frac{ML}{1-ML}$ = Logaritma natural probabilitas manajemen laba

BT = Deferred Load

BPK = Current Tax Burden

BA = Accrual Base

KA = Audit Quality

3.2 Discussion

Deferred Tax expenses have an influence on earnings management in manufacturing companies in the 2019-2021 span according to the results of this study. This is in accordance with previous research which states that deferred tax expense has an effect on earnings management of food and beverage manufacturing companies 2012-2014 [14]. Supported by other research which states that deferred tax expense affects earnings management [15].

This occurs as a result of the business delaying its taxes to lower stated earnings. One of three hypotheses pertaining to positive accounting theory, the Political Cost Hypothesis as a justification for tax savings, states that businesses have a propensity to save or postpone taxes in order to minimize reported earnings [16]. This can be done by delaying income and accelerating costs to save taxes, one of which is by engineering deferred tax expense related to accruals so as to enable management to manage earnings [14].

Earnings management is influenced by the current tax burden in this study. This is in line with Nabil's research which states that the current tax burden has a significant effect on earnings management in consumer goods manufacturing companies listed on the IDX [17]. Earnings management is influenced by the current tax burden in this study. This is in line with Nabil's research which states that the current tax burden has a significant effect on earnings management in consumer goods manufacturing companies listed on the IDX [18]. In his research, it can be seen that a small current tax burden on a company listed on the IDX does not necessarily indicate that the company is doing earnings management.

The accrual basis has an influence on earnings management as evidenced by the results of research that has been done. This is in line with Purnawan's research which states that the accrual basis variable affects the earnings management of companies listed on the IDX [1]. The accrual basis must be used to generate a financial report in order to meet the goals. The role of accruals, which is used to manage earnings and offer a better indication in the financial statements, has the drawback that it may be used to manipulate the financial statements' numbers in order to avoid disclosing losses to manufacturing businesses on the IDX.

Audit quality is able to have a significant effect on earnings management. This is in line with research which states that audit quality has a significant influence on earnings management of non-financial service companies [11]. Financial report audits conducted by classy auditors from large-scale Public Accounting Firms such as Bigfour are expected to reduce earnings management actions.

4. Conclusions

Based on the results of the analysis that have been described regarding manufacturing companies listed on the IDX with a time span of 2019-2021, it can be concluded that (1) Deferred Tax expenses have a significant effect on earnings management, (2) Current tax expenses have a significant effect on earnings management, (3) The accrual basis has a significant effect on earnings management, and (4) deferred expense, current tax expense, accrual basis, and audit quality have a significant effect on earnings management simultaneously.

5. Other recommendations

The author would like to thank the company and participants who have helped in completing this research well. Suggestions that can be given to future researchers are to identify theoretical reviews to help refine research by creating research gaps.

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