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STATUTORY ATTRIBUTES OF FEMALE DIRECTORS AND EARNINGS QUALITY IN INDONESIA

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Abstract: All parties with an interest in the company need quality earnings information for economic decision making. This creates a moral hazard on the part of management to use various means in order to provide good news for these parties. This study aims to examine the effect of various attributes required by law (namely business education background, proportion, years of service, and foreign citizenship) related to the presence of women in top management on the earnings quality of companies in Indonesia. With the sample criteria set, 467 observations were obtained for companies listed on the IDX in 2015 - 2018. The results obtained indicate that the business education background and foreign citizenship of female directors affect earnings quality. Meanwhile, the proportion and tenure of female directors have no effect on earnings quality.

Keywords: *Earnings Quality, Background Of Business Education, Proportion, Tenure, Foreign Nationality.*

INTRODUCTION

Financial reporting is a communication medium for companies to provide information about the company's performance in a period to its users. One indicator of good company performance is quality earnings information; reliable, precise, adequate, or in other words has low information asymmetry (Darmayanti & Kassim, 2020; Sarun, 2016).

Several accounting scandals, both worldwide (such as Enron, Worldcom, Lehman Brothers, Freddy Mac, Tyco, and so on), as well as those occurring in Indonesia (such as Garuda, Jiwasraya, Jasindo, Krakatau Steel, Asabri, and so on), have captured public attention and reduce their trust in earnings information (Darmayanti & Kassim, 2021). For example, Enron, the 7th largest energy company in the US in 2001 carried out a fraud scandal through its financial statements, which sacrificed the company's stakeholders (Rubin & Segal, 2019), or the alleged manipulation of financial statements at Garuda Indonesia in 2018 which resulted in the Indonesian state-owned airline being sanctioned by the Ministry of Finance and restatement of financial statements by the Financial Services Authority (CNN Indonesia, 2019). These cases further convince the public that earnings management activities always occur in companies, both in the form of real earnings management and accrual earnings management (Darmayanti & Kassim, 2020), which results in increasingly questioning the quality of the company's earnings.

Previous research that focused on corporate governance stated that the board of directors as part of the monitoring mechanism plays an important role in controlling the level of quality of financial reporting so as to reduce earnings management actions (Darmayanti et al., 2022; Gounopoulos & Pham, 2018; Kirsch, 2018; Koevoets, 2017; Waweru & Riro, 2013). Furthermore, research on board of directors that focuses on gender equality states that the presence of female directors is believed to provide great benefits for the company, such as: a different way of managing team work (Ward & Forker, 2017); take advantage of cultural, racial, and ethnic diversity into opportunities (Tavanti & Werhane, 2013); High protection of owners through executive decisions (Chen, Crossland, & Huang, 2014; Cruz et al., 2012); focus on improving the quality of corporate earnings and tend to be sensitive to reputation tarnishing and the risk of lawsuits (Srinidhi et al., 2011).

In Indonesia, in the determination of directors, there are several attributes of legislation regulated by the Financial Services Authority as well as those determined by the company's articles of association in selecting directors, such as educational background, proportion, tenure, and nationality, which aim to simplify the duties of directors in carry out the management supervisory function effectively (Fama & Jensen, 2019); and tend to be open to constructive suggestions in the boardroom (Gull, 2018).

Recent studies have shown a correlation between business educational background and income quality (Darmayanti et al., 2021; Levi et al., 2014; Hussin & Othman, 2012; Gounopoulos & Pham, 2018; Nekhili & Gatfaoui, 2013). Especially if there are female directors, earnings quality tends to increase (Darmayanti et al., 2021); financial reporting policies tend to be conservative (Arun et al., 2015); and managers tend to be cautious in managing earnings (Corkery, 2018; Gull, 2018; Lammers & Garcia, 2017; Armstrong et al., 2014).

