



Article Type: Research Paper

Earnings management in times of crisis: A political cost hypothesis

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Abstract

Research aims: The COVID-19 pandemic disrupted multiple industries, including chemistry, pharmaceuticals, telecommunications, and healthcare. This study, thus, explores how these sectors managed their earnings concerning political factors during the pandemic. Since these sectors play a critical role in maintaining business stability during this period, the authors hypothesize that some companies within them may have manipulated their profits.

Design/Methodology/Approach: This study used quantitative methods to analyze a sample of companies in the chemical, pharmaceutical, telecommunications, and healthcare sectors listed on the Indonesia Stock Exchange from 2018 to 2022. Out of 60 companies, 20 met the criteria. The authors then tested the political costs hypothesis using Kotari et al.'s (2005) calculation method and a discrimination test for discretionary accrual values.

Research findings: The findings reveal that some companies practiced earnings management with varying degrees across sectors. Notably, not all companies employed revenue reduction as a manipulation tactic. Significant differences were observed between the pre-pandemic and pandemic periods. It is worth highlighting that not all COVID-19 beneficiaries resorted to earnings management to access government incentives or facilities.

Theoretical contribution/Originality: The findings of this research offer empirical evidence from both a theoretical standpoint and an analysis of the financial status of the involved companies.

Practical/Policy Implication: This study aims to investigate if companies manipulated earnings during the COVID-19 pandemic by intentionally reducing their profits when their sectors were thriving due to the pandemic.

Research Limitation: This research is limited by its use of quarterly data, incomplete data for some companies, and a reliance on existing data rather than current information collection.

Keywords: Earning Management; Political Cost Hypothesis; Discretionary Accrual



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DOI: 10.18196/jai.v24i2.19610

CITATION:

Paramastri, H., Atmini, S., & Rahman, A.F. (2023). Earnings management in times of crisis: A political cost hypothesis. *Journal of Accounting and Investment*, 24(3), 923-936.

ARTICLE HISTORY

Received:

23 Aug 2023

Revised:

06 Sep 2023

27 Sep 2023

Accepted:

30 Sep 2023



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JAI Website:



Introduction

Statistics Indonesia [Badan Pusat Statistik] (2020) reported that the pandemic led to a 5.32% decrease in Indonesia's economy in the second quarter of 2020. For instance, the transportation industry experienced a significant profit contraction of 34.29%, primarily due to a sharp decline in production caused by the pandemic. Industries involved in textiles, clothing, and tobacco processing also saw profit decreases of 14.23% and 10.84%, respectively. The financial sector likewise was under pressure during the pandemic, evident in the Composite Stock Price Index [IHSG], which hit its lowest level on March 24, 2020, at 3,937.6 points (Amanda, 2020).

The pandemic has significantly impacted various business activities, including those of companies listed on the Indonesia Stock Exchange (BEI). Hidayat, the Executive Director of the Indonesian Issuers Association, outlined that several sectors were most severely affected by the pandemic due to a significant drop in revenue. These affected issuers came from the hospitality, tourism, transportation, construction, infrastructure, and energy industries (Sidik, 2020).

Nevertheless, some companies did not suffer severe impacts from the spread of the coronavirus, i.e., some that operated in the chemical, pharmaceutical, telecommunications, and healthcare sectors (Aldin, 2020). According to data from the Ministry of Industry of the Republic of Indonesia [Kementrian Perindustrian, Republik Indonesia] (2020c), the chemical, pharmaceutical, and traditional medicine industries experienced growth of 8.65% to meet domestic demand for medicines during the COVID-19 pandemic. This is further supported by statements indicating that the healthcare sector is expected to benefit for the next 3-5 years (Elena, 2020).

The chemical, pharmaceutical, and telecommunications sectors can be expected to potentially continue experiencing increasing profits in 2020 compared to previous years. This situation contrasts with what was experienced by industries under pressure due to the pandemic. In this case, the pandemic has transformed people's lifestyles and shifted towards digital transformation. This has increased the demand for home internet access. Telkom has been serving the increased demand throughout 2020, adding more than 1.01 million IndiHome customers, resulting in a 14.5% growth in the customer base compared to the end of 2019 (CNN Indonesia, 2021).

