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Influence of *Good Corporate Governance* and Capital structure to Profitability and ProfitManagement in Manufacturing CompanyListed on Efek the Indonesia Stock Exchange

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***Abstract**: Research objectives: (1) to partially analyze the effect of good corporate governance and capital structure on profitability. (2) to partially analyze the effect of good corporate governance and capital structure on earnings management. (3) to analyze the effect of profitability on earnings management. (4) To partially analyze the effect of good corporate governance and capital structure on earnings management through profitability.Quantitative research approach. Research locations on the Indonesia Stock Exchange by accessing data through the Indonesia Capital Market Directory via the IDX website. The object of research in manufacturing companies listed on the Indonesia Stock Exchange in the period 2015 -2019. The population is 142 companies and the sample is 42 (210 sample units). The technique of sample collection is by purposive sampling. The analytical method uses the Structural Equauation Model (SEM) and SPSS-23.The results of the study: (1) good corporate governance and capital structure partially have positive and significant effect on profitability, (2) good corporate governance has a positive and significant effect on earnings management, (3) capital structure has a positive and not significant effect on earnings management, (4) profitability has a positive and significant effect on earnings management. (5) good corporate governance and capital structure partially have a positive and significant effect on earnings management through profitability.*
***Keywords:** Good Corporate Governance, Capital Structure, Profitability, Profit Management*

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I. Preliminary

Earnings management is a form of deviation committed by agents in the process of preparing financial statements within the limits allowed based on accounting principles. Earnings management is carried out by agents with the aim of providing misleading information for users of financial statements. Various motivations that cause managers to manage earnings, namely: (1) motivation of contracts, compensation, and loans, (2) capital market motivation, and (3) types of companies. Halim, et al. (2005), divides the way of understanding earnings management into two. (1) see it as opportunistic behavior of managers to maximize their utility in dealing with compensation contracts, debt contracts, and political costs (Opportinistic Earning Management). (2) views earnings management from the perspective of efficient contracting (Efficient Earning Management), where earnings management gives managers the flexibility to protect themselves and the company in anticipating unexpected events for the benefit of those involved in the contract.

The efforts made by the company to minimize earnings management are through Good Corporate Governance (GCG). The implementation of GCG in Indonesia is still not meeting expectations. Therefore the application of GCG requires a strong commitment to make it happen (Hamdani, 2016: 111). The Indonesian Institute for Corporate Governance (IICG) is one of the parties that encourages the creation of GCG in Indonesia. IICG is committed to supporting GCG practices in Indonesia and helping companies apply GCG concepts. GCG encourages the formation of transparent, clean and professional management work patterns. GCG is expected to eliminate the opportunistic behavior of agents to take earnings management actions. Research on the effect of GCG on earnings management has been carried out broadly. However, there are still inconsistencies between the results of existing research. Research from Eva Rosa Dewi S and Moh. Khoiruddin. (2016) proved that institutional ownership, managerial ownership, board size and audit committee size had no significant effect on earnings management. While the proportion of independent commissioners has a positive and significant effect on earnings management. Similarly, research from Tegar and Andri (2014) proves that audit committee, managerial ownership and institutional ownership partially have a significant effect on earnings management. Finally, research from Mawardi (2017) proves that GCG has a significant positive effect on earnings management.

A profitable company generally borrows in small amounts. That is because they need a little external financing. Companies that are less profitable tend to have more debt because of insufficient internal funds and because debt is the preferred external source. External funds are preferred in the form of debt rather than capital. Long-term funding through debt will incur a fixed burden in the form of interest which has an impact on reducing profitability. Decisions regarding the source of funds relating to capital structure. Research on the effect of capital structure on earnings management has been carried out broadly. However, there are still inconsistencies between the results of existing research. Research conducted by Obeidat et al. (2016) shows that there is a positive relationship between capital structure and earnings management. This study explains that decisions on capital structure can effectively minimize the opportunistic behavior of managers to take earnings management actions. The results of the study support the findings of Novita (2017), Sofia (2016) which proves that the proxy capital structure with leverage ratio has a significant effect on real earnings management. However, these findings contradict the findings of Dendi (2017), Alfitrah (2018), I Ketut et al. (2015), which proves that capital structure has no significant effect on earnings management.

