

The Impact of Information and Firm Size on Earnings Management in Indonesia's Primary Consumer Sector Companies

Muliyani¹, Syamsudin²

Faculty of Economic and Business, University of Pamulang, Indonesia

Abstract

This study examines the influence of information asymmetry and firm size on earnings management in Indonesian listed firms. Using panel data analysis, the research evaluates both individual and joint effects of these variables. Descriptive statistics indicate a moderate level of earnings management, with firms exhibiting both income-increasing and income-decreasing adjustments. The results of hypothesis testing reveal that information asymmetry alone does not significantly affect earnings management ($p = 0.1764$), while firm size has a significant negative effect ($p = 0.0001$), suggesting that larger firms engage in less opportunistic reporting. However, the F-test shows that information asymmetry and firm size jointly have a significant impact on earnings management ($p = 0.036$), explaining 34.72% of the variation in the dependent variable. These findings align with agency theory, which emphasizes managerial discretion under information imbalance, and signaling theory, which highlights the strategic use of earnings to communicate firm performance. The study underscores the importance of governance and monitoring mechanisms in mitigating earnings manipulation in Indonesian firms.

Keywords: Information Asymmetry, Firm Size, Earnings Management

JEL Classification: G30; G32

Introduction

Corresponding author's email : : dosen00572@unpam.ac.id

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Financial statements are essential instruments for describing a company's performance; earnings information is frequently used by investors, creditors, and other external parties as a benchmark of financial performance. Consistency of earnings from one period to another enhances market perceptions of corporate stability and quality. However, the flexibility inherent in accounting standards allows management to exercise subjective judgment in choosing accounting policies and estimates, thereby creating opportunities for earnings management (Nasution & Pratiwi, 2023).

Winarno (2022) found that both accrual-based and real earnings management practices tend to reduce earnings persistence and weaken the relevance of earnings information as a performance indicator. This is consistent with Fraditya (2023), who reported that accrual earnings management negatively affects earnings quality among manufacturing firms listed on the Indonesia Stock Exchange. Furthermore, Farichah (2017) emphasized that even after the adoption of IFRS, the relationship between earnings management and earnings quality remains significant, suggesting that regulatory pressure has not entirely eliminated managerial opportunism in financial reporting.

One factor that drives earnings management is information asymmetry. This condition arises when managers have greater access to information about the company's prospects compared to external parties, creating opportunities for opportunistic behavior such as manipulating reported earnings. Setiawati and Syaiful (2022) found that information asymmetry had no significant effect on earnings management in Indonesian manufacturing firms, suggesting that improved transparency and monitoring mechanisms can reduce managerial discretion. In contrast, Isnawati et al. (2024) reported that information asymmetry had a positive and significant effect on earnings management in consumer sector companies listed on the Indonesia Stock Exchange, indicating that when managers possess superior information, the likelihood of earnings manipulation increases. Sekrihwati and Lestari (2021) further emphasized that information asymmetry remains a critical determinant of earnings management among leading manufacturing firms, consistent with agency theory, which posits that unequal access to information can motivate managers to act in self-interest.

Another factor influencing earnings management is firm size. Larger firms generally have more resources, stronger governance mechanisms, and closer scrutiny from regulators and investors, which can limit earnings manipulation. However, as noted by Setiawati and Syaiful

(2022), firm size exhibited a significant negative relationship with earnings management, implying that larger firms tend to behave more conservatively in financial reporting. Meanwhile, Isnawati et al. (2024) found no significant influence of firm size on earnings management, suggesting that company scale alone may not guarantee better reporting integrity. These findings collectively indicate that the relationship between firm size and earnings management remains context-dependent across industries and monitoring environments.

Agency theory explains earnings management as a result of conflicts of interest between shareholders (principals) and managers (agents), in which information asymmetry provides managers with the opportunity to manipulate financial reports for personal benefit (Al-Malkawi, 2023). Meanwhile, signaling theory assumes that managers use accounting information to convey positive signals about firm performance, aiming to reduce investor uncertainty and improve market perception (Shukla & Kumar, 2022). Both perspectives have been widely adopted to explain earnings management behavior in emerging markets, including Indonesia.

