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**The Moderating Role of Corporate Governance in the Relationship between
Executive Compensation and Earnings Management in Indonesia: Evidence from
Jones and Kothari Models**

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Abstract. This study examines the relationship between accrual-based earnings management and executive compensation in Indonesian listed companies and assesses whether corporate governance moderates that relationship. The analysis covers the 2022-2024 period and uses 207 firm-year observations from 69 companies with complete financial, compensation, and governance disclosures. Earnings management is proxied by discretionary accruals estimated using the Jones model and is later re-tested with the Kothari model for robustness. Corporate governance is measured through a 32-item index derived from Indonesian good corporate governance guidelines. Ordinary least squares regression is employed with firm size, leverage, and return on assets as control variables. The findings indicate that discretionary accruals are not consistently associated with higher executive compensation across specifications. Firm size and return on assets are the most stable determinants of compensation. Moderation and split-sample tests suggest that governance quality shapes the compensation-reporting relationship, although the strength of the evidence is sensitive to the earnings-management proxy used. Overall, the study highlights the importance of stronger governance and more transparent compensation design in reducing reporting risk.

Keywords: executive compensation, earnings management, corporate governance, Indonesia, discretionary accruals

1. Introduction

The Fraud Risk Management (FRM) Survey conducted in 2022 revealed that only 54% of companies in Indonesia have ever conducted a Fraud Risk Assessment (IIA et al., 2023). These findings suggest that the level of preparedness for fraud risk controls and the quality of oversight processes remain uneven, making financial reporting distortions a significant concern in corporate practices in Indonesia. In financial accounting, earnings management is understood as the use of managerial judgment in reporting to influence reported profit figures, which may deviate from underlying economic performance (Bui, 2024). This view has gained significant traction because earnings management can occur through accrual choices or the manipulation of actual activities that impact a company's cash flows and operations (Habib et al., 2022). In the reality of the Indonesian capital market, profit figures influence perceptions of performance and risk, meaning that earnings management has the potential to reduce the quality of information for investors, creditors, and stakeholders. This is particularly true as pressure to meet performance targets increases during the recovery period and business strategy adjustments in Indonesia following the COVID-19 pandemic from 2022 to 2024.

This issue relates to agency theory, which explains that the separation of ownership and control creates conflicts of interest and information asymmetry, thereby providing executives with opportunities to act opportunistically if oversight mechanisms are not sufficiently effective (Tekin & Polat, 2020). In relation to agency theory, incentives serve as a tool to align interests; however, misaligned incentives can encourage reporting behavior that does not fully reflect the company's performance (Nienhaus, 2022).

One incentive closely linked to corporate performance is executive compensation. (Tahir et al., 2019) indicates that profit-based bonus structures create accounting incentives related to accrual-based reporting decisions. Upon closer examination, the more executive incentives are sensitive to reported results or firm value, the greater the tendency for earnings manipulation, whether through increased accruals or improper reporting, (Harris et al., 2019) . Thus, total executive compensation, which reflects remuneration and performance-based rewards, can be positioned as a driving factor that needs to be examined in relation to earnings management in Indonesian companies.

(Nguyen et al., 2024) in their study revealed that earnings management is not only determined by incentives but also by the strength of corporate oversight. *Corporate governance* is defined as a set of mechanisms that influence managerial decisions regarding ownership and control, thereby functioning to curb opportunistic behavior and enhance the credibility of financial reporting . Empirical evidence indicates that board and audit committee characteristics are negatively associated with accrual levels, thereby supporting the supervisory role in curbing earnings management (Almarayeh et al., 2022) . These findings provide a strong basis for the view that the impact of executive compensation on earnings management should be understood in conjunction with the quality of *corporate governance*, as strong *corporate governance* can increase the detection costs and reputational costs of manipulation (Hidayat et al., 2022) .

Nevertheless, many studies are inconsistent, as *corporate governance* is a complex aspect; thus, overly narrow measurements risk failing to capture the actual variations in governance practices (Bansal, 2024) . Many studies measure *corporate governance* using one or two structural proxies, such as the proportion of independent directors, board size, or the existence of an audit committee, resulting in the process dimensions—including ethics, compliance, and disclosure quality—being underrepresented. This situation may explain why some studies find weak or inconsistent effects, even though certain theories and micro-evidence suggest that oversight mechanisms play a crucial role (Fitrasari, 2023) . Therefore, *corporate governance* measurement must employ multiple indicators to ensure stable and comprehensive measurement (Nguyen et al., 2024) .

Corporate governance is measured using 32 indicators derived from Indonesia's general guidelines on good *corporate governance*, which emphasize the principles of transparency, accountability, responsibility, independence, as well as fairness and equality (KNKG, 2021) . With this approach, *corporate governance* is not treated merely as a structural attribute but as a governance practice that can be observed through the disclosure of corporate body policies, control processes, and commitment to compliance, making it more suitable for explaining variations in the quality of oversight in companies, particularly in developing countries (Hong et al., 2023) such as Indonesia.

Corporate governance can serve as a mechanism to reduce unmonitored discretion, thereby lowering the likelihood of earnings management even when compensation is high (Hong et al., 2023) . Furthermore, the quality of *corporate governance* also has the potential to determine how strongly compensation incentives impact earnings management, as strong governance enhances monitoring effectiveness, whereas weak governance allows incentives to more easily turn into manipulative practices. This conditional argument positions *corporate governance* as the key to explaining the discrepancies in previous research findings, which often assume that the relationship between incentives and earnings management is uniform across firms.

The use of *Return on Assets (ROA)*, *Leverage*, and *Firm Size* is crucial, as all three are closely related to incentives and opportunities for earnings management. *Leverage* can increase pressure to meet debt covenants and encourage accrual manipulation, particularly as covenants approach breach. (Butt et al., 2016) . Meanwhile, *ROA* reflects performance that is often correlated with discretionary accruals, making performance control essential to ensure earnings management inferences are not biased by performance (Collins et al., 2017) and *Firm size* is related to public scrutiny, operational complexity, and the capacity of control systems, which can influence the opportunities and costs of engaging in earnings management while potentially correlating with compensation structures and governance practices (Nguyen et al., 2024) .

