

EFFECT OF PROFIT MANAGEMENT ON ANNUAL REPORT READABILITY

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ABSTRACT: *The purpose of this study is to examine the effect of earnings management on the readability of annual reports by using data from the non-financial sector of companies listed on the Indonesia Stock Exchange (IDX) for the period (2014-2018). Total observations were 825, using data collection techniques using purposive sampling and data analysis using multiple regression analysis methods. The results show that the increase in income reflects earnings management which has a negative effect on the readability of annual reports, while the results of the second and third hypotheses are an increase in income and discretionary accruals and an increase in income and discretionary accruals above the median, both of which simultaneously reflect earnings management which has no significant effect on the readability of the annual report*

Keywords: *earnings management, annual report readability, discretionary accruals*

ABSTRAK: Tujuan penelitian ini untuk menguji pengaruh manajemen laba terhadap keterbacaan laporan tahunan dengan menggunakan data sektor non-keuangan perusahaan yang terdaftar di Bursa Efek Indonesia (BEI) periode (2014-2018). Total observasi yaitu 825, dengan menggunakan teknik pengumpulan data menggunakan *purposive sampling* dan analisis data memakai metode analisis regresi berganda. Hasil penelitian menunjukkan bahwa peningkatan pendapatan mencerminkan manajemen laba yang berpengaruh negatif terhadap keterbacaan laporan tahunan, sedangkan hasil hipotesis kedua dan ketiga yaitu peningkatan pendapatan dan *discretionary accruals* serta peningkatan pendapatan dan *discretionary accruals* di atas median, keduanya secara bersamaan mencerminkan manajemen laba yang tidak berpengaruh secara signifikan terhadap keterbacaan laporan tahunan.

Kata Kunci: manajemen laba, keterbacaan laporan tahunan, *discretionary accruals*

Preliminary

The importance of information in the annual report for all parties, resulted in the preparation of financial statements having reporting standards. The Indonesia Stock Exchange (IDX) requires all listed companies to publish an annual report for the purpose of making it available to users of the annual report. in accordance with the Financial Services Authority Regulation number 29/POJK.04/2016 Annual Report of Issuers or Public Companies article 1 point 1, the annual

report is a form of accountability for corporate governance to shareholders and stakeholders. This standard can be found in a Circular (SE) Financial Services Authority (OJK) number 30/SEOJK.04/2016 part 3 number 1 point a, where each annual report must contain management analysis and discussion. The annual report that is designed, not only contains issues according to standards, but also understood by the reader. This is necessary so that report users can make decisions based on the news received,

especially for shareholders/investors. The decisions taken will also affect the future of a company (Miller, 2010; You and Zhang, 2009).

The focus of this research is to measure the level of readability of the annual report through the ease of reading. This study uses the Gunning Fog Index as one of the ways and crucial aspects to measure the understanding of descriptive text in the company's annual report. This measurement is not based on the length of a paragraph disclosed by management, but according to the complexity of the paragraph (Lo et al, 2016). The readability of the report is part of the consideration of management responsibilities, namely the Board of Directors and the Board of Commissioners using the aim of maintaining a better level of quality of financial reports. therefore, it contributes to the company's success and helps shareholders avoid losses due to misinformation (Pivac, Vuko, and Cular, 2017).

Management as the party running the company, of course, will try to exceed the revenue in the previous year using the goal so that the company's performance is permanently viewed by stakeholders. Lundholm et al (2014) found that strategically management manipulated the readability of the annual report through the analysis and management discussion section. in the process of exceeding the target, it is possible for management to carry out earnings management in order to achieve or exceed the target. from Lo et al (2016), companies that achieve or exceed targets should provide news that is practically understandable compared to using companies that do not reach the target. however, the commonality of profit management can exist and cause an asymmetry of issues for readers.

Lo et al (2016) citing Li (2008) and Bloomfield (2008) stated that there are two crucial things related to readability and financial performance to achieve the target. The first is obfuscation, in which managers try to cover up bad news for failing to achieve targets, by conveying news that is difficult for readers to understand. The second is ontology,

namely the existence of bad news which essentially has a nature that is more difficult to communicate to readers. For this reason, the readability of the report as part of the information can be used as a benchmark for the origin of the company's condition, which is reflected in the level of complexity of the disclosure analysis and management discussion. the increasing complexity, then the possibility of earnings management in the company.

