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# EARNINGS QUALITY: AN EMPIRICAL STUDY ON INFRASTRUCTURE, UTILITIES, AND TRANSPORTATION SECTOR COMPANIES

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## Abstract

This research has high urgency given the current issues in the global business environment. Today, businesses around the world are faced with pressure to improve the quality of their financial statements in the context of increasingly stringent reporting standards and changes in accounting regulations.The primary aim of this research is to investigate the influence of profitability, leverage, and firm size on the integrity and reliability of financial earnings. This study encompasses the complete set of infrastructure, utilities, and transportation companies that were publicly listed on the Indonesia Stock Exchange (IDX) during the period spanning from 2020 to 2022. The researchers employed a purposive sampling technique to select a sample of 30 companies meeting the predetermined criteria. This approach led to the collection of 90 data points. The methodology employed in this study involves using the documentation technique, explicitly relying on secondary data obtained from financial statements. The data analysis technique employed encompasses multiple stages. The initial step in the analysis involves assessing the model's accuracy through various tests, including the Chow test, Hausman test, and Lagrange multiplier test. Subsequently, the classical assumption test is conducted, encompassing the multicollinearity and heteroscedasticity tests. Finally, the panel data regression equation is formulated, and hypothesis testing is performed using the Eviews 12 software. This research study presents empirical findings demonstrating a negative relationship between profitability and firm size with earnings quality while indicating a positive association between leverage and earnings quality.

**Keywords:** earnings quality, profitability, leverage, and firm size.

## *Abstrak*

*Penelitian ini memiliki urgensi yang tinggi mengingat isu-isu terkini dalam lingkungan bisnis global. Saat ini, bisnis di seluruh dunia dihadapkan pada tekanan untuk meningkatkan kualitas laporan keuangan mereka dalam konteks standar pelaporan yang semakin ketat dan perubahan peraturan akuntansi.Penelitian ini bertujuan menganalisis pengaruh profitabilitas, leverage, dan ukuran perusahaan pada keandalan serta kualitas laba. Lingkup studi mencakup seluruh perusahaan di bidang infrastruktur, utilitas, dan transportasi yang terdaftar di Bursa Efek Indonesia (BEI) selama periode 2020-2022. Peneliti menggunakan metode purposive sampling untuk memilih sampel dari 30 perusahaan yang memenuhi kriteria yang telah ditentukan, menghasilkan kumpulan data sebanyak 90 data. Metodologi penelitian ini menggunakan pendekatan dokumentasi, dengan mengandalkan data sekunder yang diambil dari laporan keuangan. Analisis data dilakukan melalui beberapa tahap, dimulai dari menguji ketepatan model dengan berbagai uji, termasuk uji Chow, uji Hausman, dan uji pengali Lagrange. Selanjutnya, dilakukan uji asumsi klasik, mencakup uji multikolinearitas dan heteroskedastisitas. Akhirnya, persamaan regresi data panel dibentuk, dan pengujian hipotesis dilakukan menggunakan perangkat lunak Eviews 12. Temuan empiris dalam penelitian ini mengindikasikan adanya korelasi negatif antara profitabilitas dan ukuran perusahaan dengan kualitas laba, sambil menunjukkan korelasi positif antara leverage dan kualitas laba. Penelitian ini juga mempertimbangkan perubahan regulasi terbaru dalam standar pelaporan keuangan di Indonesia, sehingga memberikan gambaran yang lebih komprehensif tentang situasi terkini.*

***Kata kunci:*** *kualitas laba, profitabilitas, leverage, and ukuran perusahaan.*

# INTRODUCTION

The number of companies listed on the Indonesian Stock Exchange (BEI) reflects that the capital market in Indonesia is experiencing development. It reflects the closing of the Composite Stock Price Index (IHSG) in 2020. The index closed at 5,979.07 or decreased by 0.95% in 2021. The index showed positive performance by increasing by 10.08%, reaching the position of 6,581.5, and in 2022, the index will close at 6,850.52 or an increase of 4.09%. According to the Investment Coordinating Board (BPKM), investment in Indonesia continues to increase from 826.3 in 2020 to 1,207 in 2022. The increase in the IHSG in Indonesia was also offset by an increase in investment in Indonesia, which reflects that investment in Indonesia is one of the best choices in the world.