The period from 2022 to 2024 in Indonesia is a relevant time to assess the dynamics of incentives and oversight as companies navigate performance pressures and stakeholder expectations during a phase of recovery and strategic adjustment. By examining total executive compensation against earnings management and treating *corporate governance* as both an explanatory factor and a moderating condition for the strength of this relationship, this study is expected to provide a more nuanced empirical contribution compared to studies that merely treat governance as a single proxy or a mere control variable. The use of a 32-indicator index also addresses the literature's call for more valid and reliable measurements of *corporate governance*, given the complexity of the governance construct.

This study contributes to companies in designing compensation packages and strengthening governance to align with the goal of improving the quality of financial reporting and reducing the scope for earnings management that undermines market credibility; academically, it strengthens the understanding of how compensation-based incentives relate to reporting choices and how governance mechanisms curb opportunistic behavior as predicted by agency theory.

2. Theory and Hypothesis Development

Executive compensation is fundamentally designed to align the interests of shareholders and executives by linking rewards to reported performance (Tekin & Polat, 2020). When performance information is asymmetric and shareholders do not fully observe executive actions, executives have room to influence the performance that serves as the basis for evaluation. In agency theory, performance-based compensation structures can create incentives for executives to improve the value of the indicators targeted by compensation (Loyola & Portilla, 2020). (in their study revealed that weaknesses in oversight can increase the likelihood of executives maximizing their personal utility through reporting that does not fully reflect the company's actual conditions). Thus, compensation incentives can drive opportunistic reporting behavior when the personal benefits of achieving targets outweigh the costs incurred (Nienhaus, 2022).

Accounting policy choices are viewed as rational responses to the contracts and incentives faced by executives. On the other hand, since executive compensation is tied to accounting profits, executives choose methods and estimates that increase current-period profits or at least shift profits between periods to serve contractual interests (Bansal, 2024). This pattern arises because accounting profit is often used as an easily observable performance variable, making it the primary target of discretionary actions. (Tahir et al., 2019) found in their study that bonuses may be associated with accrual decisions that shift profits between periods in accordance with target ranges and contractual limits. These results are consistent with the view that accounting is not merely a reporting tool but also a contractual instrument that generates economic consequences for executives (Loyola & Portilla, 2020).

Accruals provide flexibility in revenue recognition, provisions, and asset valuation without altering the cash flow of that year (Greusard, 2022). Discretionary accruals are a commonly used measure to capture reporting distortions based on accounting choices. When compensation is tied to earnings, the incentive to manage these discretionary components becomes stronger because even small changes in estimates can impact the achievement of targets. Thus, there is a rational link between executive compensation and the use of discretionary accruals as a means of adjusting reported earnings.

(Harris et al., 2019) found that higher executive incentives are correlated with lower earnings quality or higher levels of *discretionary accruals*, although the direction and strength of the relationship may depend on the institutional context. Furthermore, other findings reveal that executives tend to increase the use of accounting discretion and *misreporting* practices (Nienhaus, 2022) and executive incentives may reinforce the tendency to engage in accrual-based earnings management. This accumulating evidence suggests that executive compensation may be linked to increased discretionary accruals as a strategy to meet performance targets that affect remuneration.

H1 Discretionary earnings management accruals are positively associated with executive compensation.

Corporate governance mechanisms act as a monitoring system that limits managerial discretion and reduces the risk of opportunistic behavior in reporting. When the oversight functions of the board and committees operate effectively, managers' scope to adjust accounting estimates tends to narrow as the probability of detection also increases. In agency theory, strong oversight reduces monitoring costs for shareholders and increases the expected costs of manipulative behavior for managers. Consequently, compensation incentives do not always lead to earnings management in all companies but depend on the strength of internal control mechanisms (Tekin & Polat, 2020) . Thus, strong governance can alter reporting behavior by reducing opportunities and diminishing the net benefits of earnings manipulation (Assenso-Okofu et al., 2021) .

Empirical evidence suggests that the quality of oversight is often associated with a reduction in the level of earnings management (Nguyen et al., 2024) . More independent and active audit committees are associated with a reduction in abnormal accruals because the review of financial statements and interactions with auditors become more effective (Almarayeh et al., 2022) . A higher proportion of independent directors is also frequently associated with better reporting quality, as independence enhances objectivity in evaluating accounting policies and challenges managerial decisions (Awais Amin & Cumming, 2023) . Governance failures correlate with increased risks of misstatement and fraud, which conceptually fall on the same spectrum as *opportunistic earnings management* practices. This pattern implies that strong governance can act as a primary barrier against the use of discretionary accruals for personal gain.

Strong governance is also linked to the quality of compensation design and setting processes, for example through board independence in establishing remuneration policies and restrictions on rent-extraction practices (Harymawan et al., 2020) . Weak governance can make compensation more likely to reflect managerial power rather than performance, thereby increasing incentives to present seemingly good accounting performance through earnings management. Conversely, good governance tends to promote contracts more aligned with long-term performance and establishes stricter evaluation mechanisms, thereby reducing the benefits of short-term profit manipulation. In a positive accounting approach, changes in contract structure and the enforcement of monitoring alter the cost-benefit trade-off of discretionary accounting choices (Shi et al., 2021) .

If executive compensation increases the incentive to meet profit targets, then strong governance mechanisms should weaken the transmission of that incentive into earnings management practices because oversight increases the probability of correction and reputational costs (Assenso-Okofu et al., 2021) . In firms with weak governance, high or increasingly performance-based compensation is more likely to be correlated with discretionary accruals due to low monitoring and unchecked reporting discretion (Assenso-Okofu et al., 2021) . The relationship between incentives and earnings manipulation becomes more pronounced when the oversight environment is weak, whereas the quality of governance and auditor oversight can mitigate opportunistic reporting behavior. This logic explains why previous research findings may vary, as differences in governance quality can make the relationship between compensation and earnings management nonhomogeneous across firms (Loyola & Portilla, 2020) . Therefore, testing the interaction between compensation and governance quality is crucial to capturing conditions where executive incentives lead to earnings management.

