-RESEARCH ARTICLE-

GOOD CORPORATE GOVERNANCE, AUDIT TENURE, AND THEIR JOINT EFFECT ON EARNINGS MANAGEMENT: EVIDENCE FROM INDONESIAN LISTED FIRMS

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─**Abstract**─

The paper examines the effect of corporate governance and audit tenure on earnings management among Indonesian Stock Exchange (IDX)-listed firms. The paper examines how the corporate governance mechanisms, as gauged by the Corporate Governance Index (CGI), and the audit tenure, affect the probability of earnings management, in the background of an emerging market. In particular, the paper will evaluate the possibility of reducing the possible adverse impacts of longer audit tenures on earnings management by stronger governance structures. Through regression models and data of Indonesian firms in a 10-year period between 2010-2020, the results show that although the positive association of higher CGI scores with better governance practices is common, it does not always result in lower earnings management. Actually, tight governance structures can also co-exist with opportunistic earnings manipulation as a result of symbolic compliance or low enforcement. The paper also indicates that longer audit term increases earnings management, especially in firms with poorly developed systems of governance. The findings also add to the literature by illuminating on the multifaceted interplay between corporate governance and audit tenure in influencing earnings management. The results have significant policy implications on policy makers and regulators in the emerging markets, with the fact that there should be more governance controls and the audit tenure should be well managed so as to promote more financial transparency and less earnings manipulation.

Keywords: Corporate Governance Index, Audit Tenure, Earnings Management, Indonesian Stock Exchange.

INTRODUCTION

Earnings management (EM) refers to the deliberate act of altering financial reports by a management with the aim of fulfilling certain financial objectives, including fulfilling earnings expectations or the stock market impressions. EM is a controversial practice in the framework of financial reporting (Miletić & Radić, 2022). Although a certain level of EM could be acceptable under accounting rules, such as smoothing of income or deferral of revenue, extreme EM would misrepresent the true financial performance of a company and mislead investors, creditors, and other stakeholders (Burlacu et al., 2024; Ghosh, 2025). The EM may be of different types, such as, accounting estimates, expenses shifting, or the premature recognition of revenues.

Despite the fact that EM, when used properly, may be a valid instrument in some cases, its excessive use or misuse contravenes the confidence factor that investors and stakeholders have in financial statements, which is inefficient in the market and influences the option of capital allocation.

The issue of EM is especially alarming in the emerging economies such as Indonesia where the financial markets are only developing. After the Asian Financial Crisis of 1997-1998 that caused major changes in corporate governance (CG), Indonesia has made some attempts to enhance its regulatory environment. Such initiatives were to increase transparency, accountability and reduce unethical conducts like earnings manipulation. Nevertheless, even with these advancements, EM continues to be a problem, particularly in the family-controlled companies where ownership and control issue are often centralized, and the independence of the board of directors is at risk (Gavana et al., 2025; Helal, 2022; Prencipe & Bar-Yosef, 2011).

CG is considered an important tool in regulating the EM by making sure that the decisions of the managers are in line with the interest of the shareholders. The independent board of directors, effective audit committees, and effective internal controls ensure good CG practices that offer the required control over the discretion that managers have in the manipulation of earnings. A corporate governance Index (CGI) is one of the measures of the quality of CG that is widely used and that combines various measures of governance such as board composition, shareholder rights, and the effectiveness of the audit committee (Abdallah, 2021). An increase in CGI score usually implies a better system of governance, which is likely to restrain managerial opportunism and decrease the EM (Shira, 2025).

There is a strong CG framework, including independent boards, active audit committees, and clear shareholder rights, which are aimed at minimizing discretion of the managers in financial reporting. These mechanisms offer supervision, so that the decision taken by the managers are in line with the interests of shareholders and other stakeholders. This has been proven in earlier research showing that firms with larger CGI scores are less likely to manipulate their earnings. Indicatively, Nasiri and Ramakrishnan (2020) established that the more the CG rating of the Malaysian firms, the less the chances of EM because the presence of independent governance structures reduces EM opportunities. In a similar vein, Asghar et al. (2020) held that the better a firm practices its governance as indicated by a high score in CGI, the more reliable are the financial statements because the firm is subjected to stricter internal control and external audit. Based on these findings it is clear that effective governance mechanisms not only create transparency, but also enhance accountability of the management that is vital in deterring earnings manipulation.

Audit tenure is another aspect that is of concern in the quality of financial reporting and this is defined as the number of years that an audit firm has been working with a

firm. The connection between the audit tenure and EM is complicated. Prolonged tenures of the auditors can result in a more effective perception of the company by the auditor, which can increase the quality of the audit and decrease the manipulation of earnings (Alhazmi et al., 2024). Nevertheless, long-term relationships can also reduce the independence of the auditor, making the management more likely to engage in EM because of the excessive familiarity of the auditor with the management (Afzali et al., 2025; Nyongesa, 2025). Auditor independence risk due to long-term audit tenure is a vital factor that should be handled especially in the emerging markets where the regulatory frameworks are yet to be developed.