This statement is further reinforced by information from the Portal Informasi Indonesia (2021), which indicates that the telecommunications sector continued to grow amid the pandemic, with a projected 8% annual growth in 2022. According to Helmy Yusman Santoso, Director and Chief Financial Officer of PT Tower Bersama Infrastructure Tbk (TBIG), the telecommunications industry has the potential for growth in tandem with the increasing number of internet users, thereby demanding an increase in supporting telecommunications infrastructure (Hastuti, 2021).

Moreover, the growing need for digital telecommunications is in response to government efforts to curb the spread of the coronavirus and mitigate the pandemic's negative impacts. The government is actively working to recover all affected sectors, issuing various policies to ease the burden on businesses during the pandemic. One such policy requires industrial companies or industrial areas to have an Operational Permit and Industrial Activity Mobility Permit (IOMKI), as outlined in the Circular of the Minister of Industry No. 7 of 2020 (Kementrian Perindustrian, Republik Indonesia, 2020a).

Additionally, the government has introduced incentives, including Ministerial Decision No. 8 of 2020 concerning Determining Certain Natural Gas Users and Prices in the Industrial Sector, eliminating minimum contract payments, and aligning payments with actual usage (Kementrian Perindustrian, Republik Indonesia, 2020b). In the realm of taxation, the government implemented policies, beginning with issuing Regulation of the

Minister of Finance (PMK) No. 23/PMK.03/2020 on March 21, 2020, to provide tax incentives for industries affected by the coronavirus outbreak. These incentives encompass Article 21 Income Tax, Article 22 Import Tax, Article 25 Income Tax installment payments, and Value Added Tax (VAT) incentives. The regulations governing these tax incentives are continuously updated to adapt to the pandemic's evolving conditions.

Therefore, this research aims to investigate industries unaffected by the COVID-19 pandemic. Industries not mentioned in the tax incentive regulations (PMK) are considered unaffected by the pandemic. The study seeks to explore whether there is a practice of earnings management motivated by reducing political costs among companies in these unaffected sectors. Specifically, the chemical, pharmaceutical, telecommunications, and healthcare sectors are excluded from the tax incentive regulations.

Further, this study examines the motivation for political cost in earnings management practices within industries presumed to have benefited during the COVID-19 pandemic, including chemistry, pharmaceuticals, telecommunications, and healthcare (Aldin, 2020). This is further supported by government regulations that provide specific benefits and facilities to business owners in these sectors during the pandemic. These benefits and facilities include tax incentives and ease of business activities for certain industries. As stated above, the government initiated tax incentive policies for industries affected by the pandemic, beginning with issuing Regulation of the Minister of Finance (PMK) No. 23/PMK.03/2020 on March 21, 2020. These tax incentive regulations have been continuously updated to adapt to the changing pandemic conditions. The extension of tax incentives was accomplished by issuing PMK No. 44/PMK.03/2020, PMK No. 86/PMK.03/2020, PMK No. 9/PMK.03/2021, and PMK No. 82/PMK.03/2021. These incentives cover Article 21 Income Tax, Article 22 Import Tax, Article 25 Income Tax installment payments, final income tax incentives, construction service incentives, government-borne final income tax, and Value Added Tax (VAT) incentives. These regulations also specify the types of industrial sectors affected by the coronavirus pandemic eligible for tax incentive facilities.

According to the research conducted by Indahsari and Fitriandi (2021) regarding taxation, due to the incentives provided during the COVID-19 pandemic, two incentives have a significant impact, namely on Article 22 Import Tax (*PPh Pasal 22 Impor*) and Article 25, which can affect the cash flow of corporate taxpayers. On the other hand, several industry sectors, namely the chemical, pharmaceutical, telecommunications, and healthcare sectors, were not mentioned in the appendix of the Minister of Finance Regulation (PMK) regarding the provision of these tax incentives, as they were not significantly affected by the pandemic.