H2 The relationship between executive compensation and earnings management is weaker for firms with strong corporate governance mechanisms and stronger for firms with weak corporate governance mechanisms.

3. Research Methods

3.1 Data Selection

Our analysis uses companies listed on the Indonesia Stock Exchange (IDX) with annual accounting and compensation data covering the period from 2022 to 2024. This population was selected because public companies have relatively uniform reporting obligations, enabling comparisons across companies and across years. The 2022–2024 period was chosen to capture the most current and relevant conditions regarding the dynamics of executive compensation incentives and profit reporting practices. Data was obtained from financial statements, annual reports, and supporting documents published by companies through information disclosure channels and their official websites.

The sample was selected using *purposive sampling* by establishing criteria aligned with the measurement needs of the research variables. Among these criteria are that companies must consistently publish financial statements and annual reports for every year in the 2022–2024 period without any missing years, and specifically, companies must provide the information needed to calculate all research variables.

Companies that did not consistently provide this data were excluded from the sample.

Of the total 1,007 company observations during the 2022–2024 period from all companies listed on the Indonesia Stock Exchange, only 69 companies had complete and consistent data for all research variables. When information is unavailable or inconsistent, variable measurements become biased and reduce the validity of empirical inferences. This condition aligns with the argument that accounting research heavily relies on data transparency to minimize *measurement error* and enhance the comparability of results . Lack of transparency can also signal higher agency risk and weak monitoring mechanisms, particularly when relevant compensation and governance information is not adequately disclosed (Caban-Garcia et al., 2020) .

3.2 Measurement of Good Corporate Governance

Good corporate governance is viewed as a crucial foundation in a market-based economy. This concept is closely linked to the level of trust stakeholders place in both the companies that implement it and the quality of a country's business environment (KNKG, 2021) . The quality of *good corporate governance* implementation can be evaluated through an index-based measurement approach, namely the good corporate governance index (Nguyen et al., 2024) . To be applicable in the Indonesian context, the development of the *Good Corporate Governance* Index was conducted by aligning the indicators with the elements of *good corporate governance* practices as outlined in the General Guidelines on Good Corporate Governance (KNKG, 2021) , which include board composition, the audit committee, the remuneration committee, shareholder rights, financial and audit matters, and disclosure.

The *Good Corporate Governance* Index is subsequently utilized as a proxy to assess how well a company implements the principles of *good corporate governance* (Owusu & Weir, 2016) . This index comprises 32 indicators of *good corporate governance* implementation that have been adapted to align with the General Guidelines on Good Corporate Governance (KNKG, 2021) . These thirty-two items were derived from information available in the companies' annual reports. Each item was assigned a score of 1 if the company disclosed it and a score of 0 if there was no disclosure. The company's index score was obtained by summing all items, with a maximum score of 32 indicating full compliance or 100 percent adherence to the guidelines used. The indicators used in the index are listed in the appendix.

3.3 Measurement of Executive Compensation

The primary independent variable in this study is total executive compensation, treated as a form of short-term compensation because it reflects the rewards received by executives within a single reporting period, as explained by (Bushman, 2021) . The focus on short-term compensation is relevant because incentive contracts linked to current-period performance can encourage managers to be more responsive to profit reporting targets (Nienhaus, 2022) . In line with the contractual perspective in agency theory, performance-based compensation schemes can create incentives for managers to maximize their utility through specific

accounting choices (Nienhaus, 2022) . Therefore, total executive compensation is used to capture the intensity of incentives embedded in compensation contracts that may influence reporting behavior.

In the design phase, this study aimed to measure compensation by separating it into three components—total compensation, bonuses, and fixed compensation—to distinguish variable incentives from more routine components, as is commonly done in compensation studies (M. Costa et al., 2023) . However, not all companies in Indonesia present details of bonuses and fixed compensation separately, so only total compensation is consistently available across the entire sample. The limitation of companies in Indonesia in disclosing executive compensation separately between bonuses and fixed compensation indicates that remuneration transparency remains relatively low and may reduce the accountability of the compensation committee and diminish the pressure to design incentive schemes that encourage long-term performance (Siwendu & Ambe, 2024) .

3.4 Measurement of earnings management

The use of accrual-based earnings management measures was chosen in this study to distinguish between the two main forms of earnings management: real-activity-based and accrual-based. In the accrual approach, managers can leverage the flexibility of accounting standards to determine accounting figures through accrual discretion (Habib et al., 2022) . The *discretionary accruals* measure was selected because of its broad applicability for detecting accrual-based earnings management in *firm-year* data, including in studies related to executive incentives (M. Costa et al., 2023) . The measurement was conducted using the *Jones Model*, developed by Jones with modifications also used in the study (C. M. Costa & Soares, 2022) . All components were obtained from the annual financial statements of public companies in Indonesia for the years 2022–2024.

In measuring discretionary accruals, the first step is to calculate total accruals by subtracting net income from operating cash flow.

$$TAC = NI_{it} - CFO_{it}$$

After obtaining the value of Total Accruals (TAC), it is then estimated using the Ordinary Least Squares (OLS) regression equation as shown below.

$$\frac{TA_{it}}{A_{it-1}} = \beta_1 \left(\frac{1}{A_{it-1}} \right) + \beta_2 \left(\frac{\Delta Rev_{it}}{A_{it-1}} \right) + \beta_3 \left(\frac{PPE_{it}}{A_{it-1}} \right) + \varepsilon \quad (1)$$

After obtaining the regression coefficients from the previous equation, nondiscretionary accruals (NDA) are calculated using the following equation:

$$NDA_{it} = \beta_1 \left(\frac{1}{A_{it-1}} \right) + \beta_2 \left(\frac{\Delta Rev_{it} - \Delta Rec_{it}}{A_{it-1}} \right) + \beta_3 \left(\frac{PPE_{it}}{A_{it-1}} \right) \quad (2)$$