Profitability for investors, shareholders and stakeholders is often used as a basis for evaluating company performance (Nugroho, 2014). Increasing profitability requires good company management or GCG. GCG will encourage the formation of a transparent, clean, and professional manager / board of directors working pattern (Ramdhaningsih and Utama, 2013). Slefer and Vishny (1997) in Luh (2017), GCG implementation gives investors confidence that agents can benefit them, will not embezzle funds, there is transparency and clear information on the company's performance in the future. A positive signal will increase the confidence of potential investors and affect the availability of funds needed by agents to support the increase in probability.

Research on the effect of GCG on profitability has been carried out extensively. However, there are still inconsistencies among the results of existing studies, such as: research from Iqbal and Kakakel (2010), Rini and Ghozali (2012), Sukandar (2014), Elly et al. (2015), Babtunde and Akeju (2016), Johanes et al. (2016), Muhammad (2017), Saladin (2018), Selly (2019), prove that GCG has a positive and significant effect on profitability. This shows the better implementation of GCG through a mechanism and transparency system, the ability to increase the profit (profitability) of the company is getting better. However, according to research from Hidayat et al. (2014) and Wang (2014) the board of commissioners has a negative and significant relationship to profitability.

II. LiteratureReview

Good Corporate Governance (GCG) is a set of regulations that establish the relationship between shareholders, management, creditors, government, employees and other internal and external stakeholders with respect to their rights and obligations, or in other words a system that directs and controls company. Transparency, accountability, responsibility, independence are the principles of GCG (Hidayah, 2008). According to the National Committee on Governance Policy (KNKG) (2006), GCG has six main objectives: (a) Encouraging the achievement of company sustainability through management based on the principles of transparency, accountability, responsibility and fairness and equality. (b) Encouraging the empowerment of the functions and independence of each organ of the company, namely the board of commissioners, directors and general meeting of shareholders (GMS). (c) Encourage shareholders, members of the board of commissioners and directors to make decisions and carry out their actions based on high moral values and compliance with laws and regulations. (d) Encourage the emergence of awareness and corporate social responsibility towards the community and environmental sustainability, especially around the company. (e) Optimizing company value for shareholders by taking into account other stakeholders. (f) Increase the competitiveness of companies nationally and internationally so as to increase market confidence that can encourage investment flows and national economic growth and sustainability.

The capital structure is a mix of permanent (long-term) funding sources that the company uses to provide the results of a complete analysis of how the company utilizes the assets and at the same time spends those assets. (Mahwiyah et al. 2016: 1). The components of capital structure according to Sutrisno (2011: 324) include: (a) long-term debt, (b) own capital. capital structure of a company is influenced by many factors where the main factors are: (a) interest rates, (b) stability of "earnings", (c) composition of assets, (d) risk levels of assets, (e) magnitude the amount of capital required, (f) the state of the capital market, (g) the nature of management, (h) the size of a company.

Profitability is the ability of a company to make a profit expressed as a percentage. (Hasibun, 2007). The use of this ratio shows the efficiency of the company (Kasmir, 2014: 196). Profitability is used to measure the company's ability to generate profits at the level of sales, assets and certain share capital (Hanafi, 2014: 42). There are two types of profitability ratios according to Kasmir (2014: 197): (a). Profitability related to sales. (b) Profitability related to investment, consisting of Return on Investments-ROI and Return on Equity-ROE. Profitability according to Kasmir (2014: 197): (a) measuring or calculating the profits earned by the company in a certain period, (b) assessing the company's profit position the previous year with the current year, (c) assessing the development of earnings over time, (d) assess the amount of net profit after tax with own capital, (e) measure the productivity of all company funds used for both loan capital and own capital, (f) measure the productivity of all company funds used for own capital. Benefits of profitability: (a) know the level of profit earned by the company in one period, (b) know the company's profit position the previous year with the current year, (c) know the development of profits from time to time, e) know the amount of net profit after tax with owner's equity.