Long audit tenures can lead to the development of circumstances where the auditors, as they are familiar with the clients, lose their independence and are more willing to audit to the tastes of management in terms of financial reporting, which enhances the chances of EM. Ismael et al. (2025) discovered that long audit terms were positively related to the increased EM since long-term relationships between auditors and clients can decrease the objectivity of auditors. Santos Jaén et al. (2023) similarly contended that long term auditor-client relationships could lead to reduction in rigor of the audit, which increases likelihood of earnings manipulation. Kamarudin et al. (2022) also highlighted that in emerging markets, where regulation might not be that strict, the possibility of auditor independence being compromised is especially high, which increases the potential of EM. This shows the essence of controlling the audit tenure, especially in emerging economies, to ensure the independence of the auditor and minimized the risk of earnings manipulation.

When abused, EM is able to give a false impression of the actual financial condition of firms, which may result in poor capital allocation and financial instability. As a result, the role of CG and audit practices in determining the EM has been of great concern to both academicians and practitioners. The study is both theoretically and practically important. Theoretically, it adds to the body of literature on EM because it aims at the relationship between CG and audit tenure. Majority of the past studies have researched either CG or audit tenure separately but not many studies have addressed the interaction effects of both variables on EM especially in the emerging markets (Burlacu et al., 2024; Gavana et al., 2025; Nasiri & Ramakrishnan 2020; Prencipe & Bar-Yosef, 2011; Shira, 2025). This study builds on the current body of knowledge by studying the interaction of these two significant variables to determine their impact on the earning management. The Indonesian situation is especially fascinating due to the specific issues and problems that it experiences, such as the concentrated ownership, family-owned firms, and the comparatively lower adherence to the CG standards.

Additionally, the results of this research may be used by the policymakers, regulators and managers of companies in Indonesia. The relationship between CG and audit tenure can be understood to give an idea about the way CG structures can be enhanced

and the audit practice can be improved. On the same note, the findings may assist the corporate managers to design their governance systems more appropriately to minimize earnings manipulation and enhance overall quality of financial reporting. This study will be aimed at achieving the following objectives:

1. To test the effect of CG (measured by CGI) on EM in Indonesian listed companies on the IDX.
2. To determine how the tenure of the auditor influences the EM in these companies.
3. To explore the question on whether audit tenure and CG interacted with EM.

The paper will be structured as follows: Chapter 1 will give the background, research objectives and the significance of the study. Chapter 2 conducts a literature review on appropriate literature regarding CG, audit tenure, and EM. Chapter 3 provides a research methodology, which involves data sources, research design and data analysis. The results of the analysis are provided in Chapter 4 and discussed in terms of their implications. Chapter 5 is the last part of the study and summarizes all the main findings and provides the recommendations on how to conduct future research and policies.

LITERATURE REVIEW

EM, CG, and audit tenure are important areas of study that can help in understanding the quality and transparency of financial reporting particularly in developing economies such as Indonesia. The credibility of the financial information is gaining significance as the world financial markets are ever-expanding. When abused, EM is able to give a false impression of the actual financial condition of firms, which may result in poor capital allocation and financial instability. As a result, the role of CG and audit practices in determining the EM has been of great concern to both academicians and practitioners. Two major variables that are often discussed in the literature as affecting the EM are the CG Index (CGI) and audit tenure. This review aims at offering information on how CG and auditing standards can be enhanced to minimize earnings manipulation in the emerging economies by examining the relationship between these variables in the Indonesian context.

EARNINGS MANAGEMENT

EM is the intentional act of controlling financial reporting to reach certain objectives, including earnings expectations, stock prices, or matching financial performance with compensation of the management. Although the accounting standards allow certain types of EM, such as income smoothing or accrual adjustment, the excessive form of EM distorts the true financial performance of the company and confuses its stakeholders (Baskaran et al., 2020). There are two types of EM, namely accrual-based EM (AEM) and real EM (REM). AEM is characterized by the use of discretionary accruals including provisions of bad debts or depreciation schedules to

manipulate reported earnings. REM, however, is the actual operational decision-making, that is, postponing or increasing expenditures and revenues to achieve financial goals (Habib et al., 2022).

One of the biggest issues with EM is that it may destroy the credibility of financial reports. Over manipulation may result in information asymmetry where the investors and the stakeholders are misinformed on the financial performance of a company thereby affecting their capacity to make informed decisions (Stone et al., 2019). Consequently, the management of earnings has emerged as a very important field of research and a variety of theories have been put forward to explain the reasons behind the high number of firms practicing EM. The agency theory Meckling and Jensen (1976) assumes that the managers, who are the agents of the shareholders, can distort earnings to suit their interests, which include meeting their performance goals or their compensation maximization. According to the political cost theory Watts and Zimmerman (1978), it is mentioned that the perceived size of a firm can be minimized to avoid regulatory oversight or taxes through EM. EM in Indonesia is also still an issue, particularly in family-owned firms, where the management will have greater freedom to manipulate earnings without much control.