The final step is to calculate discretionary accruals (DA) using the formula

$$DA_{it} = \frac{TA_{it}}{A_{it-1}} - NDA_{it} \quad (3)$$

Notes:

TAC = Total accrual

NI	= Net income for year t
CFO	= Cash flow from operations (cash flow from operating activities) in year t
Ait-1	= Total assets in period t-1
ΔREVit	= Change in revenue between year (t-1) and year t
PPEit	= Gross Property, Plant, and Equipment for year t
ΔRECit	= Change in net accounts receivable between year (t-1) and year t
DAit	= Discretionary accruals in period
t NDA	= Non-discretionary accruals β1,
β2, β3	= regression coefficients

3.5 Control variables

This study uses control variables to minimize an excessively large *error term*, which is consistent with research related to compensation and management. (Yan-jun & Yan-xin, 2017) state in their research that the control variables in question are firm size, leverage, and return on assets (ROA).

3.6 The Model

In the model, this study employs several models to test the hypotheses. These models include a distinction between companies with strong *corporate governance* (SGOV), companies with weak *corporate governance* (WGOV), and a combined analysis of the entire sample. Companies with *corporate governance* scores above the average are classified as strong, while those below the average are classified as weak (Assenso-Okofu et al., 2021).

The use of the natural logarithm on total compensation is an implication of data with very high variability, ensuring a normal distribution and addressing the issue of heteroscedasticity (Lee, 2020).

$$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{CGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$$

$$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{SGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$$

$$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{WGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$$

(4)

(5)

(6)

This study uses *corporate governance* as a moderating variable in the relationship between earnings management and executive compensation to examine the non-constant effect of earnings management on executive compensation (Assenso-Okofu et al., 2021)

Table 1. Operational Definitions of Variables

Variable	Operational definition
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LnTCE	Total Executive Compensation measured in rupiah and using the natural logarithm for company <i>i</i> in year <i>t</i>
DACC	Discretionary accrual calculated using Equation 3 for firm <i>i</i> in year <i>t</i>
CGOV	<i>Corporate Governance</i> measured using 32 indicators. The indicators are
	listed in the appendix for company <i>i</i> in year <i>t</i>
SIZE	Company size calculated using the natural logarithm of total assets for company <i>i</i> in year <i>t</i>
LEV	Leverage measured as long-term debt divided by total assets of firm <i>i</i> in year <i>t</i>
ROA	Return on assets, measured by the ratio of earnings after interest and taxes to total assets of company <i>i</i> in year <i>t</i>

4. Results and Discussion

4.1 Descriptive Statistics

Descriptive statistics are used to provide a general overview of the characteristics of the research data, including both the direction of the data's tendency and the variation in data across each variable. Descriptive statistics are crucial for understanding data distribution patterns, identifying indications of extreme observations or outliers (), and assessing the shape of the distribution through skewness and kurtosis values prior to conducting panel data regression model testing.

The Total Executive Compensation (TCE) variable shows significant variation across companies, even after applying the natural logarithm. In the total sample, the mean value of Total Executive Compensation is 51,629,350,000 with a median of 28,779,000,000, while the maximum value reaches 453,074,000,000. The significant difference between the mean and the median, coupled with a high skewness of 3.22 and a high kurtosis of 13.53, indicates a non-symmetrical distribution with a heavy right tail. A small number of companies have very high executive compensation compared to the majority of other companies. This finding arises because executive compensation is often influenced by company size, operational complexity, and differing incentive structures across firms.

On the other hand, discretionary accruals—used as a proxy for earnings management—exhibit a generally negative mean across the entire sample. The minimum and maximum values indicate a fairly wide range, with positive skewness and high kurtosis. Conceptually, a skewed and fat-tailed DACC distribution often occurs because earnings management practices are not evenly distributed: most companies report relatively normally, but a small group engages in more aggressive actions, resulting in extreme DACC values. Therefore, these statistics provide a methodological basis for the use of robust standard errors and/or transparent outlier handling when necessary (Iacobucci et al., 2025) .

Table 2. Descriptive Statistics for Equation 4

Source: data processed by the author, 2026

$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{CGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$								
Variable	N	Mean	Median	Std. Dev.	Min	Max	Skewness	Kurtosis
TCE	207	51,629,350,000	28,779,000,000	68,484,680,000	1,100,000	453,074,000,000	3.22	13.53
DACC	207	-0.0293	-0.0308	0.0802	-0.2280	0.5040	2.30	12.60
CGOV	207	20.9	21.0	3.75	14.0	26.0	-0.191	-1.37
SIZE	207	30.5	30.7	1.18	27.5	33.3	-0.120	-0.332
LEV	207	0.163	0.130	0.139	0.000250	0.604	0.845	0.000876
ROA	207	0.000598	0.000463	0.000815	-0.00116	0.00557	2.70	13.30

Table 3. Descriptive Statistics for Equation 5

$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{SGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$								
Variable	N	Mean	Median	Std. Dev.	Min	Max	Skewness	Kurtosis
TCE	124	30,009,070,000	18,268,380,000	32,886,900,000	1,100,000	206,383,800,000	2.22	6.61
DACC	124	-0.0299	-0.0296	0.0630	-0.1440	0.3390	1.63	8.57
CGOV	124	23.6	24.0	1.93	20.0	26.0	-0.533	-0.893
SIZE	124	30.4	30.5	1.16	27.5	33.3	-0.0864	-0.498
LEV	124	0.157	0.121	0.128	0.000757	0.541	1.04	0.619

ROA	124	0.000546	0.000428	0.000718	-0.00116	0.00557	1.04	19.20
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Source: data processed by the author, 2026

Table 4. Descriptive Statistics for Equation 6

$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{WGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$								
Variable	N	Mean	Median	Std. Dev.	Min	Max	Skewness	Kurtosis
TCE	83	83,929,510,000	60,428,030,000	91,637,180,000	1,062,500,000	453,074,000,000	2.27	5.75

DACC	83	-0.0285	-0.0374	0.1010	-0.2280	0.5040	2.33	10.40
CGOV	83	16.9	17.0	1.53	14.0	19.0	-0.00124	-1.33
SIZE	83	30.7	30.8	1.20	27.6	33.3	-0.194	-0.0233
LEV	83	0.171	0.143	0.155	0.000250	0.604	0.626	0.565
ROA	83	0.000676	0.000522	0.000940	0.000250	0.00557	2.29	9.02

Source: data processed by the author, 2026

The *Corporate Governance* (CGOV) variable represents the weight of corporate governance, measured using 32 indicators based on *good corporate governance* guidelines. The descriptive statistics table shows that the distinction between companies with strong governance (SGOV) and weak governance (WGOV) is consistent in the data. In the SGOV sample, the average CGOV is around 23.6 with a median of 24 and a range of 20–26, while in the WGOV sub-sample, the average CGOV is approximately 16.9 with a median of 17 and a range of 14 to 19.