Hypotheses Development

Signaling Theory

The signal theory that Spence presented to *Job Market Signaling* in 1973 stated that in the labor market there is information asymmetry. According to Walker (1995), asymmetric information is the difference in information that comes from company policies to stakeholders related to economic activities. Information asymmetry can be described as a lack of appropriate information influenced by company performance so that stakeholders obtain incomplete information (Bergh et al, 2018). In addition, there are several conditions that can form asymmetry, namely private, hidden, different, and lack of perfect information that exists from uncertainty and failure of management observations, structural barriers that prevent information seekers from accessing, and barriers to providing information by taking into account these issues. as an advantage for the company. Frequency theory shows the reasons why companies convey information to the market and describes that between company management and various stakeholders there is information asymmetry. This theory states how the frequency should be given by the company to users of financial statements (Morris, 1987). Signaling theory assumes that the accuracy of information known to company managers is better, which is inversely proportional to rumors known by investors or outsiders. This is what causes news asymmetry between interested parties (Bergh et al, 2018). This theory states how the frequency should be given by the company to users of financial statements (Morris, 1987). Signaling theory assumes that the accuracy of information known to company managers is better, which is inversely proportional to rumors known by investors or

outsiders. This is what causes news asymmetry between interested parties (Bergh et al, 2018). This theory states how the frequency should be given by the company to users of financial statements (Morris, 1987). Signaling theory assumes that the accuracy of information known to company managers is better, which is inversely proportional to rumors known by investors or outsiders. This is what causes news asymmetry between interested parties (Bergh et al, 2018).

Annual Report Readability

Readability in financial context disclosures is defined as the ability of investors and analysts to assimilate the evaluation of the relevance of news to disclosures; Good readability is an effective communication in presenting relevant news valuations, especially for users of annual reports (Loughran and McDonaldm, 2011). According to Pivac, Vuko and Cular (2017), management needs to consider readability to maintain the quality of its annual report so that the quality of the information in the report can contribute significantly to the company's success. Zhou et al. (2017) stated that the Gunning Fog Index has a similar calculation method using the Flesch Reading Ease where there is a division into two variables, namely sentence length and the number of syllables per word. in calculating the Gunning Fog Index, terms that consist of 3 or more syllables are the best indicators for terms that are claimed to be difficult. Readability values now vary when calculated using software, not manually. In addition, there should be no difference between the use of a software readability calculation tool using equations and only a slight difference between equations (Zhou et al, 2017),

Earnings Management

Earnings management is an action that is intentionally carried out by management using financial accounting standards as the basis for directing profit reporting at the affected level and to achieve specific goals. There are several patterns that can be claimed by earnings management groups (Scott, 2012) namely taking a bath, income minimization, income maximization, and income smoothing. Taking a Bath to charge costs and recognize future losses in the current period and write off some assets so as to form a low profit for the previous year, but will reduce costs in future periods and will

increase revenue for the next period more than it should be. Income Minimization is to reduce the profit for this period of time from the net income that the company should earn. This is usually done when the company earns very high income to reduce the tax burden. Income Maximization to increase profits in the current period as a result exceeds what it should be and is usually done to get more bonuses, increase profitability numbers, and protect the company from breach of contract against long-term debt. Income Smoothing to generate profits looks consistent from period to period. Management deliberately reduces or enlarges the profit number for a certain period to make it look continuous and stable to attract investors or to get long-term contracts. In general, investors or parties who have an interest in the company prefer companies that have fairly stable profits.

The Effect of Earnings Management on the Readability of Annual Reports

Earnings management is a process that is intentionally carried out by management using financial accounting standards as the basis for directing earnings reporting at a specified level and to achieve specific goals (Scott, 2012). Based on Lo et al (2016), there are two crucial things regarding the correlation between readability and company financial performance in order to achieve the target. The first is obfuscation, where managers have the discretion and choice of trying to cover up bad news by extending the annual report in complex terms and long sentences. The second thing is that ontology is an alternative explanation where losses and ad interim revenues are more difficult to describe than profits or profits so that bad information is more difficult to communicate to annual report readers.