Financial reports are a crucial source of information that is required by investors. Financial reports aim to provide accurate and verifiable information for investors, which is used to make investing decisions by looking at the company's profits. Net profit is an essential element of financial reports. Earnings quality can reduce capital costs, an essential element in investment decisions. Besides that, earnings quality can increase stock returns with a relationship to increased profits.

When the profits stated in the financial statements do not reflect the actual situation, then the quality of the profits will be in doubt. Financial reports have become an issue as a source of misuse of information that is detrimental to interested parties. A critical element so that investors do not make a mistake in choosing a company with quality earnings is that investors must pay attention to the criteria for good earnings quality. The efficacy of a company's profit quality can be observed through its ability to optimize operational performance and accurately forecast future performance effectively. Utilizing this metric serves as a means of evaluating the performance of a corporation.

The researchers conducted an assessment to explore the influence of profitability, leverage, and firm size on the quality of earnings in publicly listed infrastructure, utility, and transportation companies on the Indonesia Stock Exchange based on their preliminary findings.


Figure 1. Trend of Average Earnings Quality Values 2020-2022

Source: www.idx.co.id (Data processed, 2023)

Figure 1 depicts the fluctuations in profitability measures across the infrastructure, utilities, and transportation sub-sectors as documented on the Indonesian Stock Exchange from 2020 to 2022. This phenomenon exhibits a deficiency in the persistence of profitability, raising concerns about the company's ability to sustain the quality of its profits. High and low earnings quality can affect investor confidence in the company. Thus, companies need to produce good quality earnings to maintain investor confidence so they continue to invest in the company. When considering the long-term sustainability of a company, it is crucial to conduct an examination of the various factors that influence the quality of its earnings.

Profitability refers to the evaluation of a company's capacity to generate earnings or financial gains within a specific timeframe. Companies that exhibit strong profitability have the ability to attract investors and secure investments. Previous research has confirmed that there exists a positive

relationship between profitability and the quality of earnings (Anggraeni & Widati, 2022; Ardianti, 2018; M. Aslam & Tjakrawala, 2023; Kurniawan & Suryaningsih, 2017; Nirmalasari & Wahyu Widati, 2022; Putu et al., 2022). In contrast, other research results show that profitability does not significantly impact the quality of earnings (Agustin, 2022; Imad et al., 2017; Laoli et al., 2019).

One of the key determinants impacting the quality of earnings is the level of leverage employed by companies. When companies have high leverage, it can diminish investor confidence in the profitability of the company and instill apprehension among investors regarding potential investments. Consequently, this can result in a relatively subdued market response. Previous research states that leverage has a positive effect on earnings quality. However, different results were shown that leverage does not affect earnings quality (Abidin et al., 2022; Al-Vionita & Asyik, 2020; Laoli & Herawaty, 2019; Marpaung, 2019; Wati, 2017).

The company's size can also impact the quality of earnings. Company size pertains to the quantitative evaluation of a company's magnitude, encompassing various indicators such as total assets, total sales, average total sales, and average total assets. Investors typically exhibit greater confidence in large corporations. Large corporations are perceived as having the ability to enhance their organizational performance by striving to enhance the quality of their earnings. Large corporations are commonly perceived to possess a more significant amount of information compared to their smaller counterparts. There exists a positive correlation between the size of a company and the quality of its earnings (Firdaus & Trisnaningsih, 2023; Liu & Skerratt, 2018; Phuong et al., 2020; Purnamasari & Fachrurrozie, 2020; Putu et al., 2022; Sari & Wiyanto, 2022). In contrast, it shows that company size does not affect earnings quality (Anggraeni & Widati, 2022; Ramadhan & Zulaihati, 2023; Rosiana Dewi & Fachrurrozie, 2021; Telaumbanua & Purwaningsih, 2022).

## LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

### Agency Theory

According to Jensen & Meckling (1976), agency theory is an agreement between two or more parties consisting of an agent and a principal. Agency theory provides an explanatory framework for understanding the dynamic between the capital owner, referred to as the principal, and the management, known as the agent. The utilization of agency theory by companies is imperative as it serves as the fundamental framework for addressing the requirements of the organization by engaging external parties who possess the capacity to effectively promote the fulfilment of these needs.

### Stakeholder Theory

According to Freeman (1984), stakeholder theory defines the company stakeholders, including all parties affected by the company, which is the main reason for the company's development. This theory describes a company's environment as a diversity of related groups, all of which need to be considered and catered for to ensure the company's healthy development and success in the long term. Stakeholders include employees, customers, suppliers, political action groups, local communities, media, and government groups. Freeman (1984) put forward stakeholder theory, which means that in achieving goals, not just seeking profits, companies need to pay attention to, balance, and fulfil the expectations of all stakeholders.

### Earnings Quality

According to Warrad (2017), the concept of earnings quality refers to the capacity of reported profits to serve as a reliable predictor of forthcoming cash flows. Quality accounting profits are profits that can minimize perceived disturbances and are free from manipulated profits (discretionary accruals). Kurniawan & Suryaningsih (2019) also argue that high-quality earnings are earnings that can reflect sustainable earnings, the amount can be maintained in the future, and can also obtain relevant information used in decision-making that can vary, persistent, predictive, and can increase profits generated in the future.

### Profitability

According to Yulianis et al. (2019), profitability is characterized as the capacity of an entity or organization to generate financial gains. The assessment of a company's profitability can be ascertained through the comparison of the generated profits with the invested funds in assets or company equity.

The utilization of Return On Assets (ROA) as a metric in this study is justified due to its ability to elucidate the efficacy of leveraging company-owned assets to generate profits.

**Leverage**

Marpaung (2019) defines leverage as using fixed-cost financing (such as debt and preferred shares) to expand ratios and returns. Setiawan (2017) stated that leverage is a company's ability to use externally borrowed funds to finance its operations. Suppose the company bears many burdens or costs (such as fixed operational and financial costs). In that case, the company will always face leverage problems.

**Firm Size**

Firm size is a metric that provides insight into categorizing a company's magnitude. The magnitude of a company's aggregate assets indicates its capacity to engage in innovative practices for organizational growth and yield substantial returns, thereby eliciting a favourable response from investors. According to Subramaniam (2019), determining company size involves the computation of the natural logarithm of the aggregate value of total assets. The quantification of assets possessed by a company can serve as a metric for evaluation. The performance of a company can be influenced by its size. The expansion of the company's scale will indirectly impact its business continuity, as evidenced by the upward trend in its financial performance.

**Profitability and Earnings Quality**

The correlation between profitability and earnings quality is of considerable importance, as it functions as a reliable metric for assessing a company's capacity to generate favorable financial gains. Therefore, it functions as a crucial determinant in the decision-making process for investors. There is a direct association between the profitability level of a company and the tendency of investors to hold onto their shares in the company. According to Kurniawan and Suryaningsih (2019), there exists a positive correlation between the return on assets (ROA) and the generated profit. There is a discrepancy between the findings of Laoli and Herawaty (2019) and the present study, as their research suggests that the metric of profitability, specifically return on assets (ROA), has an adverse effect on the integrity of earnings.

$H_1$: Profitability has a significantly positive effect on earnings quality

**Leverage and Earnings Quality**

A company that possesses a significant degree of leverage has the ability to utilize its debt in order to finance its day-to-day business operations. Consequently, it is probable that such a company will generate higher levels of profitability, which can then be allocated towards the repayment of its outstanding debt obligations. Therefore, leverage that has a high value will be responded to positively by the company so that the profits generated will be of higher quality. Quality profits do not require earnings management because earnings management will harm creditors. The aforementioned explanation is substantiated by the findings of a study conducted by Warrad (2017), indicating that leverage has a notable and positive impact on the quality of earnings.