CORPORATE GOVERNANCE AND EARNINGS MANAGEMENT

CG is the system, process and practices used to manage the direction and control of companies. Good CG will ensure that the interests of the management are in line with those of the shareholders and the stakeholders, thereby minimizing chances of manipulating the earnings. Independent boards, audit committees and clear rights of the shareholders are some of the governance mechanisms that help to prevent opportunistic actions of the management. The CGI is one of the most popular proxies of the quality of CG, and it is a composite of various elements of governance, such as board composition, shareholder rights, and independence of the audit committee (Nguyen et al., 2024).

Empirical research has revealed that the more robust CG frameworks are related to the lesser amount of EM. Riyadh et al. (2024) discovered that companies that have a more independent board and good governance practices present quality financial statements and less EM. Utomo (2024) have identified in a study of Indonesian firms that the higher the CGI score was, the less the earnings were manipulated. Nevertheless, the success of CG in diminishing EM depends on the institutional environment in general. Family-controlled firms in Indonesia who constitute a major share of the market might be having weaker governance structures despite high CGI scores. This highlights the need to know that ownership structure may be an important factor, in regulating efficiency of governance systems in preventing earnings manipulation (Herdhayinta, 2020).

A bibliometric review of 20 years of the literature on the topic of EM and CG is

carried out by Chemmaa and Ibrahimi (2025). They examine patterns, methodology and geographical patterns, which shows that there is increased interest into how governance systems such as board independence and ownership structure affect EM. Other research areas that have been identified in the study include the effects of regulatory frameworks and market conditions on these practices. Similarly, Mismiwati et al. (2025) explore the connection between CG and EM in Indonesian publicly listed companies. Their empirical research is to investigate the effect of the governance mechanisms, including the board structure, ownership concentration, and the audit committees on the EM practices. The authors discover that the better CG, the less earnings manipulation, which indicates that efficient oversight and accountability systems can reduce opportunistic financial reporting. This research can be added to the literature that has been growing on the significance of governance in guaranteeing financial transparency, especially in emerging markets such as Indonesia.

H1: *CGI have negative impact on EM*

AUDIT TENURE AND EARNINGS MANAGEMENT

Another factor that affects the EM is audit tenure or the duration that an audit firm has been working with a company. On the one hand, the long audit periods can positively affect the quality of the audit by embedding in the auditor a better understanding of the functioning of the client, which can increase his or her chances regarding the detection of the misstatements or anomalies in the financial statements (Carp & Istrate, 2021). Conversely, a long-term auditor-client relationship can jeopardize the independence of the auditor since the auditors will be more familiar with the company and they will be less likely to question the financial reporting of the company (Carp & Istrate, 2021).

Audit tenure and EM do not have a direct relationship. Some studies have established that longer audit tenure is positively related to an increase in the EM. Ismael et al. (2025) discovered that the longer the audit tenure, the more the earnings manipulation, because the auditors have incentives to preserve the relationship with clients rather than ensuring strict auditing practices. On the same note, Kamarudin et al. (2022) found that long audit tenures have the potential in undermining the quality of the audit, which consequently enhances the chances of earnings manipulation. Nevertheless, according to other research, the extent of EM in cases of long audit tenure may not necessarily be higher when auditors are independent and objective (Deginet, 2025).

Audit tenure can have a special connotation in Indonesia, where the regulatory environment is not well-established yet. Pusparani et al. (2025) found that the longer the audit tenure of the company in Indonesia, the higher the EM, particularly in companies with poor governance systems. This shows that regulators should take great caution in regards to the effect of long audit tenure on quality of financial

reporting in emerging markets. Likely, Faradhifa and Handayani (2024) investigate the effects of information asymmetry, audit tenure, and size of a company on EM. They conclude that the more information asymmetry is high, the more it will be manipulated in earnings, whereas the longer the audit tenure the less it will be. Also, bigger firms have less tendency to practice EM because there is a greater level of governance and regulation. Mnif and Slimi (2024), examine the connection between the tenure of audit partners and EM in Vietnam. In their work, the authors conclude that the higher the duration of the audit partner tenure, the lower the earnings manipulation, which indicates that the acquaintance between auditors and their clients improves the quality of the audit and deters opportunistic financial reporting. The study is relevant to the current discussions on the impact of audit tenure on the quality of financial reporting, especially in the emerging economies such as Vietnam.

H2: *Long Audit Tenure increased EM, While Short Audit Tenure reduce EM*

CORPORATE GOVERNANCE INTERACTION WITH TENURE OF AUDIT

Despite the literature on the effects of CG and audit tenure on EM being examined separately, the interaction effect of the two has not been carefully examined. The interaction hypothesis holds that the risks of long tenure of audit committee can be alleviated by good CG practices. By adopting good governance frameworks, including independent boards and good audit committees, firms can have a mechanism of ensuring that the auditors are objective and independent, even when they have a long-term relationship with the management. These control systems assist in keeping control over them and decrease the possibility of earnings manipulations that could occur due to the long-term audit-client relationships.