This governance difference is significant because strong governance is generally associated with more effective oversight mechanisms, greater transparency, and constraints on opportunistic management behavior (Nguyen et al., 2024). Conversely, weak governance can create greater room for uncontrolled decisions, both in setting compensation packages and in financial reporting decisions. Therefore, distinguishing between strong and weak governance provides a context for analyzing whether the relationship between earnings management (DACC) and executive compensation (TCE) differs under different governance conditions.

A notable difference is evident in the Total Executive Compensation (TCE) variable in the SGOV and WGOV samples. In the SGOV sample, the average TCE was 30,009,070,000 with a median of 18,268,380,000, whereas in the WGOV sample, the average TCE increased to 83,929,510,000 with a median of 60,428,030,000. These findings indicate that companies with weak governance in the sample tend to have higher executive compensation.

The firm size (SIZE) variable tends to be stable and has a relatively symmetrical distribution compared to TCE and DACC. The mean and median values of SIZE across the entire sample are around 30–31 with a standard deviation of approximately 1.1–1.2, as well as low skewness. This stability of SIZE is reasonable because the logarithmic transformation reduces the effect of extreme asset values. Academically, SIZE is important as a control variable because firm size is correlated with the ability to pay compensation, operational complexity, and the level of public exposure, all of which can influence financial reporting behavior.

The Leverage (LEV) and Return on Assets (ROA) variables exhibit sharper variations. LEV averages around 0.15–0.17 with positive skewness, indicating that some companies have high leverage, though the majority operate at lower leverage levels. From a positive accounting perspective (*debt covenant hypothesis*), high leverage can create incentives to manage earnings to meet debt covenants or maintain creditor perceptions. ROA also exhibits an asymmetric distribution and high kurtosis, indicating the presence of companies with profitability levels significantly different from others. Since profitability is often directly linked to performance-based compensation, ROA plays a crucial role in controlling for bias when testing the relationship between DACC and TCE.

4.2 Correlation Matrix

The hypothesis described in the Theory and Hypothesis Development section suggests that earnings management calculated using the Jones approach is positively associated with total executive compensation. However, as shown in Table 5, earnings management has a negative relationship with total compensation and is not significant at the 5% level.

The Jones approach to measuring earnings management has limitations in deeply distinguishing between normal and discretionary accruals (Sun, 2021). The discretionary accrual measure using the Jones approach often contains high measurement error, causing coefficients to be inconsistent and tend to be weak, thereby increasing the p-value.

The use of a control variable in the form of firm performance (SIZE) weakens the effect of earnings management on executive compensation, as earnings management moves in tandem with firm performance (Suk Yoon et al., 2022). The *Corporate Governance* variable is also not significant at the 5% level with a negative direction; this finding indicates that the influence of *Corporate Governance* on compensation is often indirect (Al Farooque et al., 2019).

The firm size variable has a dominant influence on executive compensation; however, the firm size variable cannot be omitted because doing so would introduce bias into the significant effect, as its influence is captured by other variables, and firm size serves as a control variable.

Table 5. Regression Results for Executive Compensation and Earnings Management

$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 \text{SIZE}_{it} + \beta_4 \text{LEV}_{it} + \beta_5 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$			
	Estimate	P-Value	VIF
Intercept	9.725e+00	0.00945 **	
DACC	-5.085e-17	0.08227	1.411578
CGOV	-1.291e-01	0.10795	1.100475
SIZE	5.482e-01	8.33e-07 ***	1.113971
LEV	-3.761e-01	0.63881	1.143267
ROA	2.693e+02	0.06686	1.380012
N	207		
Multiple R-squared	35.7		
F-statistic	8.579		

Significance Codes	0.01 ‘***’ 0.05 ‘**’ 0.1 ‘*’
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Source: data processed by the author, 2026

Notes: The table above is the result of the final robustness check to ensure the results are consistent.

To determine whether the firm size variable (SIZE) has a significant influence on the model, a model test was conducted without using the firm size variable (SIZE).

Table 6 shows that *corporate governance* has a significant and negative effect, thus proving the second hypothesis: the weaker *the corporate governance*, the higher the total executive compensation. On the other hand, the main variable in this study, namely earnings management (DACC), remains insignificant and also causes the Multiple R-Squared to decrease, from 35.7% to 11.7%. These findings validate that the firm size variable has a significant influence, but it is un , as it fails to resolve the main issue and instead lowers the Multiple R-Squared.

Table 6. Regression Results for Executive Compensation and Earnings Management Without the Firm Size Variable.