According to Spence (1973), gossip asymmetry between company management and cooperating parties can be shown by the signals the company gives to users of annual reports. Management is responsible for the preparation of the annual report, so they can choose the information that is shared with users of the annual report. The information will then be used as a rationale for users of the annual report to make decisions, so that what is conveyed must be relevant, thorough, and complete so that report users do not make wrong decisions. Users need to understand and understand what is conveyed in the report, this refers to the readability of the

report. To be used in decision making, management must produce annual reports using a high level of readability, so that they are easy to understand and understand. Relevant information contained in an annual report is very influential on the decision making of investors and shareholders. High readability also reduces gossip asymmetry between investors and users of other annual reports (Ajina, Sourour, and Badreddine, 2018).

One of the things that affect annual report readability is earnings management. According to previous research, earnings management causes a low level of annual report readability. This is because companies that manage profits tend to make complex financial reports with the aim of covering earnings management practices carried out by outside parties (Lo et al, 2016). The preparation of complex annual reports will also reduce the ability of users to understand and understand what is written in it, thereby reducing the ability of investors to make accurate decisions. Ideally, the annual report should have a high level of readability because it can help investors predict profits to assess the company's future performance and make decisions for appropriate system or policy changes.

This research uses *Gunning Fog Index* to measure the level of readability of the analysis and management discussion section of the annual report, it becomes a place for management to provide information regarding the overall business condition, financial condition, and operating results in the audited financial statements and other sections of the annual report. Lundholm et al (2014) found that management manipulates annual report readability through the analysis and management discussion section strategically. In addition, according to Lo et al (2016) companies with a sufficiently large motivation to manipulate profits have a more complex part of the analysis and management discussion.

Companies whose income reaches or exceeds the set standards are claimed to manage profits to be able to achieve standards by taking into account accounting policies (Lo

et al, 2016), and the limitations of non-transparent earnings management. In this case, the standard is set, which is in accordance with the company's performance last year with at least no change in earnings (zero change in earnings) as a result of increasing revenue, earnings management arises which makes the report more difficult to read using a high FOG standard. Therefore, based on the theory and research that has been carried out previously, this study reaches the position that earnings management has a negative effect on the readability of annual reports.

This study uses three models to test the three hypotheses given. In each model, different proxies are used to indicate the occurrence of profit management.

The first hypothesis uses profit management proxied by Meet or Beat Earnings (MBE) as an indicator of earnings changes. If there is a positive change in income compared to the previous period, then the company is indicated to practice profit management.

Hypothesis 1

"Increased earnings signal earnings management which makes the annual report difficult to understand."

In the second hypothesis, using MBE which is linked using discretionary accruals (DA). If the company has a positive change in income compared to the previous period accompanied by a positive DA, then the company is indicated to be doing earnings management. Thus, companies that meet both conditions will make annual reports more difficult to read.

Hypothesis 2

"Rising earnings and discretionary accruals, together indicate earnings management, which makes the annual report difficult to understand."

In the third hypothesis, using MBE which is linked using DA which is above the median value, the obtained DA is from all sample companies. If the company has a positive change in income compared to the previous period accompanied by a DA that is more than the median value, then the company is indicated to be doing earnings management.

Thus, companies that meet both of these requirements will make annual reports more difficult to read.

Hypothesis 3

“Rising earnings and discretionary accruals above the median, simultaneously indicate earnings management, which makes the annual report difficult to understand”

Research Methods

This study uses a population of non-profit sector companies financelisted on the IDX in 2014-2018. The sample criteria include being included in the main categories in the listing boards listed on the IDX in 2014-2018; companies that publish data complete annual report for 2014-2018; companies whose financial statements end on December

31 in order to avoid the effect of partial time in the measurement of variables. companies that issue financial statements expressed in Rupiah. It focuses on sample selection without the influence of exchange rates; and companywhose annual report data can be detected by the legibility calculation program.

Model 1:

$$\text{Read}(t) = +_1\text{MBE}(tt-1) +_2\text{ECN}(tt-1) +_3\text{FS}(t) +_4\text{NB}(t) + e$$

Model 2:

$$\text{Read}(t) = +_1\text{EM_EMP}(t) +_2\text{EMP}(t) +_3\text{EMN}(t) +_4\text{ECN}(tt-1) +_5\text{FS}(t) +_6\text{NB}(t) + e$$

Model 3:

$$\text{Read}(t) = +_1\text{EM_EMHP}(t) +_2\text{EMP}(t) +_3\text{EMLP}(t) +_4\text{EMN}(tt-1) +_5\text{ECN}(tt-1) +_6\text{FS}(t) +_7\text{NB}(t) + e$$