On the other hand, the long tenure of auditors can enhance chances of earnings manipulation in firms that have weak governance structures because there is no independence of auditors. Under these circumstances, the auditors might get too close to the management and this might create conflict of interest or complacency that would prevent them to provide an objective evaluation of financial statements. (Sulieman et al., 2024) claim that the long audit engagement time in the context of deficient CG might only increase earning management practices because the auditors might have less motivation to question the decisions of the management or report the inconsistencies. In such a way, CG effectiveness in mitigating earnings manipulation is even more important in companies with a longer audit term. This highlights the necessity of having a holistic overview of the interplay between CG and audit tenure in affecting the integrity of financial reporting.

The role of this interaction has been emphasized in recent studies. Anam Iqbal et al. (2022) discovered that the existence of effective governance mechanisms greatly minimized the chances of earning manipulation, even in firms where audit experience

was long. In the same vein, Mnif and Slimi (2024) indicated that good CG would help to reduce the adverse consequences of long audit tenure on EM, specifically, in family-owned businesses in Indonesia. The proposed research will fill this gap by examining the interaction of CG, as used in CGI, and audit tenure on EM of the Indonesian firms. This study offers a special situation in the Indonesian market because it has experienced significant reforms in its regulations, yet, issues of family control and ineffective enforcement mechanisms remain.

H3: *CGI and Audit Tenure interaction reduce the EM*

LITERATURE GAP

Although there are extensive studies that have investigated the personal impacts of CG and audit tenure on EM, there are still key gaps in the studies. First, although CG has been found to have an impact on the EM due to their provision of oversight mechanisms (Gavana et al., 2025; Ismael et al., 2025; Nasiri & Ramakrishnan 2020; Nyongesa, 2025), little consideration has been given to the interplay of CG and audit tenure on the EM. The literature usually concentrates on the audit tenure or CG, and does not explore the interaction between the two variables, particularly in an emerging market setup.

Additionally, the literature on CG and EM has already found that the more effective the governance structure, including independent boards and strong audit committees, the lower the EM (Faradhifa & Handayani, 2024). Nevertheless, such studies do not give much focus on moderating factor of governance in relation between audit tenure and EM. In particular, the audit tenure that has been reported to influence EM due to its influence on the auditor independence has been examined independently without considering the role of effective CG that could affect or mediate this relationship (Deginet, 2025). With regard to audit tenure, various studies have shown that long audit tenure is positively correlated to the EM as the independence of auditors is weakened with time (Mnif & Slimi, 2024). The study of this association is however inconclusive and not enough evidence exists on how the CG practices especially in family-owned companies can reduce or increase the possible adverse impacts of long audit tenures.

Therefore, Indonesian setting provides a special context through which the gaps have been analyzed since the country has witnessed significant regulatory changes to enhance CG. Nonetheless, laxity of these laws, especially in the family-owned companies, still remains a problem. Moreover, the changing CG environment in Indonesia offers a chance to investigate how the practices of governance and tenure of an auditor can affect the EM, especially with the specific issues of corporate ownership structure and connections between auditors and clients.

RESEARCH METHODOLOGY

Data

The current research employed a quantitative research method to examine the association between EM and independent variables, such as CG and audit tenure, among listed companies on the Indonesian stock Exchange. The current study used the modified Jones model by Dechow et al. (1995) to measure EM, adjusted for performance (Kothari et al., 2005), due to high performance volatility in the Indonesian market. Therefore, construct a composite index from 1 to 100. Board structure and independence (Weight: 40%) Board independence percentage of independent directors on the board. Board size refers to the number of board members. The existence and independence of the audit committee are measured using a dummy variable (1 if independent members are present on the audit committee, zero if they are not) or the proportion of independent members on the audit committee. Further, the separation of the CEO and board chair is measured through a dummy variable (1 if separated, zero if dual). Both the parent company and the state possess this company (Weight: 30%). Institutional ownership refers to the percentage of shares held by institutional investors. Publicly available annual reports of companies listed on the Indonesian stock exchange provide data on variables such as CG components, audit tenure, interaction term of (CG*audit tenure), EM, and other control variables, including firm size, leverage, and profitability. Thus, this research employed secondary data from 2010 to 2024 to examine empirical findings.

Sample and Measurement of Variable

The present study considers all non-financial companies listed on the Indonesian stock exchange as the target population. As of November 2025, the Indonesian stock exchange had 954 listed companies with a total market capitalization of $855 billion. This data was collected from the annual reports of the 100 non-financial companies on the Indonesian stock exchange. The dependent variable is EM, measured using the modified Jones model by Dechow et al. (1995) adjusted for performance (Kothari et al., 2005), due to high performance volatility in the Indonesian market. Furthermore, the composite corporate index is constructed with the different components of CG like board structure and independence, board size, audit committee, and separation of the CEO, board chair, and institutional ownership. Moreover, the audit tenure measure is the number of years the current audit firm has been conducting audits. The current study employed to examine the interaction term of CG index and audit tenure. The variables and measurements are given in Table 1.

Table 1: Variables Description and Measurement

Variables	Code	Description and Measurement
Earning Management	EM	Measured using the Modified Jones Model (Dechow et al., 1995), adjusted for performance (Kothari et al., 2005) to account for high performance volatility in the Indonesian market.
Corporate Governance Index	CGI	Constructed from various CG components including board structure, board independence, board size, audit committee independence, CEO/board chair separation, and institutional ownership
Audit Tenure	AT	Measured as the number of years that the current audit firm has conducted audits for the company
Firm Size	FS	Measured as total assets or market capitalization
Leverage	LG	Measured as the ratio of total debt to total equity or total debt to total assets.
Profitability	OS	Measured by commonly used profitability ratios such as Return on Assets (ROA), Return on Equity (ROE), or Return on Sales (ROS).