Earnings management is the involvement of management in preparing financial statements to maximize personal gain and profit of the company (Schipper, 2015: 92). Hasty and Herawaty (201) concluded that Scott divided the two ways of understanding earnings management that should be applied in a company, namely: earnings management as an opportunistic behavior, (2) efficient earnings management. Factors that become the driving force behind the occurrence of earnings management (Watt and Zimmerman, 2012), namely: (a) Bonus Plan Hypothesis. (b) Debt Covenant Hypothesis. (c) Political Cost Hypothesis. Earnings management pattern according to Scoot (2000) can be done by: (1) Taking a Bath. (2) Income Minimazation (3) Income Maximization. (4). Income Smoothing. (5). Offsetting extraordinary / unusual gains. (6) Aggressive accounting applications. (7) Timing Revenue and Expense Recognition. Earnings management can be done with three techniques (Halim, 2015) are: (1) Changes in accounting methods. (2) Playing accounting policies. (3) Shifting the period of cost or income.

Hypothesis

H1: Good Corporate Governance has a positive and significant effect on profitability.
H2: Capital structure has a positive and significant effect on profitability.
H3: Good Corporate Governance has a positive and significant effect on earnings management.
H4: Capital structure has a positive and significant effect on earnings management.
H5: Profitability has a positive and significant effect on earnings management.
H6: Good Corporate Governance has a positive and significant effect on earnings management through profitability.
H7: Capital structure has a positive and significant effect on earnings management through profitability.

III. ResearchMethods

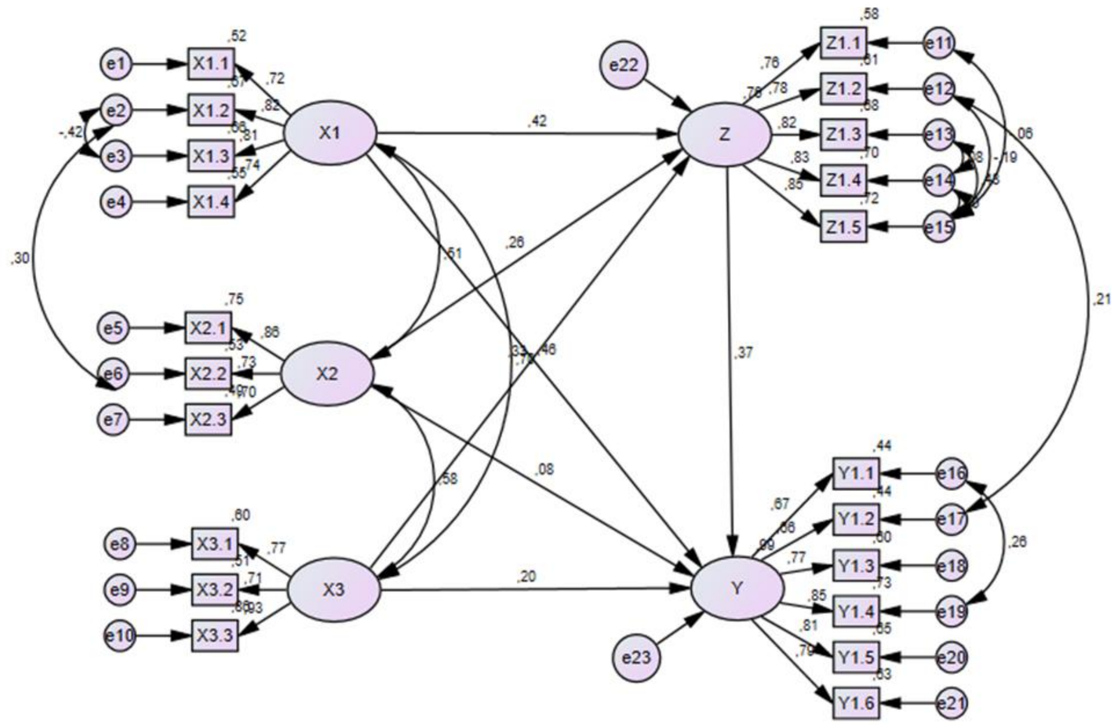
The approach taken in data collection is documentation. The location of this research was conducted at the Indonesia Stock Exchange by accessing data through the Indonesia Capital Market Directory via the IDX website. The object of research is manufacturing companies listed on the Indonesia Stock Exchange for the period of 2015 -2019. The population is 142 companies and the sample is 42 (210 sample units). The technique of sample collection is by purposive sampling. The analytical method uses the Structural Equauation Model (SEM) and SPSS-23. GCG indicators (X1) (commissioner size: X1.1; board of directors size: X1.2; audit commission size), capital structure (X2) (LtDER: X2.1, LtDAR: X2.2, DER: X2.3, DAR : X2.4), profitability (ROA: Y1 :, ROE: Y2, GPM: Y3, OPM: Y4, NPM: Y5, EP: Y6), earnings management (Jones modification model: Z1, accrual working capital model: Z2, De Angelo models: Z3)