$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 \text{LEV}_{it} + \beta_4 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$			
	Estimate	P-Value	VIF
Intercept	2.803e+01	<2e-16 ***	
DACC	-3.408e-17	0.3112	1.395029
CGOV	-2.273e-01	0.0135 *	1.041881
LEV	6.357e-01	0.4836	1.079378
ROA	2.927e+02	0.0865	1.378754
N	207		

Multiple R-squared	11.7%
F-statistic	2.607
Significance Codes	0.01 ‘***’ 0.05 ‘**’ 0.1 ‘*’

Source: data processed by the author, 2026

Based on the results of the previous tests, the main model indicates that firm size (SIZE) is a very strong determinant of executive compensation, while the direct effects of accrual-based earnings management (DACC) and *corporate governance* (CGOV) tend to be weak or inconsistent when control variables are included; and *corporate governance* (CGOV) only becomes significant when SIZE is excluded, indicating the possibility of overlapping effects and potential specification bias if firm-specific contexts are not controlled for. These findings underscore the urgency of testing the moderating mechanisms of *corporate governance*, as corporate governance theoretically acts as a monitoring mechanism that can weaken or strengthen the consequences of managers’ opportunistic behavior in financial reporting (Essa et al., 2016). This leads to the formulation of the following hypothesis:

H3 The relationship between executive compensation and earnings management is weaker in companies with stronger corporate governance mechanisms compared to companies with weak corporate governance

As shown in Table 7, earnings management is not significant and has a negative direction, but the moderating variable is significant with a negative direction. This finding demonstrates that the effect of earnings management is highly dependent on the level of *corporate governance* and tends to be weakened when *corporate governance* is stronger. Returning to Table 2, it is evident that the average *corporate governance* score is 21 with a median of 20.9. This indicates that an increase in earnings management (DACC) in companies with typical governance levels tends to be associated with a decrease in executive compensation.

Table 7. Regression Results for Executive Compensation and Earnings Management Moderated by Corporate Governance

$\text{LnTCE}_{it} = \alpha_0 + \beta_1 \text{DACC}_{it} + \beta_2 \text{CGOV}_{it} + \beta_3 (\text{CGOV}_{it} \times \text{DACC}_{it}) + \beta_4 \text{SIZE}_{it} + \beta_5 \text{LEV}_{it} + \beta_6 \text{ROA}_{it} + \gamma_i + \varepsilon_{it}$		
	Estimate	P-Value

Intercept	11.58111	1.49e-05**
DACC	10.79752	0.1137
CGOV	-0.15588	3.33e-08***
CGOV*DACC	0.74025	0.0334*
SIZE	0.49602	1.12e-08**
LEV	0.44960	0.5225
ROA	348.58356	0.0043**
N	207	
Multiple R-squared	31.87%	
F-statistic	15.59	
Significance Codes	0.01 '***' 0.05 '**' 0.1 '*'	

Source: data processed by the author, 2026

The separation of the sample into strong (SGOV) and weak (WGOV) *corporate governance* groups is necessary as a step in further analysis because previous estimation results indicate that the relationship between earnings management (DACC) and executive compensation is conditional on the level of governance, rather than a homogeneous relationship across all companies. This is reflected in the previously estimated moderation model, where the interaction coefficient proved significant ($p < 0.05$) with a negative direction, while the main coefficient of earnings management (DACC) itself became insignificant. Methodologically, this condition indicates the presence of heterogeneity of effects, namely that the influence of earnings management (DACC) on executive compensation varies depending on the strength of governance mechanisms.

Separating these models leads to a more precise interpretation and avoids average conclusions that obscure differences in firm behavior under strong and weak governance.

Table 8. Regression Results for Executive Compensation and Earnings Management Moderated by Strong and Weak *Corporate Governance*

	Strong Corporate Governance (Equation 5)	Weak Corporate Governance (Equation 6)
Intercept	13.18023 (0.00121**)	9.14300 (0.0136*)
DACC	36.38306 (0.08240.)	17.16353 (1.1504)
CGOV	-0.11304 (0.13535)	-0.14322 (0.0743)
CGOV*DACC	-1.80023 (0.4826*)	-1.15841 (0.0972.)
SIZE	0.40527 (0.00222**)	0.57378 (2.67e-07***)
LEV	0.96277 (0.41740)	-0.06085 (0.9385)
ROA	462.23884 (0.01768*)	292.88405 (0.0392*)
N	124	83
Multiple R-squared	18.89%	38.57%
F-statistic	4.54	7.954
Significance Codes	0.01 ‘***’ 0.05 ‘**’ 0.1 ‘*’	0.01 ‘***’ 0.05 ‘**’ 0.1 ‘*’

Source: data processed by the author, 2026

Essentially, this study examines the relationship between accrual-based earnings management (DACC) and executive compensation as it varies across different levels of *corporate governance*. In agency theory, compensation serves as a contractual instrument that can incentivize or deter opportunistic managerial behavior, while governance functions as a monitoring mechanism that curtails opportunistic actions (Nguyen et al., 2024) .

In the regression results of Equation 6—specifically for companies with weak corporate governance (WGOV)—the interaction coefficient is negative and significant at the 10% level, while the earnings management coefficient remains insignificant but negative in direction. This indicates that as *corporate*

governance quality improves, even within the weak governance group, the relationship between earnings management and executive compensation weakens. This finding aligns with the view of “that discretionary accruals reflect managerial discretion, which can reduce the credibility of reporting and increase risk. On the other hand, a significantly positive *return on assets* (ROA) indicates a performance-based compensation element, while *leverage* (LEV) is not significant—which is reasonable since leverage often exerts a two-way influence, namely creditor monitoring and contractual pressure, making its lack of significance reasonable (Huang et al., 2024) .

Meanwhile, in the regression results of equation 5, the five main patterns that emerge are essentially consistent but exhibit a trend toward better data quality, as they exhibit significance levels of 5–10%. Academically, this supports the argument that under stronger governance, audit committees, boards, or compensation committees are better able to sever the link between discretionary accrual-based performance and compensation, so that discretionary accruals do not become the basis for rewards; or, when governance is strong, compensation is more likely to reflect performance assessments considered more credible, rather than accounting profits that are susceptible to being driven by accrual discretion (Harymawan et al., 2020) . The consistency of results regarding the firm size (SIZE) and Return on Assets (ROA) variables further reinforces the narrative that the most stable determinants of compensation are scale and performance (Blanes et al., 2020) .