As seen from the statutory attributes, the results of the research support the importance of earnings quality in a company; such as tenure that can improve earnings quality (Tiwari & Ahamed, 2018; Kim & Yang, 2014; Li et al., 2013); foreign female directors are believed to be able to improve company performance (Chiu et al., 2013); the background of foreign nationals makes them more networked, more independent, and skilled (Gull, 2018; Enofe et al., 2017); carry out monitoring activities effectively and efficiently (Srinidhi et al., 2011); maintain reputation through quality income (Abdulmalik & Ahmad, 2016). Based on the explanation above, this study aims to examine the legal side of the existence of female directors on earnings quality in Indonesia.

LITERATURE REVIEW

Earnings quality cannot be defined in a single standardized conclusion, depending on the context of the decision. An analyst sees high-quality earnings if earnings information reflects the company's current operating performance and can be an indicator of future operating performance (Dechow, 2002); while creditors see high-quality earnings if the income can be easily converted into cash flow and reflects the actual performance of the manager (Kamarudin & Ismail, 2014). That is, quality earnings depend on the accuracy of information, describe the company's financial performance, and can be used in predicting the company's operating performance in the future (Fathussalmi et al., 2019).

There are several studies that emphasize factors affecting earnings quality. Yet, there are few studies that focus on the presence of women on the board of directors. This research is interesting, because especially in Indonesia, the presence of women in management is still very limited at 11.3% in ASEAN (Credit Suisse Research Institute, 2019). The contribution of this research is expected to be able to answer the question of the importance of increasing the number of women in top management, especially in Indonesia.

Indonesia Corporate Governance Manual (2018) confirms that business education background, experience, knowledge, and skills are important factors in increasing company effectiveness. In addition to regulation, previous research has documented that a director who has expertise in finance will affect the way she works in evaluating company performance (Custódio & Metzger, 2014; Levi et al., 2014); provide a useful perspective in risk assessment (Hussin & Othman, 2012).

Good accounting decisions can be obtained if the director has adequate financial skills and experience, so that the quality of financial reports can be guaranteed (Gounopoulos & Pham, 2018; Nekhili & Gatfaoui, 2013); and negatively related to earnings management activities (Li et al., 2016). Then the proposed hypothesis is:

H1: The business education background of female directors has an effect on earnings quality.

A number of previous studies have found that the proportion of women on the board of directors has an effect on accounting aggressiveness (Gavious et al., 2012); effective decision making (Corkery, 2018; Smith, 2014); suppress earnings management activities (Gull et al., 2018; Armstrong et al., 2014).

While several studies have found the opposite, the proportion of women has a significant negative effect on company performance (Sun et al., 2011; Darmadi, 2013). Then the proposed hypothesis is:

H2: The proportion of female directors has an effect on earnings quality.

Indonesian regulations do not stipulate a term limit for members of the board of directors. The generally accepted practice is that a director can hold office for a maximum of five years and have the opportunity to be re-elected (Indonesia Corporate Governance Manual, 2018).

There are several points of view about a person's tenure and its relationship to earnings quality. When someone is in the comfort zone, they tend to be reluctant to change because they feel that what has been done has reached the optimal condition (Allen, 1969); and earnings management activities tend to increase (Kim & Yang, 2014; Li et al., 2013).

However, several other studies have found that a long tenure makes a director better understand the company's conditions and tend to have a commitment to improve company performance (Buchanan, 2018); carry out effective monitoring because long tenure supports better knowledge and experience regarding company conditions (Sun et al., 2011); and increased earnings quality (Firoozi et al., 2016).Then the proposed hypothesis is:

Previous research on the presence of foreign directors on earnings quality is inconsistent. The first study found that the presence of foreign directors tended to be high cost and ineffective; low understanding of law, accounting standards, governance, and local norms (Hooghiemstra et al., 2019); tend to have difficulty in active communication in the local language (Hooghiemstra et al., 2019; Piekkari et al., 2015); thus interfering with effective decision making in the boardroom (Miletkov et al., 2017; Piekkari et al., 2015). This has an impact on increasing earnings management (Hooghiemstra et al., 2019).