IV. Research Results AndDiscussion

Descriptive Statistics, Confirmatory Factor Analysis, Goodness of Fit

Descriptive statistics indicate that the average value (μ) of each indicator is: X1.1 (4 people), X1.2 (5 people), X1.3 (3 people), X2.1 (38.90%), X2.2 (10.78%), X2.3 (85.27%), X2.4 (81, 25%), Y1 (8.81%), Y2 (12.78%), Y3 (24.68%), Y4 (9.49%), Y5 (8.19%), Y6 (8.18%), Z1 (0.004), Z2 (0.153), Z3 (0.003). Confirmatory Factor Analysis (CFA) shows that the indicators of each latent construct are valid and reliable (loading factor $\geq$ 0.7; Probability $\leq$ 0.05). Loading factor (Lf) and probability (P) for X1.1 (Lf = 0.782; P = 0,000), X1.2 (Lf = 0,900; P = 0,000, X1.3 (Lf = 0.827; P = 0,000), X2 .1 (Lf = 0.791; P = 0.000), X2.2 (Lf = 0.932; P = 0.000), X2.3 (Lf = 0.882; P = 0.000), X2.4 (Lf = 0.710; P = 0.000) , Y1 (Lf = 0,741; P = 0,000), Y2 (Lf = 0,784; P = 0,000), Y3 (Lf = 0,893; P = 0,000 (), Y4 (Lf = 0,879; P = 0,000), Y5 (Lf = 0,831; P = 0,000), Y6 (Lf = 0,894; P = 0,000), Z1 (Lf = 0,903; P = 0,000), Z2 (Lf = 0,849; P = 0,000), Z3 (Lf = 0,960; P = 0,000) Goodness of Fit showed that the model formed was in accordance with the conceptualization of the theory / sample observations, (x ^ (2) $\leq$182,587 &Cf = 104,128; p $\geq$0.05 &Cf = 0.089; RMSEA $\leq$0.08 &Cf = 0.038 ; GFI = 0.90 &Cf = 0.924; AGFI = 0.90 &Cf = 0.880; TLI = 0.95 &Cf = 0.986; CFI = 0.95 &Cf = 0.990).

Structural Model



V. Discussion of ResearchResults

The Effect of Good Corporate Governance (GCG) on Profitability

GCG has a positive and significant effect on profitability (P = 0.000 ,00.05 and loading factor = 0.407). So the statement from the first hypothesis is accepted. This means that as GCG increases the profitability increases. GCG gives a meaningful meaning to profitability. The results support the findings of Iqbal and Kakakel (2010), Rini and Ghozali (2012), Sukandar (2014), Elly et al. (2015), Babtunde and Akeju (2016), Johanes et al. (2016), Muhammad (2017), Saladin (2018), Selly (2019). Meanwhile, the findings of Sherly et al. (2016) proved that the board of commissioners had a significant positive effect on ROE, the board of directors had a significant positive effect on ROE, the audit committee had no significant effect on ROE. The findings from Hidayat et al. (2014) and Wang (2014) prove that the board of commissioners has a negative and significant relationship to profitability. Likewise, findings from Muhammad (2016) prove that: institutional ownership, managerial ownership, independent commissioners have a positive and significant effect on profitability; the board of commissioners and the board of directors have positive and not significant effect on profitability.