A key finding addressing your question regarding why Discretionary Accruals (DACC) are not significant after controlling for variables is the interaction model; the DACC coefficient itself represents the effect of DACC under the condition CGOV = 0, whereas the range of CGOV in real-world data is far from zero. Consequently, it is statistically reasonable for the earnings management (DACC) coefficient to appear insignificant even though the conditional relationship is strong. Furthermore, the Jones-model-based proxy for discretionary accruals reinforces the notion that it contains measurement error due to the imperfect separation of normal and discretionary accruals, so that when you include strong controls like SIZE and ROA—which are economically closely linked to earnings management—the residual variation in earnings management (DACC) related to actual earnings management becomes smaller and harder to detect (Nguyen et al., 2024) .

Overall, the results from both WGOV and SGOV point to the same conclusion: the interaction between DACC and governance is negative. Thus, the more governance functions—whether in weak or strong governance groups—the less likely *discretionary accruals* are to translate into higher compensation, and at a certain level, they even correlate with lower compensation. This finding aligns with the monitoring function to curb opportunistic behavior in the context of agency conflict (Boachie & Mensah, 2022) . The distinction between WGOV and SGOV is part of a robustness test that clarifies the heterogeneity of governance mechanisms, while the primary interpretation remains grounded in the conditional effects of interactions as recommended in moderation analysis (Park & Yi, 2023) .

4.3 Further Analyses

Measuring earnings management using the Jones approach, which has high measurement error, results in weak findings when regressed; therefore, a better measure of earnings management with minimal measurement error is needed. In this case, earnings management is measured using the “ , with the formula:

$$TACC_{it} = \alpha(1/TA_{it-1}) + (\beta_1 \Delta REV_{it} - \Delta RECV_{it})/TA_{it-1} + \beta_2 (PPEQ_{it}/TA_{it-1}) + \beta_3 ROA_{it-1} + \varepsilon_{it}$$

Notes:

TACC it = Total accruals of company i in year t.

TA_(it-1) = Total book value of company i’s assets at the end of year t-1.

$\Delta \text{REV}_{it} / \text{TA}_{it-1} \text{ assets}$ = Company *i*'s sales revenue in year *t* minus revenue in year *t*-1, scaled by total in year *t*-1.

$\text{PPE}_{it} / \text{TA}_{it-1}$ = The gross value of fixed assets (property, plant, and equipment) of company *i* at the end of year *t*, scaled by total assets in year *t*-1.

$\text{ROA}_{(t-1)}$ = *Return on Assets* (ROA) of company *i* in year *t*-1 (the previous period).

$\alpha, \beta_1, \beta_2, \beta_3$ = Estimated parameters. $\varepsilon_{(it)}$ = Residual value

(error term).

Table 9 shows the results of a comparison of regression results between earnings management using the Jones and Kothari approaches. The estimation results indicate that in the Kothari approach, neither earnings management nor the moderation variable ($\text{SGOV} \times \text{DACC}$) is significant, although the direction remains consistent with the Jones approach. Meanwhile, the control variables—firm size (SIZE) and return on assets (ROA)—remain consistent across both approaches. These findings suggest that strong corporate governance is the most stable determinant of compensation, driven by firm size and performance, while the contribution of accrual-based earnings management (DACC) depends on whether the DACC measure still incorporates performance components (Huang et al., 2024).

Table 9. Regression Results on Executive Compensation and Earnings Management Moderated by Corporate Governance Using the Jones and Kothari Earnings Management Formula

	<i>Strong Corporate Governance</i> (Equation 5)	<i>Strong Corporate Governance</i> (Equation 6)

	Jones model	Kothari model
Intercept P-Value	13.18023 (0.00121**)	1.328e+01 (0.00125**)
DACC	36.38306 (0.08240.)	5.717×10 ⁻¹⁶ (0.17316)
SGOV	-0.11304 (0.13535)	-1.124e-01 (0.15802)
SGOV*DACC	-1.80023 (0.4826*)	-2.870-17 (0.11460)
SIZE	0.40527 (0.00222**)	4.00e-01 (0.00273**)
LEV	0.96277 (0.41740)	1.085e+00 (0.36710)
ROA	462.23884 (0.01768*)	4.957e+02 (0.01352*)
N	124	124
Multiple R-squared	18.89%	17.36%
F-statistic	4.54	4.096
Significance Codes	0.01 ‘***’ 0.05 ‘**’ 0.1 ‘*’	

Source: data processed by the author, 2026

Based on the findings in Table 9, this further reinforces the view that the moderation results using the Jones approach should be interpreted as sensitive to the earnings management measurement method, whereas Kothari provides more conservative robustness. Evidence of moderation (SGOV×DACC) is more evident in the Jones measurement but weakens in the Kothari model; thus, moderation results should be treated as findings that must be interpreted alongside robustness checks of *earnings management* measurements.

Next, we compared the estimation results without the moderation variable using two different accrual earnings management proxies, the Jones model and the Kothari model, to assess the consistency of the findings when discretionary accruals are measured using different approaches.

Table 10. Regression Results on Executive Compensation and Earnings Management Using the Jones and Kothari Earnings Management Formulas

	All Research Samples	All Research Samples
	Jones model	Kothari model
Intercept	9.725e+00 (0.00945 **)	1.134e+01 (2.49e-05**)
DACC	-5.085e-17 (0.08227 .)	-6.686e-17 (0.01015*
CGOV	-1.291e-01 (0.10795)	-1.332e-01 (2.24e-08***)
SIZE	5.482e-01 (8.33e-07 ***)	4.897e-01 (2.24e-08***)
LEV	-3.761e-01 (0.63881)	2.192e-01 (0.75636)
ROA	2.693e+02 (0.06686)	3.875e+02 (0.00201**)
N	207	207
Multiple R-squared	35.7%	29.8%
F-statistic	8.579	17.08
Significance Codes	0.01 '***' 0.05 '**' 0.1 '*'	

Source: data processed by the author, 2026

A comparison of the two models in Table 10 shows that although both estimate discretionary accruals, the results are not entirely identical. In the Jones model, earnings management (DACC) tends to be negative but not significant at the 5% level, whereas in the Kothari earnings management model (DACC) becomes

negative and significant, indicating that performance adjustments in the Kothari model can yield a better measure of discretionary accruals than performance effects, making the relationship between DACC and compensation easier to detect statistically.