While the second research group concluded otherwise. The limitations of the local network have an impact on maintaining the independence of the supervisory task, achieving more focused

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goals (Chiu et al., 2016); have a broad external network, more expertise (Gull, 2018); a more visionary perspective and ready to be controversial (Enofe et al., 2017). In addition, the work culture they carry tends to make them work more effectively and efficiently (Srinidhi et al., 2011); and can improve earnings quality and maintain the reputation of the directors (Abdulmalik & Ahmad, 2016). Then the proposed hypothesis is:

According to a review of related literature mentioned above, a distilled overview of conceptual model and hypothesis are portrayed in Figure 1.

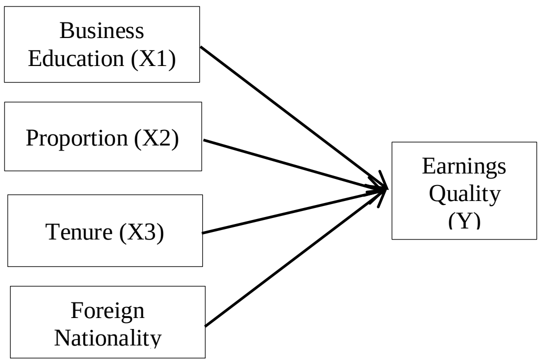

Figure 1 Research Model

METHOD

The population of this study were all companies listed on the Indonesia Stock Exchange from 2015 to 2018. Using the purposive sampling method, the researchers chose a representative sample with the following criteria: 1). The company is not included in the banking sector and other financial institutions; 2). The company is not experiencing financial problems; 3). The company publishes financial statements on December 31 during the year under review; 4). The company has the data needed in this study.

The dependent variable in this study is the quality of earnings as measured by the standard deviation of the residuals (Dechow, 2002) and the formula used is:

$$WCA_{i,t} = \beta_{0,i} + \beta_{1,i} CFO_{i,(t-1)} + \beta_{2,i} CFO_{i,t} + \beta_{3,i} CFO_{i,(t+1)} + \varepsilon_{i,t} \quad (1)$$

$$WCA_{i,t} = \Delta CA_{i,t} - \Delta CL_{i,t} - \Delta CASH_{i,t} + \Delta DEBT_{i,t} \quad (2)$$

$$CFO_{i,t} = NI_{i,t} - (\Delta CA_{i,t} - \Delta CL_{i,t} - \Delta CASH_{i,t} + \Delta DEBT_{i,t} - DEP_{i,t}) \quad (3)$$

Where WCA is the company's accrued working capital; CFO (operating cash flow); CA (current assets); CL (current liabilities); CASH (cash); DEBT (long-term liabilities maturing in the current year); NI (net income); and DEP (depreciation). All variables are deflated by total assets.

While the independent variables in this study are 1). The business education background of female directors is measured by the percentage of female directors who have an undergraduate education with a business background out of the total female directors (Gull et al., 2018); 2). The proportion is measured by the percentage of female directors compared to the total directors (Triana & Asri, 2017); 3). The tenure of female directors is measured by the average tenure of women per company per year of observation (Kim & Yang, 2014); and 4). The foreign nationality of female directors is measured by the percentage of the number of foreign female directors divided by the total number of female directors (Bennouri et al., 2018).

The research model used to examine the relationship between the statutory attributes of female directors on earnings quality in Indonesia is as follows:

$$EQ = \alpha + \beta_1 BE + \beta_2 PROP + \beta_3 TEN + \beta_4 FN + \varepsilon_{i,t}$$

Where, EQ (earnings quality); BE (business education background); PROP (proportion); TEN (tenure/term of office); FN (foreign nationality).

Due to the limited number of female directors in public companies listed on the IDX, this research uses the unbalance panel data. The testing phase begins with testing the classical assumptions (multicollinearity, heteroscedasticity, and autocorrelation), in order to obtain certainty that the data has met the requirements of statistical techniques. Then proceed with the hypothesis testing phase, using a significance level of 5%. In this study, researchers used SPSS version 20.0 as a test tool.