The control variable data were also extracted from the annual report. The variables used in the study are presented in Figure 1 given below:
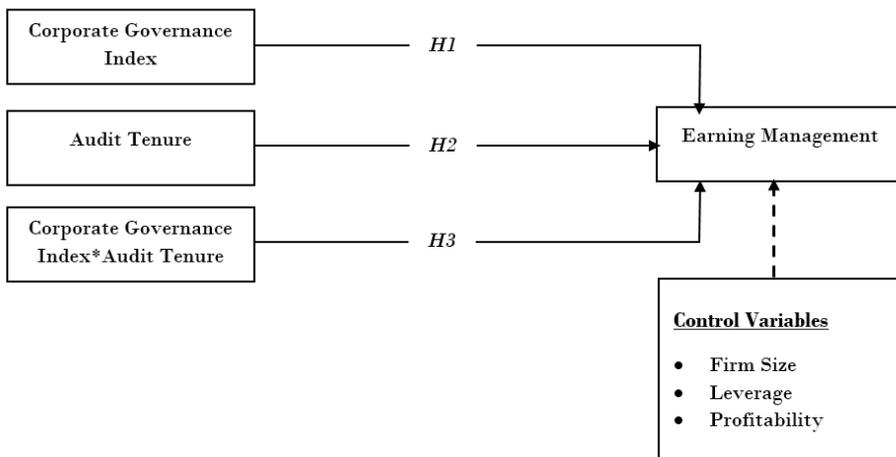
Research Model

Figure 1: Research Model (Source: Author)

Econometric Model Estimation

The present study employed panel data estimation techniques to generate the empirical findings. According to Himmelberg et al. (1999), this technique is helpful for specifically addressing unobserved vulnerability in companies' data. The panel data estimation model is helpful for mixed time-series and cross-sectional observations, thereby reducing the risk of multicollinearity. The current study used a three-panel estimation method to investigate the causal effects among the variables and to obtain empirical findings. The present study employed three model estimation techniques: OLS, random effects, and fixed effects (Wang et al., 2019). The reason for

the variation in the number of listed firms across sectors is. This study used a balanced panel data analysis to account for the various data types in the dataset, which included both time-series and cross-sectional observations. The random-effect model assumes that there is no relationship between the independent variables and the individual effects. Hongming et al. (2020) found that all individuals had identical repressor intercepts and slopes when addressing the random effect. We used the strategies above to improve the statistical analysis and chose the model with the most precise predictions. In addition, the Hausman test was used to compare the two models' strengths. Basic model equations are as follows:

$$EM = f(CGI, AT, FS, LG, OS) \quad (1)$$
$$EM = f(CGI, AT, FS, LG, OS, CGI * AT) \quad (2)$$
$$EM_{it} = \beta_0 + \beta_1 CGI_{it} + \beta_2 AT_{it} + \beta_3 FS_{it} + \beta_4 LG_{it} + \beta_5 OS_{it} + \varepsilon_{it} \quad (3)$$
$$EM_{it} = \beta_0 + \beta_1 CGI_{it} + \beta_2 AT_{it} + \beta_3 FS_{it} + \beta_4 LG_{it} + \beta_5 OS_{it} + \beta_6 (CGI * AT)_{it} + \varepsilon_{it} \quad (4)$$

RESULTS AND DISCUSSION

Descriptive

Table 2 presents the descriptive statistics for the main variables used in the research: EM (EM), CG index (CGI), audit tenure (AT), firm size (FS), leverage (LG), and profitability (PF). These statistics describe the central tendency, variability, and distribution of variables in the sampled firms. The descriptive findings indicate that the firms are highly heterogeneous in terms of governance quality, audit practices, financial structure, and ownership. There are weak or moderate governance structures. The audit tenure is short, characterized by high rotation and low familiarity among auditors. Leverage and ownership concentration vary across firms. There is also a significant difference in the EM practices among firms. Such patterns align with existing studies indicating that the institutional environments of emerging markets promote variation in the quality of governance and reporting

Table 2: Descriptive Analysis

Variable	EM	CGI	AT	FS	LG	PF
Mean	7.751	3.111	0.014	22.401	0.341	0.067
Std. Dev.	1.229	1.849	0.094	1.669	0.209	0.053
Min	5.088	0.988	0.251	19.788	0.038	0.108
Max	11.399	7.999	0.511	27.899	0.930	0.420
Median	7.343	2.543	0.058	21.843	0.567	0.241

Correlation

The Pearson correlation coefficients between the study variables are shown in Table 3: CG index (CGI), audit tenure (AT), EM (EM), firm size (FS), leverage (LG), and

profitability (PF). The correlations indicate the direction and strength of the linear relationships between these variables. Firm size is closely related to governance, with larger firms using stronger forms of governance. The variables of EM have a weak association with governance, tenure, and performance. Profitability and leverage exhibit a strong negative relationship: greater leverage corresponds to lower profitability. Multicollinearity issues are not found, except for a very high correlation.