$H_2$: Leverage has a significantly positive effect on earnings quality

**Firm Size and Earnings Quality**

The relationship between firm size and earnings quality can be attributed to the notion that larger companies possess a greater capacity to generate investor interest, as they are presumed to have a stronger motivation to exhibit more sophisticated and rigorous financial reporting practices. In line with the findings of Kurniawan and Suryaningsih (2019), it can be argued that the magnitude of a firm has a

detrimental impact on the quality of its earnings. The correlation between company size and profit generation does not necessarily indicate a direct and accurate reflection of the prevailing circumstances.
$H_3$: Firm Size has a significantly positive effect on earnings quality

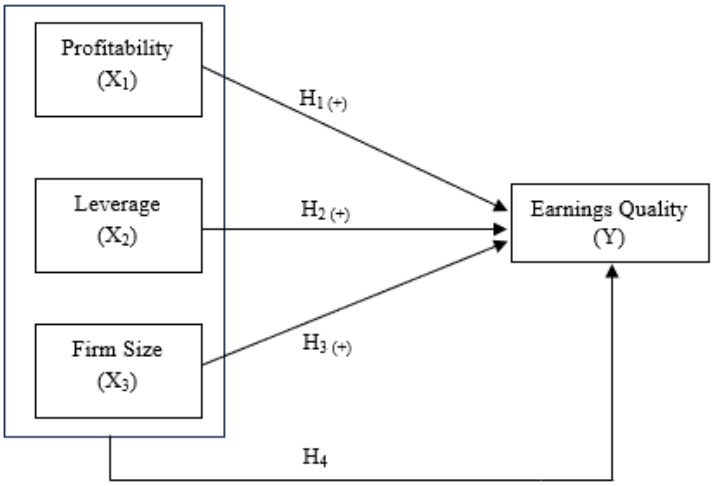


Figure 2. Research Model
Source: (data processed, 2023)

## RESEARCH METHODS

The present study employs a causal research design, utilizing a quantitative methodology. The research utilized secondary data in the form of company financial reports from the infrastructure, utilities, and transportation sectors. The data spanned from 2020 to 2022 and was obtained from the official databases of IDX and OJK. The sampling technique used is purposive sampling with sample criteria. Table 1 shows the criteria include:

Table 1. Data Criteria

| No | Criteria | Total |
|---|---|---|
| 1 | This study examines the companies operating in the infrastructure, utility, and transportation sectors that are listed on the Indonesia Stock Exchange (IDX) during the period from 2020 to 2022. | 100 |
| 2 | During the period from 2020 to 2022, there are companies operating in the infrastructure, utility, and transportation sectors that demonstrate inconsistency in their release of annual reports. | (11) |
| 3 | During the period spanning from 2020 to 2022, companies operating within the infrastructure, utilities, and transportation sectors that refrain from utilizing the Indonesian currency, known as the rupiah, will be examined. | (25) |
| 4 | This research investigates the financial performance of companies within the infrastructure, utilities, and transportation sectors, with a particular emphasis on the losses they reported between 2020 and 2022. | (34) |
| The samples in this study | | 30 |
| Periods (2020-2022) | | 3 |
| Sample data used | | 90 |

Source: data processed (2023)

The dataset will be processed and processed using the help of Eviews 12 software. The data analysis technique carried out consists of several stages. The initial step in evaluating the model accuracy involves conducting several tests, including the Chow test, Hausman test, and Lagrange multiplier test. Subsequently, the classical assumption test is performed, which encompasses the multicollinearity test and heteroscedasticity test. Finally, the panel data regression equation and hypothesis testing are employed. Normality and autocorrelation assumption tests were carried out in

this study, which states that in panel data regression testing, these two assumption tests are not necessary (Ekananda, 2016; Ghasemi & Zahediasl, 2012; Gujarati & Porter, 2008).