However, despite their theoretical strength, these frameworks often lead to **contradictory predictions** when firm size is introduced as a contextual factor. From the agency perspective, larger firms are expected to face higher monitoring intensity, which should constrain opportunistic reporting. Conversely, signaling theory suggests that larger firms have stronger incentives to maintain reputation and provide favorable signals to investors, which may encourage income-increasing practices. Empirical studies also show inconsistent evidence: some report a negative relationship between firm size and earnings management (Setiawati & Syaiful, 2022), while others find no significant or even positive associations (Isnawati et al., 2024; Faradhifa & Handayani, 2023).

These inconsistencies reveal a **theoretical gap** regarding how agency-driven opportunism and signaling-driven transparency interact under different firm size conditions. Prior research has rarely explored how firm size moderates or mediates the link between information asymmetry and earnings management, especially within developing-country contexts where corporate governance and disclosure quality vary widely (Adewunmi, 2024). Therefore, this study aims to bridge the theoretical gap by integrating agency and signaling theories to explain the dual role of firm size — as both a potential constraint and an amplifier — in influencing earnings management practices.

Empirical Gap

Previous studies have presented mixed results regarding the relationship between information asymmetry, firm size, and earnings management. For instance, Faradhifa and Handayani (2023) found that information asymmetry has a positive and significant influence on accrual-based earnings management, supporting the view that unequal access to information provides managers with discretion to manipulate reported earnings. In contrast, Setiawati and Syaiful (2022) revealed that information asymmetry has no significant effect on earnings management, indicating that improved transparency and governance can reduce opportunistic reporting behavior.

Similarly, empirical evidence on the role of firm size remains inconsistent. Sekrihwati and Lestari (2021) found that larger companies tend to engage less in earnings management due to tighter monitoring and reputational concerns, whereas Isnawati et al. (2024) reported that firm size does not significantly influence earnings management in consumer sector companies. These contradictory findings underscore that the relationship between firm characteristics and earnings management may depend on contextual factors such as governance quality, industry type, and information environment.

In Indonesia, the urgency of understanding earnings management practices is illustrated by the alleged manipulation case involving PT Tiga Pilar Sejahtera Food Tbk (AISA) in 2019, as revealed in the Ernst & Young Indonesia investigative report (Wareza, 2019). Such cases highlight the vulnerability of firms in the consumer goods sector—an industry essential to daily consumption yet often overlooked in corporate governance research compared to manufacturing or banking sectors.

Therefore, this study focuses on companies in Indonesia's consumer primary sector listed on the Indonesia Stock Exchange (IDX) during the 2019–2023 period to re-examine the influence of information asymmetry and firm size on earnings management, both simultaneously and partially. Specifically, it addresses three main questions: (1) Do information asymmetry and firm size jointly affect earnings management? (2) Does information asymmetry have a partial effect on earnings management? and (3) Does firm size have a partial effect on earnings management?

Through these objectives, the study seeks to provide theoretical contributions by strengthening the application of agency theory and signaling theory in explaining managerial behavior, while also offering empirical contributions by clarifying previous inconsistencies in findings. Furthermore, the results are expected to provide practical implications for investors, regulators,

and company management to enhance financial reporting quality and corporate governance within Indonesia's consumer sector.

Literature review

Basic Theories

Agency Theory

Agency theory explains the relationship between principals (shareholders) and agents (managers) within a company. The separation between ownership and control causes managers to have more comprehensive information about the company's internal conditions compared to external stakeholders. This imbalance of information, known as information asymmetry, may encourage managers to act opportunistically to maximize their personal interests—for example, through earnings manipulation. According to Jensen and Meckling (1976), such agency conflicts arise because managers do not always act in the best interests of shareholders. Similarly, Al-Malkawi (2023) emphasizes that weak monitoring and dispersed ownership intensify agency problems, thereby increasing the likelihood of earnings management in firms with high information asymmetry.

Signaling Theory

Signalling theory emphasizes that companies provide signals to the market through the disclosure of financial information. Positive signals, such as strong and stable earnings or extensive voluntary disclosure, are expected to reduce investor uncertainty and increase confidence (Adiwibowo 2018; Mahendra & Daljono 2023). However, managers may manipulate earnings figures or present overly optimistic disclosures to create a more favourable company image, thereby creating a gap between actual and reported conditions.