Table 3: Correlation Analysis

	CGI	AT	EM	FS	LG	PF
CGI	1					
AT	–0.201	1				
EM	–0.199	–0.088	1			
FS	0.278	0.018	–0.211	1		
LG	–0.048	0.0278	0.211	0.295	1	
PF	0.201	–0.039	–0.187	0.052	–0.394	1

Breusch–Pagan Lagrange Multiplier (LM) Test.

Table 4 has an exact estimation for the analysis of this investigation. Given that the chi-square value is statistically significant at the 5% level of probability, the test's consistent conclusion suggests that choosing the fixed and random effects was the correct selection for the data analysis.

Table 4: Results of Breusch–Pagan Lagrange Multiplier (LM) Test.

	Statistics	p
Cross-section F	29.734	0.000
Cross-section $\chi2$	251.982	0.000

Autocorrelation Test

Table 5 verifies the absence of autocorrelation in the data, as no correlation is found. Given the probability value of 0.056, which indicates the lack of autocorrelation, the findings clearly show that there is no autocorrelation problem.

Table 5: Results of Autocorrelation and Heteroscedasticity Test.

Wooldridge test for autocorrelation	Breusch–Pagan/Cook–Weisberg test for heteroscedasticity
H0: No first-order autocorrelation	H0: Constant variance
F (9) = 57.842	$\chi2(1) = 4.763$
Prob > F = 0.056	Prob > $\chi2$ = 0.029

Table 5 illustrates heteroscedasticity in the data. The results show that the data is homoscedastic, with no concerns about heteroscedasticity ($p < 5\%$). Table 5: Results of Autocorrelation and Heteroscedasticity Test.

Hausman Test

Table 6 describes the procedure for determining whether a random or fixed effect is the better technique for estimating. The data clearly show that the fixed effect model is more appropriate than the random effect model. The Hausman test provides strong evidence that the fixed-effect model is the best way to forecast the study's results, as demonstrated by the statistically significant probability value.

Table 6: Hausman Test Finding

Test summary	χ^2 statistics	Prob
Cross-section random	23.873	0.000

Regression Model 1

The findings of the three estimation methods, namely, Pooled OLS, Fixed Effects (FE), and the Random Effects (RE), are presented in Table 7 in an attempt to determine the effects of CG, audit tenure, and the characteristics of the firm on the management of earnings in the case of listed companies. Model Selection Tests: The LM test (χ^2 = 298.651, p = 0.001) indicates that panel-data techniques (FE or RE) are preferable to pooled OLS. The Hausman test (2 = 16.271, p = 0.001) favors the fixed effects model, indicating that FE yields the same results and is the estimator of choice. Consequently, the fixed effects results are to be interpreted. The impact of CG on EM is positive and exceedingly significant (FE: 0.132, t = 2.892, p = 0.01). This implies that more robust CG systems need not lead to lower earnings manipulation; in other cases, such systems may be accompanied by symbolic compliance or weak governance. In the new markets, there may not be rigid enforcement of the governance mechanisms, and this gives the firms flexibility to operate under a formal structure but still practice opportunistic reporting. Recent studies show that reporting quality does not consistently improve with greater governance, due to institutional weaknesses (Amous & Ben Amar, 2025; Sasmita, 2025; Senan, 2024).

There is a positive and significant relationship between audit tenure and EM (FE: 8 = 0.178, t = 2.672, p < 0.05). The longer the auditor-client relationship, the more familiarity-related threats may arise, the less determinative the auditor's skepticism may be, and the greater the potential for audit independence to be limited, thereby increasing the probability of earnings manipulation. Recent research confirms that audit tenure may decrease audit quality in developing economies (Abouelela et al., 2025; Alhazmi et al., 2024; Tabsyir & Yunita, 2025). The size of the firm is also positively and significantly correlated with EM (FE: 2003): 0.129, t = 2.003). Smaller companies tend to face fewer pressures to keep earnings steady, withstand political scrutiny, or address complex business, all of which can motivate earnings manipulation. This is consistent with recent studies indicating that firm size tends to be more beneficial for the EM incentive (Banerjee et al., 2024; Lestari et al., 2025).

The relationship between leverage and its effect is positive and significant (FE: 0.087, t = 2.221). Profusely leveraged companies will also report inflated earnings to meet debt obligations and avoid bankruptcy. Incentives related to earnings manipulation are primarily driven by debt in emerging economies. The modern research confirms this observation (Bansal, 2023). In all one models, profitability plays an important role and positively influences EM (FE: 0.104, t = 2.124). EM can be used by profitable companies to sustain performance trends or to satisfy shareholders. The finding indicates that financially healthy companies can adopt strategic earnings reporting. This aligns with recent findings that increased profitability can stimulate upward earnings smoothing (Pujakusuma & Gowon, 2025). Model Fit and Diagnostic Tests also presented in Table 7. The R2 value (FE model = 13.291%) indicates that the variables are moderately effective in explaining variations in the management of earnings. The significance of the overall model is verified with an F-statistic (p < 0.01). The joint significance of the predictors in the RE model is indicated by a Wald 2 statistic (p < 0.001).