The provision of tax incentives certainly impacts the decrease in state revenue from the tax sector. This situation will incentivize the government to counterbalance it by optimizing state revenue from the tax sector, particularly focusing on taxes paid by industries that have benefited during the pandemic. The government may enact policies

to ensure that companies contributing significantly to the COVID-19 recovery and those thriving in the pandemic shoulder a proportionate tax burden. Given the inherent profit-maximizing nature of businesses, companies often seek ways to minimize their tax liabilities. This behavior prompts the government to bolster tax collection mechanisms and close potential loopholes businesses might exploit.

Conversely, companies tend to avoid optimizing state revenue from the tax sector. There is a tendency for companies to reduce their performance, hoping to evade government tax optimization efforts. This phenomenon underscores the importance of strong regulatory oversight and enforcement to ensure tax compliance. Governments must remain vigilant, adapting and enhancing tax regulations to stay ahead of evolving corporate strategies to minimize tax obligations.

Building upon this, this research aims to investigate whether earnings management practices are characterized by profit reduction patterns undertaken by companies unaffected by this pandemic. These companies, which are not eligible for the tax incentives provided by the government, could potentially be targeted by the government to optimize revenue collection in the tax sector. By understanding the strategies employed by these companies to reduce their taxable income, the government can refine tax policies and enforcement to address potential gaps and promote a fair and equitable tax system. Additionally, this research aims to shed light on the broader implications of such earnings management practices, both for government revenue and overall economic stability, helping to guide policy decisions and regulatory actions in the post-pandemic landscape.

Literature Review and Hypotheses Development

Positive Accounting Theory

Positive Accounting Theory (PAT) aims to explain and predict accounting practices (Watts & Zimmerman, 1986, p. 2). Explanation of accounting practices involves providing reasons for observed practices. The assumptions used in Positive Accounting Theory are that the capital market is efficient, individuals act opportunistically and rationally in their self-interest, and accounting information is both an economic and political commodity. The concept of an efficient capital market stems from accounting's decision-usefulness concept. An efficient capital market helps conceptualize information related to financial statement usefulness. According to Kanodia et al. (2016), accounting calculations influence many decisions, and financial reporting outcomes have a tangible effect on providing information. Financial disclosures have a real impact on influencing a wide array of decisions through accounting calculations.

Based on the exposition by Scott (2017, p. 73), financial reporting based on historical costs utilizes the concept of the usefulness of financial statements. Financial statements are expected to provide problem-solving as a step of identification to be carried out by the users of financial statements to obtain accurate information for better decision-

making. Accounting is only useful if the information received is timely, making accounting information more cost-effective compared to other forms of information. From the perspective of opportunistic behavior, there is an angle that management or managers utilize information asymmetry between external and internal parties of the company to maximize certain decisions, such as compensation contracts, debt contracts, and regulations. This phenomenon can be observed in the activities of political cost and debt covenant hypotheses (Priantinah, 2016).

Agency Theory

The Agency Theory, proposed by Jensen and Meckling in 1976, underpins contemporary corporate business practices by drawing from economics, decision theory, sociology, and organizational theories. This theory focuses on the dynamics between the principal (investor) and the agent (manager), articulated through a collaborative contract called the nexus of contracts. As explained by Wolk et al. (1992), the Agency Theory serves as a focal point for understanding the relationship between the company owner (principal) and management (agent). It elucidates the parties involved in the dynamics of corporate agency, including employment contracts between owners and managers and loan contracts between managers and lenders.

However, according to Zardkhoohi et al. (2015), in the Traditional Agency Theory, the agent is considered the perpetrator of errors, and the principal is seen as a victim, overlooking the complex relationship between the principal and the agent that affects third-party stakeholders. There exists a complex framework related to the dynamics of the relationship between the principal and the agent, where the agent and principal must navigate the appropriate situation to behave in the best interest of third parties. The agent and principal are not only involved in a simple relationship but also involve third parties within that relationship.

Hypothesis

The purpose of Positive Accounting Theory is to explain and predict accounting practices. It posits that accounting serves as a tool for monitoring contracts among parties involved in managing a company using accounting figures. Accounting provides information that forms the basis for resource allocation, management compensation, and debt agreement oversight decisions. Management seeks to influence these decisions through choices in accounting methods, accounting estimates, shifting the timing of expense and revenue recognition, and transferring costs and revenues between companies. The choices made by management regarding accounting policies or actual actions that affect desired profit reporting are termed earnings management (Scott, 2017, p. 445).