Earnings Management

Earnings management refers to managerial actions intended to influence the process of financial reporting to achieve specific objectives, such as meeting contractual targets, influencing

market perceptions, or complying with regulatory expectations. Although such practices are often carried out within the boundaries of generally accepted accounting principles, they can reduce the transparency and reliability of financial statements. According to Scott (2015), earnings management involves the choice of accounting methods that alter reported earnings to influence stakeholders' judgment about a company's economic performance. Similarly, Winarno (2022) found that both accrual and real earnings management negatively affect earnings persistence, indicating a decline in the quality and credibility of reported information.

Empirical Studies

Research on information asymmetry and earnings management has produced inconsistent results. Faradhifa and Handayani (2023) found that information asymmetry positively and significantly affects accrual-based earnings management, suggesting that when managers have superior information, they are more likely to manipulate reported earnings. Similarly, Isnawati et al. (2024) confirmed that information asymmetry significantly influences earnings management in consumer sector firms listed on the Indonesia Stock Exchange. In contrast, Setiawati and Syaiful (2022) reported no significant relationship between information asymmetry and earnings management, implying that enhanced monitoring and governance mechanisms can mitigate opportunistic behavior.

Studies examining firm size and earnings management also show mixed evidence. Sekrihwati and Lestari (2021) demonstrated that firm size negatively affects earnings management, as larger firms face stronger scrutiny and reputational pressure. Conversely, Faradhifa and Handayani (2023) found that smaller companies tend to engage in income-increasing strategies to meet performance expectations, while Isnawati et al. (2024) reported that firm size has no significant impact.

These contradictory findings reveal that the relationship between information asymmetry, firm size, and earnings management remains context-dependent, influenced by governance quality, ownership structure, and industry characteristics. Therefore, further investigation is needed—particularly in Indonesia's consumer primary sector, which plays a strategic role in economic resilience yet remains underexplored compared to manufacturing and financial industries.

Information Asymmetry and Earnings Management

Information asymmetry occurs when managers possess greater access to internal company information than external stakeholders, which allows them to make decisions not fully observable by investors or creditors. This imbalance of information can motivate managers to act opportunistically, including manipulating reported earnings to meet specific objectives. According to Jensen and Meckling (1976), the separation between ownership and control generates agency problems that enable managers to exploit information advantages for personal benefit. In line with this view, Faradhifa and Handayani (2023) found that information asymmetry positively and significantly influences earnings management, suggesting that managers use their superior knowledge to adjust accruals and influence reported performance. Similarly, Isnawati et al. (2024) reported a significant effect of information asymmetry on earnings management in consumer sector companies listed on the Indonesia Stock Exchange. Conversely, Setiawati and Syaiful (2022) found no significant relationship between information asymmetry and earnings management, implying that stronger monitoring and corporate governance mechanisms can mitigate opportunistic behavior.

H1: Information asymmetry has a significant effect on earnings management.

Firm Size and Earnings Management

Firm size reflects a company's level of resources, visibility, and the extent of external monitoring. Larger firms generally attract more attention from investors, regulators, and analysts, which tends to reduce earnings management practices due to reputational risk and stricter oversight. Sekrihwati and Lestari (2021) found that firm size has a negative effect on earnings management, indicating that larger companies are more transparent and face stronger governance pressure. Similarly, Winarno (2022) explained that the level of disclosure and monitoring in large firms reduces managers' flexibility to manipulate financial results.

However, other studies show that large firms may still engage in earnings management to maintain the appearance of stable performance or meet market expectations. Faradhifa and Handayani (2023) observed that smaller and medium-sized firms tend to perform income-increasing adjustments, while large firms may also manipulate earnings for signaling purposes. Meanwhile, Isnawati et al. (2024) reported that firm size has no significant influence on earnings management in Indonesian consumer sector companies, suggesting that contextual factors such as ownership concentration and governance quality can moderate this relationship.

H2: Firm size has a significant effect on earnings management.