Table 2. Variable Measurement

| Variable | Operational Definition | Measure | Scale |
|---|---|---|---|
| Earnings Quality (Y) | Earnings quality refers to a company's capacity to maintain consistent levels of consumption over a given period. | QIR = CFO/NI<br>QIR = Quality of Income Ratio<br>CFO = Cash flow from operations<br>N.I. = Net Income | Ratio |
| Profitability ($X_1$) | Profitability refers to a company's capacity to generate profits through the demonstration of its performance. | ROA = (EAT/TA) x 100%<br>ROA = return on assets ratio<br>EAT = Earnings after tax<br>T.A. = Total asset | Ratio |
| Leverage ($X_2$) | Leverage is a financial metric utilized to assess a company's reliance on creditors for the purpose of financing its corporate assets. | DAR = (TU/TA) x 100%<br>DAR = Debt to Asset Ratio<br>T.U. = Total Debt<br>TA = Total Asset | Ratio |
| Firm Size ($X_3$) | The magnitude of a firm can be assessed by examining its income, total assets, and total equity. | Size = Ln Total Asset<br>Size = Firm size<br>Ln Total Asset = Natural Logarithm of Total Assets | Ratio |

Source: Data processed (2023)

# RESULT AND DISCUSSION

### Model Selection Test

Table 3 shows the chow test results, a model comparison test between the standard and fixed effect models. This test uses the cross-section F significance value parameter, which shows 0.0232, meaning that the model chosen is the fixed effect model because the significance value is smaller than 0.05 (Ghozali & Ratmono, 2020).

**Table 3. Chow Test**

Redundant Fixed Effects Tests
Equation: Untitled
Test cross-section fixed effects

| Effects Test | Statistic | d.f. | Prob. |
|---|---|---|---|
| Cross-section F | 1.855930 | (29,57) | 0.0232 |
| Cross-section Chi-square | 59.838635 | 29 | 0.0006 |

**Source: Eviews Output (2023)**

Table 4 shows the results of the Hausman test, a model comparison test between the fixed and random effect models. The test uses the random cross-section significance value parameter, which shows 0.8212, meaning that the model chosen is the random effect model because the significance value is more significant than 0.05 (Studenmund, 2017).

**Table 4. Hausman Test**

Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section random effects

| Test Summary | Chi-Sq. Statistic | Chi-Sq. d.f. | Prob. |
|---|---|---|---|
| Cross-section random | 0.917597 | 3 | 0.8212 |

**Source: Eviews Output (2023)**

To reconfirm, the model to be determined is the Lagrange multiplier (L.M.) test, a model comparison test between the random and standard effect models. Table 5 shows the results of the L.M. test with the Breusch-Pagan cross-section significance value parameter showing 0.0374, meaning that the model chosen is the random effect model because the significance value is smaller than 0.05 (Studenmund, 2017).

**Table 5. Lagrange Multiplier Test**

Lagrange Multiplier Tests for Random Effects
Null hypotheses: No effects
Alternative hypotheses: Two-sided (Breusch-Pagan) and one-sided (all others) alternatives

| | Test Hypothesis Cross-section | Time | Both |
|---|---|---|---|
| Breusch-Pagan | 4.333668 (0.0374) | 0.236559 (0.6267) | 4.570227 (0.0325) |
| Honda | 2.081746 (0.0187) | 0.486374 (0.3134) | 1.815935 (0.0347) |
| King-Wu | 2.081746 (0.0187) | 0.486374 (0.3134) | 0.999187 (0.1589) |
| Standardized Honda | 2.376641 (0.0087) | 1.116381 (0.1321) | -2.271394 (0.9884) |
| Standardized King-Wu | 2.376641 (0.0087) | 1.116381 (0.1321) | -1.180251 (0.8810) |
| Gourieroux et al. | -- | -- | 4.570227 (0.0417) |

**Source: Eviews Output (2023)**

**Assumption Classic Tests**

A multicollinearity test was conducted to ensure no high correlation between independent variables. Table 6 shows a high correlation between the ROA and leverage variables. It was seen that the centred VIF value of the ROA and leverage variables is greater than 10, which means there are multicollinear symptoms (Ghozali & Ratmono, 2020). So that this assumption is fulfilled and testing can be continued, it is necessary to transform the data on the two variables. Data transformation in this study uses a log function mechanism (logarithm) on ROA and leverage variables.