The government has issued numerous regulations across various sectors to prevent and mitigate the impact of the pandemic. One of the regulations implemented in the industries affected by the pandemic is the provision of tax incentive facilities. According to Indahsari and Fitriandi (2021), the tax incentives provided by the government are

predominantly used by businesses to cover losses during the pandemic. This situation has led to companies unaffected by the pandemic, not receiving tax incentives, and facing political costs to consider several things because they did not receive tax incentive facilities. Industries unaffected by the pandemic are suspected to be engaged in earnings management practices, and they may reduce their earnings to minimize the political costs they have to bear (Watts & Zimmerman, 1978). Earnings management also focuses on how companies make decisions on financial reporting that can impact the quality of the reports (Beyer et al., 2019). Based on this description, the hypothesis in this study is as follows:

H₁: Companies in the chemical, pharmaceutical, healthcare, and telecommunications sectors are indicated to engage in earnings management activities during the pandemic.

Research Method

This research employed a quantitative approach to identify a specific event at a particular point in time. The type of research conducted was explanatory research, explaining the relationships between various variables. This study utilized data obtained from secondary sources, indirectly collected through various sources, such as records or archives, retrieved through documentation methods. Then, the population for this study consisted of companies operating in the chemical, pharmaceutical, healthcare, and telecommunications sectors listed on the Indonesia Stock Exchange (IDX) from 2018 to 2022, based on the sector classification published by IDX in 2020. The years 2018 to 2019 were used as sample data from the pre-pandemic period, while the years 2020 to 2022 were used as sample data for the pandemic years.

The choice to focus on companies within the chemical, pharmaceutical, telecommunications, and healthcare sectors for this research was driven by the observation that these industries remained relatively unaffected by the COVID-19 pandemic while potentially engaging in earnings management practices. The sample selection process employed purposive sampling, specifically judgment sampling. The criteria for sample selection encompassed companies within these industry segments listed on the Indonesia Stock Exchange (BEI) from 2018 to 2022, with a consistent presence and reporting of quarterly financial statements and utilizing the Indonesian Rupiah (IDR) as their currency. Out of 60 companies in this sector, only 20 met all these criteria and were chosen as the research sample.

In this research, earnings management practices were proxied by discretionary accruals (DA) and estimated using the Performance Matched Discretionary Accrual Measure model developed by Kothari et al. (2005). The model used to estimate earnings management practices was a discretionary accrual model based on the Jones (1991) model, modified by Dechow et al. (1995) and further expanded by Kothari et al. (2005) to incorporate the element of ROA. Therefore, the model employed in this study was Kothari's et al. (2005) discretionary accrual model.

The formula for measuring discretionary accruals (DA) involved the following steps:
The Total Accruals (TACit) value was derived from the calculation as follows:

$$TAC_{it} = NDA_{it} + DA_{it} \dots (1)$$

To calculate TACit, the following formula was utilized:

$$TAC_{it} = [\Delta Current Assets_t - \Delta Cash_t] - [\Delta Current Liabilities - \Delta Current Maturities of Long-Term Debt - \Delta Income Taxes Payable] - Depreciation and Amortization Expense_t \dots (2)$$

The total accrual value was estimated through a regression equation as follows:

$$TAC_{it}/AST_{it} = \beta_0 + \beta_1 (1/AST_{it}) + \beta_2 (\Delta REV_{it}/AST_{it}) + \beta_3 (PPE_{it}/AST_{it}) + \beta_4 (ROA_{it}/AST_{it}) + \varepsilon_{it} \dots (3)$$

To compute NDA, the formula is as follows:

$$NDA_{it} = \beta_0 + \beta_1 (1/AST_{it}) + \beta_2 (\Delta REV_{it} - \Delta REC_{it}) / AST_{it} + \beta_3 (PPE_{it}/AST_{it}) + \beta_4 (ROA_{it}/AST_{it}) + \varepsilon_{it} \dots (4)$$