Information Asymmetry, Firm Size, and Earnings Management

When considered simultaneously, information asymmetry and firm size may influence earnings management in a more complex and interrelated manner. Information asymmetry provides managers with opportunities to manipulate reported earnings due to unequal access to internal information. Conversely, firm size can act as either a constraining or amplifying factor depending on the strength of monitoring mechanisms and market expectations. According to Jensen and Meckling (1976), higher information asymmetry exacerbates agency conflicts, which may lead to opportunistic behavior such as earnings manipulation. Meanwhile, Shukla and Kumar (2022) argue from a signaling perspective that larger firms are motivated to provide credible signals through transparent financial reporting to reduce investor uncertainty; however, when information asymmetry persists, even large firms may engage in earnings management to maintain favorable perceptions.

Empirical research supports this duality. Faradhifa and Handayani (2023) found that both information asymmetry and firm size jointly influence earnings management in Indonesian listed firms, while Isnawati et al. (2024) observed that firm-specific characteristics, including size and governance, moderate the effect of information asymmetry on managerial discretion. These findings suggest that the interaction between information asymmetry and firm size determines the extent and direction of earnings management practices.

H3: Information asymmetry and firm size simultaneously have a significant effect on earnings management.

Research Method

The research used in this study is quantitative research with a causal associative approach. Quantitative research is used to study a specific group of people or sample, and it involves collecting data using tools or instruments, then analyzing the data using statistical methods to test

an existing hypothesis. A causal associative approach means the research looks at how two or more variables are connected or influence each other.

The data used in this study comes from secondary sources. Secondary data is information that is not collected directly by the researchers but is taken from existing documents, such as books, articles, and other materials that are related to and support the research. In this case, the data comes from the company's financial statements for the years 2019 to 2023.

The study included primary consumer sector companies listed on the Indonesia Stock Exchange from 2019 to 2023, making a total of 87 companies. The samples were chosen using purposive sampling, which means selecting based on specific criteria. These criteria are: (1) companies in the primary consumer sector listed on the IDX during the 2019-2023 period. (2) companies in the primary consumer sector that released financial reports during the same time. (3) companies in the primary consumer sector listed on the IDX that were profitable during the research period. (4) companies that had complete data for the research variables during the 2019-2023 period. This method was used because it helps get data that is relevant and representative of the study's goals.

The main way to collect data in this study is through the documentation method. This method records past events and can include written materials like financial reports. Data is gathered by looking at the reports from the companies chosen as part of the research. The study looks at how one variable influences another, where one is the cause and the other is the effect. To do this, the study uses several techniques such as descriptive statistical analysis, estimating a panel data regression model, selecting the best model for panel data, checking classical assumptions, performing panel data regression analysis, and testing hypotheses. These techniques are expected to provide a detailed and useful picture for understanding earnings management.

Table 1 Operational Variables of Research

Variable	Type	Indicator	Measurement	Source
Information Asymmetry	Independent	Degree of disparity in information between management and external stakeholders	Measured using the Bid-Ask Spread (BAS) formula: $BAS = (Ask\ Price - Bid\ Price) / ((Ask\ Price + Bid\ Price) / 2)$	Botosan (1997); Cai, Keasey, & Short (2006); Faradhifa & Handayani (2023)

Variable	Type	Indicator	Measurement	Source
Firm Size	Independent	The overall size of a company, reflecting its total resources and economic scale	Measured by the natural logarithm of total assets (Ln Total Assets)	Nazir & Afza (2009); Sekrihwati & Lestari (2021); Isnawati et al. (2024)
Earnings Management	Dependent	Managerial manipulation of reported earnings to achieve specific objectives	Measured using the Modified Jones Model to estimate discretionary accruals	Dechow, Sloan, & Sweeney (1995); Winarno (2022); Faradhifa & Handayani (2023)

Source: Researchers (2025)

Results and Discussion

Results

Before conducting hypothesis testing, it is necessary to provide an overview of the data through descriptive statistics. Descriptive statistics summarize the characteristics of each variable used in the study, including the mean, median, maximum, minimum, standard deviation, skewness, and kurtosis. These measures help describe the central tendency, variability, and distribution of the data, thereby offering a preliminary understanding of the sample before further analysis is carried out.

Table 2 below presents the descriptive statistics for the three main variables in this study, namely earnings management (EM), information asymmetry (AI), and firm size (FS), based on 120 observations of consumer primary sector companies listed on the Indonesia Stock Exchange during the 2019–2023 period.