**Table 6. Multicollinearity Test (pre-transform)**

Variance Inflation Factors
Sample: 1 90
Included observations: 90

| Variable | Coefficient Variance | Uncentered VIF | Centred VIF |
|---|---|---|---|
| C | 57.19676 | 194.8850 | NA |
| X1 | 53.15256 | 10976.98 | 10836.38 |
| X2 | 1.919235 | 10963.70 | 10816.25 |
| X3 | 0.070634 | 196.6098 | 1.204363 |

**Source: Eviews Output (2023)**

Table 7 shows that after transforming the data using the log function (logarithm), the symptoms of multicollinearity have been resolved. The VIF values for the ROA and leverage variables are below 10, indicating the absence of multicollinearity among the independent variables. Consequently, it is reasonable to proceed with further tests (Ghozali & Ratmono, 2020).

**Table 7. Multicollinearity Test (post-transform)**

Variance Inflation Factors
Sample: 1 90
Included observations: 90

| Variable | Coefficient Variance | Uncentered VIF | Centred VIF |
|---|---|---|---|
| C | 43.79812 | 169.0272 | NA |
| LOG(X1) | 0.143802 | 6.826576 | 1.149780 |
| LOG(X2) | 0.299331 | 2.084083 | 1.101370 |
| X3 | 0.055768 | 175.8204 | 1.077014 |

**Source: Eviews Output (2023)**

**Heteroscedasticity Test**

The heteroscedasticity test is a statistical procedure employed to examine the hypothesis that the variability of the dependent variable does not remain constant across all levels of the independent variables within a regression model. This test seeks to assess the presence of instability or non-uniform variation in the dependent variable as the independent variable changes value.

Table 8 shows the heteroscedasticity test results with the Breusch-Pagan-Godfrey approach using the chi-square significance parameter. The results show that the chi-square significance value is 0.1671, which is more significant than 0.05, meaning that the data does not experience symptoms of heteroscedasticity or is homogeneous (Ghozali & Ratmono, 2020).

**Table 8. Heteroscedasticity Test**

Heteroskedasticity Test: Breusch-Pagan-Godfrey
Null hypothesis: Homoskedasticity

| | | | |
|---|---|---|---|
| F-statistic | 1.709676 | Prob. F(3,86) | 0.1710 |
| Obs*R-squared | 5.065482 | Prob. Chi-Square(3) | 0.1671 |
| Scaled explained SS | 38.01045 | Prob. Chi-Square(3) | 0.0000 |

**Source: Eviews Output (2023)**

**Re-Selection Model Test**

Following the data transformation of the ROA and leverage variables, it becomes imperative to reassess the accuracy of the model. The results of the Chow test, as presented in Table 9, indicate a

cross-section F significance parameter of 0.0023. This value is below the conventional threshold of 0.05, leading to the conclusion that the fixed effect model is selected.

**Table 9. Chow Test (post-transform)**

Redundant Fixed Effects Tests
Equation: Untitled
Test cross-section fixed effects

| Effects Test | Statistic | d.f. | Prob. |
|---|---|---|---|
| Cross-section F | 2.404076 | (29,57) | 0.0023 |
| Cross-section Chi-square | 71.902309 | 29 | 0.0000 |

**Source: Eviews Output (2023)**

The subsequent step entails conducting a comparative analysis between the fixed model and the random effect model. The results of the Hausman test are presented in Table 10. The random cross-section significance parameter is reported to be 0.0119, which is below the conventional threshold of 0.05. This suggests that the fixed effect model has been chosen as the ultimate model.

**Table 10. Hausman Test (post-transform)**

Correlated Random Effects - Hausman Test
Equation: Untitled
Test cross-section random effects

| Test Summary | Chi-Sq. Statistic | Chi-Sq. d.f. | Prob. |
|---|---|---|---|
| Cross-section random | 10.963794 | 3 | 0.0119 |