Table 1:Determination of the Number of Samples

Information	Amount
Non-financial sector companies listed on the IDX during 2014-2018	536
Companies registered after 2014	(210)
Companies with incomplete annual report data for the 2014-2018 period	(101)
Companies that use one language in their annual reports	(19)
Companies whose annual reports do not read the Gunning Fog Index calculation program	(28)
Companies that use currencies other than Rupiah	(13)
Total companies sampled	165
Total observations (165 companies x 5 years)	825

Source: Data processed

Dependent Variable

The dependent variableusedin this study is the annual report readability. Readability in this studyhitung uses the Gunning Fog Index developed by Robert Gunning (1952) to measure readability.The

number of words per sentence is calculated by dividing the number of words by the number of sentences in the analysis and management discussion section. Word complexity is measured by the three or more syllables each word has. The readability value received can be interpreted as below

Table 2:Annual Report Readability Standard

FOG value	Information
FOG 18	Unreadable
FOG 14 - 18	Hard to read
FOG 12 - 14	Ideal
FOG 10 - 12	Acceptable

Independent Variable

The independent variable applied in this study is earnings management by applying several different proxies to calculate earnings management according to Lo et al (2016), which is described under.

1. Proxy on First Model: MBE (Meet or Beat Earnings)

Earnings management with MBE proxy where $MBE = 1$ if the current year's EPS and the previous year's EPS are more than equal to zero ($MBE = 0$). MBE is a strategy used by companies with low incomes, to be able to maintain relationships with investors through an easier-to-understand explanation of the annual report (Bloomfield, 2008).

2. Proxy on the Second Model: MBE*EMP (Positive Earnings Management)

Earnings management is measured by MBE and companies that have discretionary accruals positive (EMP). The discretionary accruals formula used in this study belongs to Kothari et al. (2005), namely $TA_{it} = 0 / ASSETS_{it-1} + 1 \Delta SALES_{it} + 2PPE_{it} + 3ROA_{it-1} + uit$, where TA_{it} is the total accruals, $SALES_{it}$ is the change in sales revenue divided by total assets ($ASSETS_{it-1}$), PPE_{it} as net property, plant, and equipment which is also divided by total assets ($ASSETS_{it-1}$), and ROA_{it-1} as return on assets of the previous period. According to Kothari et al. (2005), assets as the denominator aim to reduce heteroscedasticity, as well as the use of ROA as a form of control over the company's performance so that the calculation of TA can be more controlled. The Discretionary Accruals (DA) model has a large number of errors in the calculation (Dechow et al., 1995) so this study adds to the interaction with MBE as a proxy in the second calculation in order to increase the detection of companies that manage earnings, because DA and MBE act as processes and earnings management results. The EMP variable indicator (DA) is also used to identify companies that are positive for earnings management by determining the existence of

EMP if the value of discretionary accruals is more than equal to zero ($DA = 0$).

3. Proxy on the Third Model: MBE*EMHP (Highly Positive Earnings Management)

Earnings management is measured by MBE and companies with positive discretionary accruals which is above the median of all company. The calculation of discretionary accruals is the same as the second model and uses the median value because the high and low values will not be mixed so that it better describes the high and low values.

Control Variable

In this study, several control variables were used, namely:

1. *Negative Earning Changes* (ECN) if MBE is less than zero ($MBE < 0$);

2. EMN (Negative Earnings Management) where $MBE * EMN$ is obtained from the value of discretionary accruals which is smaller than zero ($DA < 0$). This proxy is a combination of MBE and EMN, where this proxy will be worth one if MBE has a value of one and EMN has a value of one;

3. $MBE * EMLP$ (Low Positive Earnings Management) where EMLP is obtained if discretionary accruals have a value greater than zero ($DA = 0$) and are below the median value;

4. *size* company as measured by the multiplication of the stock price by the number of shares *circulating*, then use the natural logarithm to make the firm size data more normally distributed; and *quantity segmentation* Business is obtained from the number of segments in the company that meet the requirements

Results And Discussion

Descriptive statistics

Variables used include readability of financial statements as proxied by readability as the dependent variable and earnings management as an independent variable which is divided into three tests with different proxies, namely Meet or Beat (MBE),

MBE*EMP (*Positive Earnings Management*), and MBE*EMHP (*High Positive Earnings Management*), as well as control variables consisting of: Negative Earning Changes (NEC), Positive Earnings Management (EMP), MBE*EMN (*Negative Earnings*

Management), MBE*Low Positive Earnings Management (EMLP), company size (*size*) and number of business segments (NBSeg) as control variables.