RESULT AND DISCUSSION

From the set sample criteria, 146 companies became the research sample, with 467 total observations for a period of 4 years of observation. Table 1 shows the descriptive statistics of the observations.

Table 1. Descriptive Statistics

	N	Min	Max	Mean	Std. Deviation
Earnings Quality (Y)	467	0.00	0.92	0.0463	0.40524
Business Education Background (X1)	467	0.00	1.00	0.6970	0.15664
Proportion (X2)	467	0.08	1.00	0.3332	5.16893
Tenure (X3)	467	1.00	28.00	6.1921	0.23081
Foreign Nationality (X4)	467	0.00	1.00	0.0690	0.15865
Valid N (listwise)	467				

Sources: Data processed with IBM SPSS Statistics for Windows, Version 25.0

From table 1, it can be seen that the variable of business education background of female directors as measured by the percentage of female directors with business education background from the total female directors has an average value of 0.697, and 0.00; 1.00; and 0.157 for the minimum, maximum, and standard deviation values. Meanwhile, the variable proportion of female directors shows a value of 0.333; 0.00; 1.00; 5,169 consecutively. The term of office variable shows a value of 6.1921; 1.00; 28.00; 0.231 for the mean, minimum, maximum, and standard deviation values. Furthermore, the foreign nationality variable shows a minimum value of 0.00; maximum value 1.00; the average value is 0.069; and a standard deviation of 0.159. Meanwhile, the research dependent variable (earnings quality) shows an average value of 0.0463; minimum value 0.00; maximum value 0.92; and the standard deviation value is 0.405.

A summary of the results of classical assumption testing and hypothesis testing can be seen in table 2.

Table 2: A Summary of the Hypothesis Testing

	β	t	Sig	Conclusion	VIF
Constant	0.044	1.977	0.049		
Business Education Background (X1)	0.046	2.524	0.012**	Accepted	1.013
Proportion (X2)	-0.050	-1.068	0.286	Rejected	1.008
Tenure (X3)	-0.001	-0.968	0.334	Rejected	1.013
Foreign Nationality (X4)	-0.065	-2.045	0.041**	Accepted	1.017
R-Square			0.024		
Adjusted R-Square			0.016		
F Statistic			2.864		
Significance of F			0.023**		
Durbin-Watson			0.430		

Dependent Variable: Earnings Quality (Y)
Note: (*) corresponds to a significance level of 10%; (**) 5% significance level; (***) 1% significance level.
Sources: Data processed with IBM SPSS Statistics for Windows, Version 25.0

Table 2 shows a summary of the results of classical assumption testing and hypothesis testing. For multicollinearity testing, all independent variables have a

VIF value around 1 (Gujarati, 2009) which means that there is no collinearity relationship between independent variables. Meanwhile, for autocorrelation testing, using Durbin-Watson obtained a value of 0.430. By using a range of -2 to +2 (Santoso, 2015), it can be concluded that there is no problem with autocorrelation.

For the test results of R2 and F statistics, the R2 value is 2.4%, meaning that the independent variable is able to influence the earnings quality variable by 2.4%; while 97.6% is influenced by other factors. Then seen from the F-statistics has a value of 2.864 and a significance of 0.023, meaning that all independent variables simultaneously have an influence on earnings quality at a value of 5%.

The first hypothesis examines the effect of female directors' business education background on earnings quality. The results of testing the first hypothesis show a regression coefficient value of 0.046 and a significance value of 0.012. From the results of this test, it is concluded that there is an effect of the educational background of female directors on earnings quality in companies listed on the IDX (Hypothesis 1 is accepted).

As the company's top management, the Board of Directors has broad responsibilities, including ensuring the quality of financial reporting. Custódio and Metzger (2014) show that directors who have financial experience and skills tend to be able to prepare quality financial reporting. Furthermore, Nekhili & Gatfaoui (2013) propose that education and business skills provide opportunities for female directors to achieve key positions in companies. Also, Li et al. (2016) ensure that if the company has female directors who understand the business environment it will be able to improve the quality of earnings

The results shown by hypothesis 1 indicate that the higher the formal education of female directors, especially in the business sector, the lower the quality of company earnings. The low earnings quality of companies led by skilled female directors in terms of formal education certainly needs to be explored. There are two indications of this possibility that comes from human character, namely greed and need. These two indications can arise because of the executive's personal needs or the existence of corporate interests that pressure them to take such action.