**Source: Eviews Output (2023)**

**Regression Equation Model and Hypothesis Test**

After going through the process of testing the accuracy of the model and classical assumptions, the linear-log or semilog regression equation model is obtained. Table 9 shows the following equation:

$$Y = a + b_1(\log X_1) + b_2(\log X_2) + b_3(X_3) + ei$$

(Studenmnund & Johnson, 2017)

$$Y = 27.96098 - 2.730027\ (ROA) + 3.348\ (leverage) - 1.033345\ (size)$$

**Table 11. The Panel Data Regression**

Dependent Variable: Y
Method: Panel EGLS (Cross-section weights)
Sample: 2020 2022
Periods included: 3
Cross-sections included: 30
Total panel (balanced) observations: 90
Linear estimation after one-step weighting matrix

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| C | 27.96098 | 10.94600 | 2.554448 | 0.0133 |
| LOG(X1) | -2.730027 | 0.201078 | -13.57693 | 0.0000 |
| LOG(X2) | 3.348558 | 0.539300 | 6.209081 | 0.0000 |
| X3 | -1.033345 | 0.392518 | -2.632608 | 0.0109 |

| Effects Specification | | | |
|---|---|---|---|
| Cross-section fixed (dummy variables) | | | |
| Weighted Statistics | | | |
| Root MSE | 3.122022 | R-squared | 0.884235 |
| Mean dependent var | 17.04641 | Adjusted R-squared | 0.819245 |
| S.D. dependent var | 27.01828 | S.E. of regression | 3.923014 |
| Sum squared resid | 877.2321 | F-statistic | 13.60556 |
| Durbin-Watson stat | 2.581364 | Prob(F-statistic) | 0.000000 |
| Unweighted Statistics | | | |
| R-squared | 0.678823 | Mean dependent var | 4.159524 |
| Sum squared residual | 910.4553 | Durbin-Watson stat | 2.722083 |

Source: Eviews Output (2023)

The t-statistic test results and the significance of the ROA variable are displayed in Table 11. The calculated t-statistic value of -13.57693 surpasses the critical t-value of -1.987, while the corresponding significance value of 0.000 is lower than the conventional threshold of 0.05. The findings of this study support the acceptance of the alternative hypothesis, indicating a statistically significant inverse association between return on assets (ROA) and earnings quality. The t-statistic test results and the significance of the leverage variable, as presented in Table 11, indicate a value of 6.209081. The obtained value surpasses the critical value of 1.987 derived from the t-table. The observed significance level is less than 0.05, specifically 0.000. Therefore, it can be deduced that the alternative hypothesis is supported, indicating a statistically significant positive correlation between leverage and earnings quality.

The results obtained from the t-statistic test and the significance analysis of the size variable in Table 11 indicate a value of -2.632608, which exceeds the critical t-value of -1.987. Moreover, the significance level of 0.0109 is observed, which is below the conventional threshold of 0.05. This suggests that the alternative hypothesis is upheld, indicating a statistically significant detrimental impact of the size variable on the quality of earnings.

In addition, the F test produces a significance value of 0.000, suggesting a statistical significance level that is lower than the commonly accepted threshold of 0.05. This suggests that the variables of return on assets (ROA), leverage, and firm size collectively exert a substantial influence on the quality of earnings.

**Coefficient of Determination**

The coefficient of determination is a statistical measure used to assess the degree to which the regression model can account for variations in the data or the degree to which the independent variable can elucidate the dependent variable. The parameter employed in this study is the adjusted R-square value, which signifies the extent to which the independent variables can account for the variability in the dependent variable. A higher adjusted R-square value, closer to 1 or 100%, suggests a more robust regression model with a better fit to the data. Table 11 presents the adjusted R-square value of 0.8192, indicating a high goodness of fit for the regression model employed in this study. Additionally, the findings indicate that the impact of return on assets (ROA), leverage, and firm size on earnings quality accounts for 81.92%. The remaining outcomes are potentially impacted by additional variables that were not investigated within the scope of this study.

# DISCUSSION

**Profitability and Earnings Quality**

Profitability has a significant negative effect on earnings quality. It shows that companies with low profitability are suspects of implementing earnings management practices. Apart from that, profitability does not reflect quality company profits and does not necessarily reflect the company's financial reports.

This evidence demonstrates that a company exhibiting a high degree of profitability possesses the capacity to generate escalating levels of financial gains. The attainment of high profitability has the potential to yield favorable returns on investments made by investors.