Effect of Capital Structure to Profitability

Capital structure has a positive and significant effect on profitability ($P = 0.007 \leq 0.05$ and loading factor = 0.224). So that the statement of the second hypothesis can be accepted. This means that the better the capital structure decision, the better the profitability. Capital structure provides meaningful meaning for profitability. The results support the findings of Ayad and Mustafa (2015); Narinder (2019) proves that capital structure has a positive and significant effect on profitability. The use of long-term debt incurs interest expense, thereby affecting tax savings and profitability. Likewise, the issuance of shares will cause dividends which will affect earnings.

The Effect of Good Corporate Governance (GCG) on Earnings Management

GCG has a positive and significant effect on earnings management ($P = 0.005 \leq 0.05$ and loading factor = 0.231) so that statements from the third hypothesis can be accepted. This means that the better the GCG, the better the earnings management. GCG gives a meaningful meaning to earnings management. The results support the findings of Tegar and Andri (2014) and Mawardi (2017) proving that GCG has a positive and significant effect on earnings management. Meanwhile, the findings from Eva and Moh. Khoiruddin. (2016) proved that institutional ownership, managerial ownership, board size and audit committee size had no significant effect on earnings management. A well-implemented GCG mechanism can minimize earnings management actions. This is due to good supervision of management performance

Effect of Capital Structure on Earnings Management

Capital structure has a positive and not significant effect on earnings management ($P = 0.071 \geq 0.05$ and loading factor = 0.134). So the statement from the fourth hypothesis is rejected. This means that the better the capital structure decision, the better the earnings management. Capital structure does not give meaning to the management of earnings management. The results support the findings of Dendi (2017), Alfitrah (2018), I ketut et al. (2015), proving that capital structure has no significant effect on earnings management. Meanwhile, findings from Obeidat et al. (2016); Novita (2017); and Sofia (2016) prove that there is a positive relationship between capital structure and earnings management. The optimal capital structure decision has no meaning for the shareholders. This is because earnings management actions are directly related to company profits.

Effect of Profitability on Earnings Management

Profitability has a positive and significant effect on earnings management (P = 0.000 ,00.05 and loading factor = 0.457). So the statement from the fifth hypothesis is accepted. This means that as profitability increases, actions to do earnings management increase. Profitability gives meaning to earnings management. The results support the findings of Dendi (2017) proving that profitability has a positive and significant effect on earnings management. Meanwhile, findings from I Ketut et al. (2015), Sofia (2016), Muhammad (2016), Novita (2017), Alfitrah (2018), proving that profitability has no significant effect on earnings management.

The Effect of Good Corporate Governance (GCG) on Profit Management through Profitability

GCG has a positive and significant effect on earnings management through profitability ($P = 0.002 \leq 0.05$ and loading factor = 0.203). So that the statement of the fifth hypothesis can be accepted. This means that profitability is increasing, so GCG and earnings management are getting better. Profitability provides a meaningful meaning as a mediation of GCG on earnings management. The results support the findings of Sofia (2016), Muhammad (2016), proving that there is a significant influence between GCG on earnings management mediated by profitability. The results of the study also show that the mechanism of supervision of management performance will provide high profitability and affect the implementation of earnings management optimally.

Effect of Capital Structures on Profit Management through Profitability

Capital structure has a positive and significant effect on earnings management through profitability ($P = 0.013 \leq 0.05$ and loading factor = 0.286). So that the statement of the fifth hypothesis can be accepted. This means that profitability is increasing, the capital structure decisions and better earnings management. Profitability provides a meaningful meaning as a mediation of the capital structure of earnings management. The results support the findings of Obeidat et al. (2016) shows that there is a positive relationship between capital structure and earnings management mediated by profitability. The results of this study also show that the policy for determining capital structure greatly influences the disclosure of actual profitability and ultimately reflects the existence of earnings management practices.

VI. Conclusions and Suggestions

(1) GCG and capital structure partially have a positive and significant effect on profitability; (2) GCG has a positive and significant effect on earnings management; (3) Capital structure has a positive and not significant effect on earnings management; (4) GCG and capital structure partially have a positive and significant effect on earnings management through profitability.

Suggestion

For Companies: Companies need to determine the optimal capital structure in order to reduce earnings management actions.Researchers will come: (a) GCG indicators can be expanded by adding GCG principles. (b) The object of research can be carried out at non-manufacturing companies.

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