The second hypothesis examines the effect of the proportion of female directors on earnings quality. The results of testing the second hypothesis show a regression coefficient value of -0.05 and a significance value of 0.286. From the results of this test, it is concluded that there is no effect of the proportion of female directors on earnings quality in companies listed on the IDX (Hypothesis 2 is rejected).

For hypothesis 2, the test results show the opposite position. Many studies have found that the diversity of the board of directors has an impact on management performance (Arun et al., 2015; Levi et al., 2014; Huang & Kisgen, 2013; Srinidhi et al., 2011). However, the results of this study further support the research findings which state that the low share of women on the board has an impact on the lack of female voices during board decision making (Huang & Sun, 2017; Jiang et al., 2013).

From table 2 descriptive statistics, it is known that the average proportion of women on the board of directors in Indonesia is around 33%. The limited number of women has an impact on their attitude during the decision-making process. There is a tendency for female directors to avoid starting arguments, refrain from exchanging individual information, communicating their opinions, or provoking lively discussions, and in the

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end their presence as a minority does not affect the preparation of quality financial reports.

The third hypothesis examines the effect of tenure of female directors on earnings quality. The results of testing the third hypothesis show a regression coefficient value of -0.01 and a significance value of 0.334. From the results of this test, it is concluded that there is no effect of tenure of female directors on earnings quality in companies listed on the IDX (Hypothesis 3 is rejected).

The results of this study do not support the findings of previous studies which show tenure can improve earnings quality (decrease earnings management). However, if seen from table 1 descriptive statistics, information is obtained that the average tenure of female directors is 6.19. This figure shows that the tenure of female directors of public companies in Indonesia tends to be long. Although the results of the study do not support the hypothesis, the direction shown by the regression coefficient supports the hypothesis that the length of tenure of female directors has an effect on the high quality of earnings.

The fourth hypothesis examines the effect of foreign nationality of female directors on earnings quality. The results of testing the fourth hypothesis show a regression coefficient value of -0.065 and a significance value of 0.041. From the results of this test, it is concluded that there is an influence of foreign nationality of female directors on earnings quality in companies listed on the IDX (Hypothesis 4 is accepted).

The results of this study are in line with the findings of previous studies that documented the positive influence of the presence of foreign directors on company performance (Ujunwa et al., 2012; Polovina & Peasnell, 2015; Gallego et al., 2015; Ruigrok et al., 2007); tendency to be more independent, full of skills, and have a broad external network (Gull, 2018); broad-minded and ready for controversy (Enofe et al., 2017); tend to be more effective and efficient in monitoring (Srinidhi et al., 2011).

CONCLUSIONS

This study aims to examine the effect of statutory attributes of female directors on earnings quality in Indonesia. By using a sample of companies listed on the Indonesia Stock Exchange from 2015 to 2018, it is concluded that the business education background of female directors and the foreign nationality of female directors affect earnings quality in Indonesia. Meanwhile, the proportion of female directors and the term of office of female directors have no effect on earnings quality in Indonesia.

The limited number of female directors in companies listed on the IDX is the main limitation in this study. This condition resulted in the research methodology in the form of unbalanced panel data (meaning the number of observations each year was not the same throughout the year of observation). The following limitation is the measurement of the earnings quality variable using residual value regression from working capital accruals resulting in a very low R2 value, so it can be seen that the effect of the independent variable on the dependent variable is minimal.

Departing from the above limitations, it is recommended that in future research it is recommended to extend the year of observation and measure the presence of female directors in the form of index numbers so that all listed companies can be used in the study. As for the measurement of earnings quality, subsequent studies use other measurements that are able to detect quality earnings in a more accurate way

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