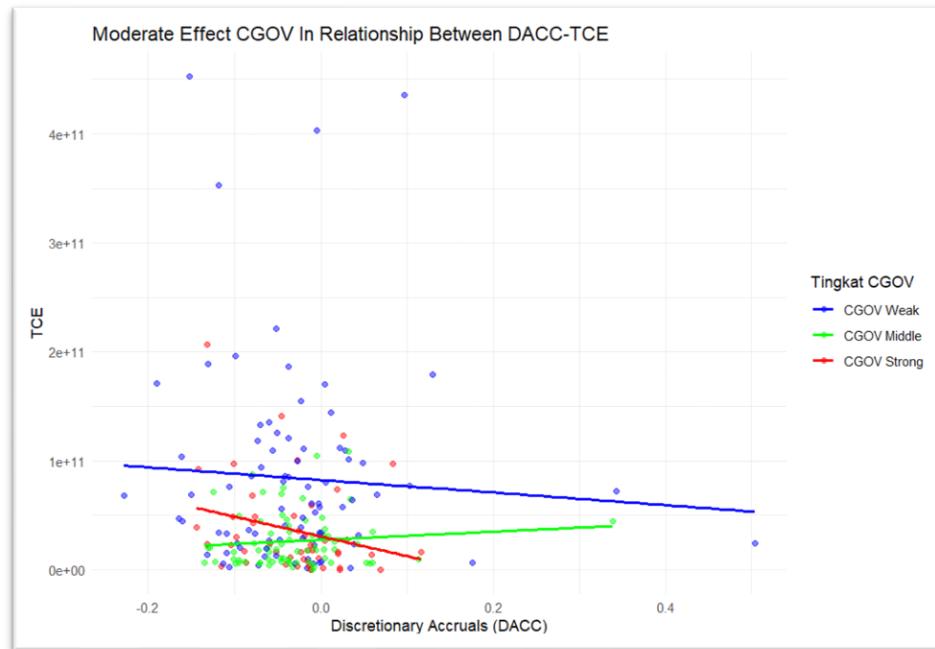
On the other hand, control variables show relatively consistent patterns in both models, particularly firm size (SIZE), which is positive and significant, and return on assets (ROA), which is positive and significant. This reinforces the argument that executive compensation levels are primarily influenced by firm size and performance, while the role of accrual earnings management depends on the sensitivity of the proxies used.

5. Conclusions

This study aims to explain the relationship between total executive compensation and discretionary accrual-based earnings management (DACC) in Indonesian firms during the 2022–2024 period, by positioning *corporate governance* as a mechanism that can weaken or strengthen this relationship, while controlling for ROA, leverage, and firm size. Out of a population of 1,007 companies, only 69 met the data completeness criteria, so the analysis was conducted on a more limited sample; meanwhile, the extremely wide variation in executive compensation levels across companies indicates the existence of remuneration disparities, which serve as an important context for interpreting the empirical results of this study.

Based on multiple linear regression estimates, hypothesis (H1), which states that earnings management (DACC) is positively associated with executive compensation, does not receive strong support. The earnings management (DACC) coefficient tends to be inconsistently significant and, in some specifications, even indicates a direction contrary to the predicted positive relationship; thus, overall, it cannot be concluded that there is a stable positive relationship between discretionary accrual earnings management and executive compensation. These findings imply that during the 2022–2024 recovery period, executive compensation in the study sample was more influenced by fundamental economic factors such as firm size and performance than by changes in discretionary accruals, and suggest that compensation incentives do not always translate directly into accrual earnings management practices as assumed in the supplementary hypothesis within the *Positive Accounting Theory* framework.

Figure 1. The Moderating Effect of Corporate Governance on the Relationship between Earnings Management and Total Executive Compensation



Source: processed data, 2026

Moderation tests indicate that the relationship between compensation and earnings management is conditional on the quality of governance. Generally, the interaction coefficients between earnings management (DACC) and *corporate governance* tend to be negative and, in some models, reach marginal significance levels, suggesting that stronger governance tends to weaken the relationship between accrual earnings management and executive compensation. These results support the logic of (H2), namely that the relationship between compensation and earnings management is weaker when governance mechanisms are strong and relatively stronger when governance is weak, as governance acts as a monitoring mechanism that increases the detection costs and reputational costs of reporting distortions. The sample was divided into SGOV (strong *corporate governance*) and WGOV (weak *corporate governance*) groups to clarify this heterogeneity and generally supports the direction of (H3), namely that the relationship under strong *corporate governance* is weaker than under weak governance regimes, although the strength of significance is influenced by sample size and differences in earnings management measurement proxies.

A comparison of earnings management measures (DACC) using the Jones and Kothari approach shows that empirical results are sensitive to the *earnings management* proxy; thus, conclusions should be interpreted as robust in direction but varying in statistical strength when the measure is adjusted for performance. Methodologically, this confirms that discretionary accruals are a proxy containing measurement error and can be contaminated by performance, making it important to include controls such as ROA and use alternative measures to strengthen the findings. Thus, the main contribution of this study is to demonstrate that the relationship between incentives and reporting in Indonesia is not homogeneous but depends on the quality of oversight mechanisms and how earnings management is measured, which aligns with agency theory and positive accounting literature regarding the roles of incentives, monitoring, and corporate contractual conditions.

Based on these findings, the recommendation for companies in Indonesia is to strengthen *corporate governance* practices substantively, not merely as a formality of compliance, particularly in companies with weak governance, through enhancing the effectiveness of the board or audit committee, improving disclosure transparency, and strengthening the reporting risk assessment process. Companies are also advised to review their compensation designs to avoid over-reliance on short-term accounting profit indicators, instead combining performance metrics that are more resistant to manipulation so that incentives are better aligned with reporting quality. Regulators and capital market stakeholders can promote consistency in the reporting of compensation components and the quality of governance disclosures to increase data availability and make reporting risk analysis more accurate.

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