Table 2 Descriptive Statistics

Variables	Mean	Median	Maximum	Minimum	Std. Deviation
Earnings Management (EM)	-0.033572	-0.034631	0.060424	-0.123367	0.040756

Variables	Mean	Median	Maximum	Minimum	Std. Deviation
Information Asymmetry (IA)	1.884105	1.625289	5.251476	0.476429	1.100530
Firm Size (FS)	29.93125	29.73914	32.85992	27.37466	1.458986

Source: EViews 9 Output, processed (2025)

Interpretation of Descriptive Statistics Based on Theory

Earnings Management (EM)

The mean value of earnings management in the sample is -0.033572 with a relatively small standard deviation of 0.040756, indicating that most firms tend to engage in earnings management at a low and relatively stable level. The minimum value of -0.123367 shows that some firms adopt income-decreasing strategies, while the maximum value of 0.060424 indicates that others engage in income-increasing adjustments.

From the agency theory perspective, the observed patterns indicate that managers exercise discretion in adjusting reported earnings due to the separation of ownership and control, allowing them to increase or decrease earnings based on personal incentives such as bonus targets, debt covenants, or performance perceptions (Jensen & Meckling, 1976). Simultaneously, signaling theory suggests that managers use earnings figures to communicate firm performance to external stakeholders, with positive adjustments signaling strength and future prospects. In this dataset, however, the slightly negative average value implies that income-decreasing strategies are more prevalent, reflecting cautious reporting behavior aimed at avoiding overstatement, regulatory scrutiny, or misaligned market expectations. Overall, these descriptive statistics illustrate that managers employ earnings management both to pursue private objectives and to influence market perceptions, while a tendency toward income-decreasing adjustments suggests a conservative or risk-averse approach to financial reporting.

Information Asymmetry (IA)

The mean value of information asymmetry in the sample is 1.884105 with a high standard deviation of 1.100530, indicating substantial variation among companies. The maximum value of 5.251476 demonstrates that some firms experience very high levels of information imbalance between managers and external stakeholders, while others show much lower levels (0.476429).

According to agency theory, high information asymmetry provides managers with greater opportunities to manipulate earnings, as external parties cannot easily verify internal company information (Jensen & Meckling, 1976).

Firm Size (FS)

The average firm size is 29.93 with a small standard deviation of 1.458986, and the range is relatively narrow (minimum 27.37, maximum 32.85). This indicates that the companies in the sample are generally large and financially stable, with relatively similar scales of operation. From the perspective of agency theory (Jensen & Meckling, 1976), larger firms tend to have stronger monitoring mechanisms, more transparent reporting systems, and higher scrutiny from external stakeholders such as regulators, auditors, and institutional investors. These characteristics reduce managerial discretion and the likelihood of opportunistic earnings manipulation, as managers in larger firms face greater reputational and regulatory risks. Conversely, smaller firms—although not dominant in this sample—are typically more inclined to engage in earnings management to project better performance and attract investors. In addition, signaling theory (Spence, 1973; Shukla & Kumar, 2022) suggests that large firms use transparent and consistent earnings disclosures as positive signals of financial strength and stability. However, these same signaling pressures may motivate managers to engage in income-smoothing behavior to maintain favorable market perceptions. Given the narrow variation in firm size among the sampled companies, the overall impact of firm size on earnings management may be relatively limited, as the firms share similar levels of governance quality, monitoring intensity, and disclosure standards.

Theoretical Synthesis

The descriptive statistics suggest that: Earnings management in the sample is relatively modest, aligning with the expectation from agency theory that managers exploit discretion but within limits. Information asymmetry shows the greatest variability, consistent with agency theory's prediction that higher asymmetry increases the scope for opportunistic behavior. Firm age indicates mature firms with less variation, which theoretically implies stronger governance and reduced likelihood of aggressive earnings management.

Panel Data Estimation

Before determining the most appropriate model to analyze the effect of information asymmetry and firm age on earnings management, regression tests were conducted using three panel data approaches, namely the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). Each model provides estimated coefficients for the independent variables along with statistical indicators such as the adjusted R² and F-statistic probability. These indicators are useful to assess the explanatory power and overall significance of the models.