Table 3: Descriptive statistics

	N	Min.	Max.	Average	Std. Deviation
<i>Readability</i>	825	8.1	21.8	14.64	2.28
MBE	825	0.00	1.00	0.53	0.49
ECN	825	0.00	1.00	0.44	0.49
EMP	825	0.00	1.00	0.93	0.25
MBE*EMP	825	0.00	1.00	0.50	0.50
MBE*EMN	825	0.00	1.00	0.01	0.12
MBE*EMHP	825	0.00	1.00	0.29	0.45
MBE*EMLP	825	0.00	1.00	0.21	0.41
<i>Size</i>	825	14.58	25,10	19.47	1.95
NBSeg	825	0.00	2.1	0.92	0.56

Source: Data processed

According to the table above, readability has an average of 14.64 which means that most of the samples used have annual reports, especially the analysis and management discussion sections which are difficult to read with the highest score of 21.8 and the lowest of 8.1 . Readability has a standard deviation of 2.28 which is the maximum increase from the average variable meaning 2.28 and the maximum decrease of minus 2.28 or the average deviation of the readability variable is 2.28.

The first hypothesis shows that the independent variable of earnings management is proxied using MBE, where MBE is an element of the independent variable that is converted into a dummy variable using the number 1 if the EPS Delta is more than 0; the opposite is given the number 0 if it does not meet the criteria. With an average of 0.53 and a standard deviation of 0.49, which means the maximum increase in the average variable is 0.49 and the maximum decrease is minus 0.49. ECN means control variable for MBE, which uses a dummy variable with number 1, if Delta EPS is less than 0; otherwise, it is 0, using an

average of 0.44 and a standard deviation of 0.49, which means the maximum increase from the average variable is 0.49 and the maximum decrease is minus 0.49.

The second hypothesis shows that the independent variable of earnings management is proxied using MBE*EMP. EMP is a control variable that is converted as a dummy variable to be the basis for calculating MBE*EMP using category = 1 If Discretionary Accruals (DA) is more than equal use 0; otherwise 0 which indicates the existence of profit management, with an average of 0.93 and a standard deviation of 0.25 which means that the maximum increase comes from the homogeneous variables of 0.25 and the maximum decrease is minus 0.25. MBE*EMP is an independent variable that applies a dummy variable using the number 1, if simultaneously MBE = 1 and EMP = 1; otherwise, if one of them is not met, then 0, using a homogeneous average of 0.50 and a standard deviation of 0.45, which means the maximum increase is positive 0, 45 and a maximum decrease of -0.45. MBE*EMN becomes the control variable using a dummy

variable using category = 1, if simultaneously MBE = 1 and EMP = 0; on the other hand, if one of them is not met, 0, using an average of 0.01 and a standard deviation of 0.12, which means the maximum increase in homogeneous average is 0.12 and the maximum decrease is minus 0.12.

In the third hypothesis, the independent variable of earnings management is proxied using MBE*EMHP. MBE*EMHP means that the independent variable that is converted as a dummy variable uses category = 1, if simultaneously MBE = 1 and EMHP = 1 which indicates that the management of DA time profit is more equal to the median value of the sample; vice versa. If one of them is not met, 0, using an average of 0.29 and a standard deviation of 0.45 which means the maximum increase in homogeneous average is 0.45 and the maximum decrease is minus 0.45. MBE*EMN became the control variable using a dummy variable with a category = 1, if simultaneously MBE = 1 and EMHP = 0 which indicates an increase in income

accompanied by earnings management below the middle value; otherwise if one of them is not met, 0, with an average of 0,

Hypothesis test

Based on table 4, it can be observed that the coefficient of determination (Adjusted R2) of 0.03 or 3.3% indicates that the independent variable, namely MBE can explain the dependent variable, namely the readability of the annual report as much as 3.3% and the remaining 96.7% is explained by the variable others not included in this study. According to the F statistical test, it can be seen that the MBE independent variable has a significant simultaneous effect on Read, which is a significance of $0.00 < 0.05$, it can be concluded that the research is feasible and relevant as a result, the model chosen has a significant effect on the dependent variable and other variables are worth mentioning. dependent variable.