The findings of this study are consistent with the prior investigations which assert that profitability exerts a favorable influence on the quality of earnings (Anggraeni & Widati, 2022; Ardianti, 2018; U. Aslam, 2023; Kurniawan & Suryaningsih, 2017; Nirmalasari & Wahyu Widati, 2022; Putu et al., 2022). In the realm of scholarly inquiry, a body of research conducted by Agustin and Rahayu (2022), Laoli and Herawaty (2019), and Aughniem et al. (2017) has yielded findings indicating that there exists no discernible impact of profitability on the quality of earnings.

**Leverage and Earnings Quality**

The presence of profitability has a notable and favourable impact on the quality of earnings. The statement aligns with stakeholder theory, which posits that as a company's leverage increases, its obligation towards creditors also intensifies. Consequently, the company is compelled to enhance its performance to generate higher profits, thereby achieving equilibrium and fulfilling the expectations of all stakeholders.

The results of this research are in line with research by Aslam & Tjakrawala (2023), Salsabillah & Aufa (2023), Alvin & Susanto (2022), Purnamasari & Fachrurrozie (2020); Aughniem et al. (2017); Warrad (2017) state that leverage has a positive effect on earnings quality. Meanwhile, research conducted by Abidin et al. (2022), Asyik (2020), Laoli & Herawaty (2019), Marpaung (2019), and Wati & Putra (2017) shows that leverage does not affect earnings quality.

**Firm Size and Earnings Quality**

The size of a firm exhibits a notable adverse impact on the quality of earnings. Expanding a company's size has implications for business continuity regarding enhancing financial performance and mitigating the risk of engaging in financial statement manipulation practices. The magnitude of a company can be gauged by the aggregate value of its assets, thereby enabling a larger-sized company to generate earnings of superior quality. Larger corporations can effectively uphold and potentially enhance the organization's financial standing, thereby circumventing the adoption of earnings management techniques.

The results of this research are in line with research by Firdaus & Trisnaningsih (2023), Sari & Wiyanto (2022); Sumertiasih & Yasa (2022); Anam & Afrohah (2020); Phuong et al. (2020); Purnamasari & Fachrurrozie (2020); According to Liu and Skeratt (2018), there exists a positive correlation between the size of a company and the quality of its earnings. In contrast to research conducted by Ramadhan et al. (2023), Anggraeni & Widati (2022), Telaumbanua & Purwaningsih (2022), and Dewi & Fachrurrozie (2021) shows that company size does not affect earnings quality.

# CONCLUSION

This study concludes that there is a negative correlation between profitability and firm size on earnings quality, while the application of leverage positively impacts earnings quality. Companies consider profitability, leverage, and firm size essential in improving their earnings quality. Increased profitability and growth in firm scale can result in high-quality earnings, especially for firms with high rates of return that can allocate financial resources efficiently. Lower leverage can improve earnings quality by reducing debt obligations. Investors should be careful in assessing financial statement information and always follow Indonesia's latest accounting standards. This study recommends using more variable measurements and suggests future research to expand the sample to various sectors to increase sample diversity.

# RECOMMENDATION

**Practical**

Investors must be careful in assessing the information provided by the company in the financial statements issued by the IDX, including looking at the company's activities in generating profit, asset utilization, and operating activities. The research results provide investors with a valuable tool to assess the financial health of businesses. From there, investors can invest more accurately and reasonably based on the available data. In addition, companies and investors are advised to keep updating the latest

information according to the accounting standards in Indonesia. For credit institutions, the determination of Earnings Quality is related to leverage, partly in considering the ability to earn income to repay loan contracts and minimize potential risks in the business operations. When Earnings Quality is appreciated, the enterprise can generate income to meet loan conditions.

**Theoretical**

Future studies suggest using other measures such as institutional ownership, corporate social responsibility (CSR), managerial ownership, and investment opportunity set to see their effect on earnings quality. Future researchers are expected to add other sectors over a more extended period to compare and expand knowledge in decision-making, especially for investors and creditors. Finally, the study suggests testing different features of earnings quality, such as earnings persistence and smoothness.

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