To ensure robustness, model selection tests were also performed, including the Chow test to compare the Common Effect and Fixed Effect models, and the Hausman test to distinguish between the Fixed Effect and Random Effect models. The results of these tests serve as the basis for selecting the most suitable model for further interpretation and hypothesis testing.

Table 3 presents a summary of the panel data regression results from the three approaches, while Table 4 reports the outcomes of the Chow and Hausman tests that determine the best-fitting model.

Table 3 Panel Data Regression

Variable / Statistic	CEM (Common Effect)	FEM (Fixed Effect)	REM (Random Effect)
Constant (C)	-0.041487 (p = 0.598)	-2.119664 (p = 0.0001)	-0.116510 (p = 0.304)
Information Asymmetry (AI)	-0.000922 (p = 0.789)	0.008355 (p = 0.176)	0.001301 (p = 0.754)
Firm Size (FS)	0.000322 (p = 0.901)	0.069170 (p = 0.0001)	0.002689 (p = 0.473)
Adjusted R ²	-0.0163	0.3473	-0.0126
Prob(F-statistic)	0.9543 (ns)	0.000005 (sig)	0.7714 (ns)
Observations	120	120	120

Source: EViews 9 Output, processed (2025); *p < 0.05

Table 4 The Chow and Hausman test

Test	Prob. Value	Decision	Selected Model
Chow Test	0.0000	Reject CEM → Use FEM	FEM

Test	Prob. Value	Decision	Selected Model
Hausman Test	0.0002	Reject REM → Use FEM	FEM

Source: EViews 9 Output, processed (2025)

Alignment with hypotheses:

H1: Information asymmetry does not significantly affect on earnings management ($p = 0.1764 > 0.05$)

H2: Firm size has a significant effect on earnings management ($p = 0.0001 < 0.05$)

H3: IA & Firm size jointly affected earnings management (F-test $p = 0.036 < 0.05$)

Discussion

The results of this study demonstrate that information asymmetry and firm size jointly influence earnings management, consistent with agency and signaling theories. According to **agency theory** (Jensen & Meckling, 1976), higher information asymmetry increases managers' discretion and opportunities for opportunistic behavior, as they have greater access to internal information than shareholders. Empirical evidence from Faradhifa and Handayani (2023) supports this, showing that firms with higher asymmetry are more likely to manipulate reported earnings to achieve personal or corporate objectives.

From the **signaling theory** perspective, managers use earnings disclosures to convey firm performance and reduce investor uncertainty. Firms with greater visibility or market presence are incentivized to maintain stable earnings signals, but such pressures can also lead to income-smoothing (Shukla & Kumar, 2022). In the Indonesian consumer goods sector, Isnawati et al. (2024) found that large firms with high information asymmetry strategically adjust earnings while controlling disclosures to project financial stability, reflecting the dual influence of managerial discretion and market signaling.

Nonetheless, the effect of information asymmetry and firm size on earnings management is context-dependent. Effective governance, stricter monitoring, and high-quality audits can mitigate opportunistic reporting, resulting in non-significant effects in some cases (Setiawati & Syaiful, 2022). Even large firms, which are more closely scrutinized, may manipulate earnings under

reputational or market pressures to meet stakeholder expectations (Sekrihwati & Lestari, 2021). These findings indicate that earnings management arises from the interaction of managerial incentives, firm characteristics, and external monitoring mechanisms, highlighting the importance of governance and transparency in shaping financial reporting practices.

Conclusion

This study shows how information asymmetry and company size affect earnings management. When these two factors are combined, they can influence the likelihood of earnings management. This is because large companies with high information asymmetry struggle to get quality reports. There are many reasons for this, such as moral hazard, adverse selection, and high agency costs, which can make it hard to tell if the data in the reports is accurate. However, the study also found that information asymmetry alone does not affect earnings management. This suggests that whether information asymmetry is high or low, it doesn't lead to more earnings management. This means the financial statements that are submitted or published are of good quality. In addition to information asymmetry, company size also affects earnings management. This means that more attention should be given to large companies. This is important because investors who are still considering investing based on financial reports need to rely on accurate and reliable information.

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