Table 7: Results of Regression Model 1

	Pooled OLS	Fixed Effect	Random Effect
CGI	0.112 (2.671***)	0.132 (2.892***)	0.122 (2.776***)
AT	0.109 (2.512**)	0.178 (2.672**)	0.156 (2.611**)
FS	0.101 (1.982**)	0.129 (2.003**)	0.118 (1.999**)
LG	0.067 (2.110**)	0.087 (2.221**)	0.071 (2.123**)
PF	0.098 (2.001**)	0.104 (2.124**)	0.112 (2.321**)
R2	11.278	13.291	12.281
F-statistics	6.871 (0.000)	5.991 (0.001)	
Wald Test χ2			6.821 (0.000)
LM Test (Pooled vs. FE or RE)	298.651 (0.000)		
As per LM test finding Fixed and random effect is more appropriate than OLS			
Hausman Test	16.271 (0.000)		
As per finding of Hausman test the random effect not appropriate test			

Model 2

Table 8 presents the findings from the pooled OLS, fixed effects (FE), and random effects (RE) models investigating the effects of CG, audit tenure, and their combination on EM among Indonesian listed companies. Several control variables (firm size, leverage, and profitability) were also used. Therefore, the results of the LM test (309.817 vs. 0.001) indicate that panel data models (FE/RE) are even better than pooled OLS. Moreover, the Hausman test (χ 2 = 17.716, p < 0.001) proves the practicality of the fixed effects model, because the FE model is consistent and better than the random effects model. As such, the fixed effects finding is the most credible. According to findings, the CG index is positively correlated with EM (FE: 8 = 0.209, t = 3.671, p = 0.01). This finding indicates that companies with higher CG scores are more likely to be earnings-managed, which is, to some extent, counterintuitive. One

potential reason is that some firms have governance mechanisms in name only (box-ticking) that do not effectively minimize opportunistic managerial behavior. It is consistent with recent findings that, in emerging markets, the quality of governance reforms can vary depending on the enforcement of regulations (Amous & Ben Amar, 2025; Sasmita, 2025; Senan, 2024).

Furthermore, the tenure of the auditor is also positive and significant (FE: 0.212, t = 3.371, p < 0.05). EM is more evident in longer auditor-client relationships, presumably because of the auditor's familiarity with the clients and a lack of independence over time. This is in line with the latest research, which suggests that a long-term audit period may lead to deteriorating audit quality (Abiola, 2022; Aondover, 2025; Yahaya, 2025). This paper use interaction term (CG*audit tenure). The interaction term has a significant influence on EM (FE = 0.354, t = 4.891, p < 0.01). This shows that the coexistence of sound CG systems and long audit tenure only enhances EM rather than mitigating it. This indicates that, where boards are highly dependent on long-term auditors, even robust governance models might be unable to constrain managerial discretion. The interaction enhances the positive rather than diminishing it, which is indicative of the complexity of governance systems in emerging markets. Recent studies also indicate that governance systems do not necessarily complement external monitoring and, in some cases, give perverse incentives (Wang, 2025; Yahaya, 2025).

Control variables: firm size is positively and significantly associated (FE = 0.121, t = 2.018). Bigger companies are more likely to use EM because they are more visible, more complex, and politically expensive. This positive relationship is confirmed by recent studies (Asghar et al., 2020; Burlacu et al., 2024). EM is also positively associated with leverage (FE = 0.099, t = 2.006).

Table 8: Results of Regression Model 2

	Pooled OLS	Fixed Effect	Random Effect
CGI	0.198 (3.314***)	0.209 (3.671***)	0.199 (3.432***)
AT	0.172 (3.123**)	0.212 (3.371**)	0.202 (3.561**)
CGI*AT	0.321(4.617***)	0.354 (4.891***)	0.329 (4.772**)
FS	0.119 (2.182**)	0.121 (2.018**)	0.099 (2.17**)
LG	0.087 1.993**)	0.099 (2.006**)	0.067 (1.921**)
PF	0.081 (1.923*)	0.088 (1.998**)	0.077 (1.891*)
R2	13.726	15.671	13.899
F-statistics	7.712 (0.000)	6.721 (0.001)	
Wald Test χ2			7.726 (0.000)
LM Test (Pooled vs. FE or RE)	309.817 (0.000)		
As per LM test finding Fixed and random effect is more appropriate than OLS			
Hausman Test	17.716 (0.000)		

Highly leveraged companies can use earnings to comply with debt covenants and escape default remedies. This aligns with the debt-covenant hypothesis and recent findings (Anam Iqbal et al., 2022). The level of profitability is substantial at the 10th percentile (FE: β = 0.088, t = 1.998). More lucrative companies might manipulate earnings upward to maintain market performance patterns and expectations. This behavior is backed up by recent evidence (Almubarak et al., 2023).