Table 4: Results of Hypothesis Testing 1

Read(t) = +₁MBE(tt-1) +₂ECN(tt-1) +₃FS(t) +₄NB(t) + e			
<i>Variables</i>	<i>Sign</i>	<i>Coef.</i>	<i>(p-value)</i>
Dependent variable: <i>Read</i>			
Independent variable:			
MBE (H1)	+	0.41	0.00**
Control variable:			
ECN	+	0.37	0.00**
<i>Size</i>	+	0.14	0.00**
NBSeg	-	-0.07	0.01*
N = 825		*Significant at p-value < 0.05	
F = 7.93		**Significant at p-value < 0.01	
SigF = 0.00			
<i>Adjusted R Square</i> = 0.03			

Source: Data processed

MBE has a p value of 0.00 on the independent variable, so it can be said that it has a significant effect on the readability of the annual report, and has a positive coefficient value of 0.41 which means that each independent variable is in sync with the proposed hypothesis, namely companies that have zero or zero income changes. a slightly positive will have a readability that is difficult to read, or in this case a high FOG value. According to the results of the individual parameter significance test or the t statistical

test, it can be concluded that all independent variables have a significant effect on the readability of the annual report and compared to companies that do not have zero or slightly positive earnings changes, companies that have zero or slightly positive earnings changes have a negative effect on the readability of the annual report. This is caused by the p value < 0.05, and the direction of the coefficient is in accordance with the hypothesis that was determined at the beginning, so it can be stated that H1 is accepted.

Table 5: Results of Hypothesis Testing 2

Read(t) = +₁EM_EMP(t) +₂EMP(t) +₃EMN(t) +₄ECN(tt-1) +₅FS(t) +₆NB(t) + e			
Variable	Directi on	Beta Coefficient	(p-value)
Dependent variable: <i>Read</i>			
Independent variable:			
MBE*EMP (H2)	+	0.14	0.06
Control variable:			
EMP (EMP)	+	0.06	0.05
MBE*EMN (EMN)	+	0.06	0.07
ECN	+	0.11	0.11
<i>Size</i>	+	0.14	0.00**
NBSeg	-	-0.08	0.009*
N = 825		*Significant at p-value < 0.05	
F = 4.96		**Significant at p-value < 0.01	
SigF = 0.00			
<i>Adjusted R Square</i> = 0.02			

Source: Data processed

According to table 5, it can be seen that the coefficient of determination, namely the readability of the annual report is only 2.8%, while the rest is explained outside the variables of 97.2%. In the F test, it can be seen that the independent variable MBE*EMP has a significant simultaneous effect on Read, which is a significance of 0.00 < 0.05, it can be concluded that the research is feasible and relevant as a result the selected sample has a significant effect on the dependent variable and other variables. properly disclose the dependent variable.

In table 5 it can be observed that the independent variable MBE*EMP has a p value of 0.06 which is the independent variable that has no significant effect on the readability of the annual report. According to table five, it can be seen that each of these independent variables has a positive coefficient value of 0.14 (MBE*EMP), which means that the independent variable is appropriate or in the same direction using the second hypothesis proposed, namely companies that have zero or slightly positive income changes and discretionary accruals with additional income

will have legibility that is difficult to read, or in this case have a high FOG value. because of that, According to the results of the individual parameter significance test or t statistical test, it can be concluded that the independent variable has no significant effect on the readability of the annual report and cannot state that compared to companies that do not have zero or slightly positive income changes,

companies that have zero or slightly positive income changes have a positive effect. negative on the readability of the annual report. According to this, it can be stated that H2 is rejected because it has no significant effect even though it has a coefficient value that is in line with the prediction.

Table 6: Results of Hypothesis Testing 3

$Read(t) = +_1EM_EMHP(t) +_2EMP(t) +_3EMLP(t) +_4EMN(tt-1) +_5ECN(tt-1) +_6FS(t) +_7NB(t) + e$			
Variable	Direc tion	Beta Coefficient	(p-value)
Dependent variable: <i>Read</i>			
Independent variable: MBE*EMHP (H3)			
	+	0.09	0.15
Control variable:			
EMP			
MBE*EMLP	+	0.06	0.05
MBE*EMN	+	0.17	0.02*
ECN	+	0.01	0.39
<i>Size</i>	+	0.11	0.12
NBSeg	+	0.14	0.00**
	-	-0.09	0.00**
N = 825		*Significant at p-value < 0.05	
F = 4.93		**Significant at p-value < 0.01	
SigF = 0.00			
<i>Adjusted R Square</i> = 0.032			