Model Fit and Significance FE R^2 = 15.671%, which implies that the model captures a moderate amount of variance in EM. The F-value is statistically significant at p = 0.01, indicating that the overall model is valid. The results of the Wald test for the RE model (χ^2 = 7.726, p = 0.001) indicate the joint significance of the predictors. Overall Interpretation The findings suggest that CG and audit tenure (independently and together) have a significant effect on EM among Indonesian listed firms.

CONCLUSION

This paper provides some useful information on the relationship between CG, audit tenure, and EM of companies listed in the Indonesian Stock Exchange between the year 2010 and 2020. This study using strong regression models as well as Fixed Effects and Random Effects models not only establishes the strong relationships between these variables, but also brings out the complexities and subtleties in the emerging markets.

The correlation between CG and EM was identified as positive and significant and is contrary to the widely accepted belief that the stronger a governance is, the lower the earnings manipulation. The result indicates that although companies with elevated CGI seem to possess strong governance systems, these systems do not necessarily work in curbing EM. As a matter of fact, the research suggests that there are companies that may be involved in symbolic compliance whereby they may seem to be adhering to governance practices in theory but in reality, they are not putting them into practice. This trend is very apparent in the emerging markets such as Indonesia where the CG laws may be unevenly and weakly enforced.

Moreover, the quality of governance mechanisms, in actual sense, may differ greatly across firms operating in the emerging market conditions because of the institutional strength and the rigor of enforcement. Consequently, companies can take the form of formal governance systems as the means of creating the illusionary look instead of enhancing transparency or accountability. This adds to a situation where an increase in CGI scores is associated with increased earnings manipulation, which points to a possible disconnect between the form and actual functioning of governance. Similar to the previous studies, the research determined that audit tenure positively influences EM significantly. The longer the relationship between the auditor and the client, the higher the chances of a compromised auditor independence whereby the firms can

easily manipulate their earnings. The consequent of longer audit tenures is a familiarity threat whereby the auditors feel comfortable with their clients and they are less skeptical and, as such, their audit becomes less effective. The discovery is especially important to the emerging markets where the quality and audit control may be less strict than in developed economies.

Interestingly, the interplay between the CG and the audit tenure added more insight to the analysis. The research discovered that in the case both companies possess good governance structures and long audit tenures, the probability of earnings manipulation is real. This negative finding indicates that the existence of well-organized CG systems might not reduce the earnings manipulation, in case auditors have served long terms. The long-time auditors would have a feeling of being dependent on the client and this may lead to the discretion of the managers unchecked. Thus, the research recommends that governing reforms are undertaken in a comprehensive manner, in which the tenure of audits should also be strictly observed together with governing constructions.

A number of control variables were also considered in the study including the size of the firm, leverage and profitability, which were all found to have strong relationships with the EM. Higher in terms of size, larger firms tend to experience more pressure to comply with the expectations on the financial matters and the level of political scrutiny. This predisposes them to EM in a bid to smooth earnings or to fulfill market expectations. Equally, highly leveraged firms had a greater tendency to manipulate their earnings to prevent defaulting the debt covenant or to avoid punishment as a result of defaulting on the financial obligations. The high leverage companies are quite tempted to make sure that the financial statements reflect stable or better financial performance.

Finally, the findings emphasize the need to enhance both the CG and audit control in new markets, such as Indonesia. To increase the transparency of the financial system and minimize the risk of EM, policymakers and regulators should focus on strengthening the governance enforcement procedures, as well as revisiting the audit tenure policies. The research is significant to the body of literature by giving empirical data on the interactive impacts of CG and audit tenure, presentable information to both scholars and regulators in the emerging market experiences.

POLICY IMPLICATIONS

The results of the study are very applicable to policymakers, regulators and CG practitioners especially in the emerging markets. The findings are important in highlighting the importance of tightening CG practices to make them not just symbolic but play a significant role in curbing EM. Specifically, the policymakers in Indonesia and other emerging economies should understand that the formal adoption

of governance mechanisms is not necessarily sufficient to minimize earnings manipulation. These mechanisms should be aligned with strict enforcement, transparency and accountability guidelines.

Furthermore, regulators ought to think about the reduction of audit tenure or coming up with mechanisms that would strengthen the independence of auditors in long-term audits. This is essential to the quality and effectiveness of audits especially in markets where auditors might get close associations with clients over a period of time. The problems associated with long audit tenures can be solved by introducing rotation policies to the auditors, or by having the auditors assess the audit relationship more often.

LIMITATIONS AND FUTURE DIRECTIONS

Although the current research enlightens on the CG, audit tenure, and EM relationship in the Indonesian setting, future research may go further to investigate how the effectiveness of CG mechanisms depends on local cultural, economic, and regulatory aspects. An extension of the scope of the research to cover cross country comparisons would also be a good idea to enable the researcher to gain a better insight on the effect of institutional environment on the results of the governance practices. The auditor quality may also be a topic of further research, including whether some audit firms are more likely to allow earnings manipulation where long tenures are involved, or how their audit procedures change over time. Investigation of audit committees and their independence in reducing earnings manipulation may also provide some valuable insights on how firms can improve the balance between governance and audit practices in order to deliver more accurate and transparent financial reporting.

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