Source: Data processed

Based on table 6, it can be seen that the coefficient of determination of 0.03 or 3% indicates that the independent variable, namely MBE*EMHP, can mention the dependent variable, namely the readability of the annual report as much as 3% and the remaining 97% is explained by other variables not included in this study. In the F test, it can be seen that the independent variable MBE*EMHP has a significant effect on readability, namely the significance of $0.00 < 0.05$, it can be concluded that the research is feasible and relevant so that the selected sample has a significant effect on the dependent variable and other variables properly explain dependent variable.

Table 6 can be seen that the independent variable MBE*EMHP has a p value of 0.15, which means that the independent variable has no significant effect on the readability of the annual report. Based on the table above, it can be observed that the independent variable has a positive coefficient value, namely 0.09 (MBE*EMHP), which means that the independent variable is synchronous or in the same direction using the proposed 2nd hypothesis, namely companies that have zero or slightly positive income changes and discretionary High income accruals will have legibility that is difficult to read, or in this case have a high FOG value. Based on the individual parameter significance

test or t statistical test, it can be concluded that the independent variable has no significant effect on the readability of the annual report. Only companies with zero or slightly positive earnings changes and discretionary accruals that slightly increase revenue have a negative effect on the readability of the annual report. Based on this, it can be stated that H3 is rejected because it has no significant effect even though it has a beta value in the same direction.

Hypothesis Discussion

According to the first hypothesis, it can be identified that companies that have positive earnings changes have the possibility to carry out profit management. Therefore, it can be concluded that the first hypothesis (H1) is accepted. The results show that companies that do earnings management when compared to companies that don't do earnings management have annual reports with a low level of readability or are difficult to read because of the high level of complexity. In conclusion, the use of complex explanations is used to make the annual report difficult to understand, this is probably due to the existence of profit management practices that the company tries to cover up.

In the second hypothesis, the coefficient is in line with the direction of the hypothesis, as a result, companies that have a positive increase in income and discretionary accruals, together have a tendency to carry out earnings management. However, the independent variable has no significant effect on the dependent variable, as a result it can be concluded that the second hypothesis (H2) is rejected. The results show that companies that do earnings management, when compared to companies that do not do earnings management, have no effect on annual report readability. Discretionary accruals are not perfect to explain the effect of earnings management on annual report readability, because there are several samples of companies that have the same positive discretionary accruals but have low complexity. Then in disclosing the results of the company's performance in the annual

report, especially the analysis and management discussion section, the company can disclose the business conditions, financial conditions, and operations that will occur in the financial statements. In addition, it could also be due to the combination of MBE and discretionary accruals which did not affect the readability of the annual report. These three things may cause the hypothesis to be rejected. It could also be due to the combination of MBE and discretionary accruals which did not affect the readability of the annual report. These three things may cause the hypothesis to be rejected. It could also be due to the combination of MBE and discretionary accruals which did not affect the readability of the annual report. These three things may cause the hypothesis to be rejected.

In the third model, companies that experience an increase in positive earnings and discretionary accruals above the median, simultaneously have the same ability to carry out earnings management because they use the hypothetical direction. But the independent variable has no significant effect on the dependent variable, so it can be concluded that the third hypothesis (H3) is rejected. The results prove that companies that carry out earnings management using a high amount of revenue increase do not have an impact on the readability of the annual report. These results support the explanation for the rejection of the second hypothesis by showing that the use of discretionary accruals above the median value is not appropriate to explain the impact of earnings management on the readability of annual reports. Because there is a sample of companies that have positive discretionary accruals above the median value, but tend to have low complexity. In conclusion, discretionary accruals cannot be linked using the readability of annual reports, but can only reflect earnings management.

Conclusion

The purpose of this study is to examine the effect of earnings management on the readability of annual reports by taking

samples from companies listed on the IDX, especially the non-financial sector. The results of the study indicate that earnings management affects the readability of annual reports in companies that have increased revenues. When there is an increase in income due to earnings management, the company will find it difficult to explain the annual report, so that the annual report becomes difficult to understand. For further research, the legibility of financial statements can be considered by using two languages, namely Indonesian and English. Thus, it can be identified whether grammar affects the readability of the annual report.

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