Finally, the formula for calculating DA is as follows:

$$DA_{it} = TAC_{it} - NDA_{it} \dots (5)$$

In this context, TAC_{it} represents the total accruals for company i in quarter t , NDA_{it} stands for non-discretionary accruals for company i in quarter t , and DA_{it} represents discretionary accruals for company i in quarter t . AST_{it} corresponds to the total assets of the company i in quarter t , ΔREV_{it} signifies the change in sales for company i in quarter t , ΔREC_{it} represents the change in accounts receivable for company i in quarter t , PPE_{it} denotes the total property, plant, and equipment for company i in quarter t , ROA_{it} indicates the return on total assets for company i in quarter t , and ε_{it} is the error term for company i in quarter t .

Moreover, hypothesis testing in this study used discrimination tests, including parametric and nonparametric tests. Parametric discrimination tests would be used when the data met the assumptions of homogeneity and normality. One of the parametric discrimination tests used is the Paired T-test. Meanwhile, nonparametric discrimination tests were employed to assess differences in medians, and one of them is the Mann-Whitney Rank Test.

Result and Discussion

Descriptive statistics provide an initial overview or description of the data to be studied. Descriptive statistics include minimum and maximum values, the mean, and standard deviation. This research used descriptive statistics to examine the discretionary accrual

values, reflecting the extent of earnings management. The results of the descriptive statistics for each data component are presented in Table 1.

Table 1. Result of Descriptive Statistics

Variable	Mean	Standard deviation	Min	Maks
All Sample Q1 2018 – Q4 2022	-0.9355	33.4519	-311.114	315.175
DA Q1 2018 - Q4 2019 (Before)	-0.6876	36.7385	-311.114	315.175
DA Q2 2020 - Q1 2022 (on)	-1.1834	29.9209	-255.048	256.563
Chemical Sector	-0.5898	41.2060	-255.048	256.563
DA Q1 2018 - Q4 2019 (Before)	0.3105	5.0589	-4.590	29.450
DA Q2 2020 - Q1 2022 (on)	-1.4893	58.4135	-255.050	256.560
Pharmacy Sector	-0.5320	9.9655	-45.604	42.963
DA Q1 2018 - Q4 2019 (Before)	-0.4292	12.3534	-45.600	42.960
DA Q2 2020 - Q1 2022 (on)	-0.5321	9.9649	-45.600	42.960
Telecommunication Sector	-3.0240	56.6452	-311.114	315.175
DA Q1 2018 - Q4 2019 (Before)	-2.8725	80.6806	-311.110	315.170
DA Q2 2020 - Q1 2022 (on)	-3.1763	3.3587	-12.860	7.300
Healthcare Sector	-0.0947	11.7419	-52.226	50.928
DA Q1 2018 - Q4 2019 (Before)	0.E+00	15.4753	-52.230	50.930
DA Q2 2020 - Q1 2022 (on)	-0.1895	6.3088	-11.280	22.500

Note: DA = discretionary accruals.

Based on the information from Table 1, it can be projected as follows. Concerning information related to DA as a whole, the findings indicated that earnings management activities conducted by each sector tended to decrease earnings. This was evident from the DA, with an average value of -0.9355. However, the data dispersion for DA was quite high, at 33.4519, primarily due to the data originating from various sectors. This was further emphasized by the significant difference between the minimum value of -311.114 and the maximum value of 315.175. Therefore, although companies engaged in earnings management to decrease earnings, some had increased. Furthermore, before the pandemic, companies in these sectors also engaged in earnings management, but with a lower decrease in earnings compared to during the pandemic, as shown by the average values, which were approximately -0.6876 before the pandemic and around -1.1834 during the pandemic.

Additionally, based on Table 1, there is observational data for each sector, and some sectors exhibited similar patterns of earnings management, such as the chemical and healthcare sectors. Data presented for the chemical and pharmaceutical sectors as a whole showed that companies in these sectors tended to engage in earnings management by decreasing earnings. It was evident from the average values, approximately -0.5898 for the chemical sector and -0.0947 for the pharmaceutical sector. Before the pandemic, the chemical and healthcare sectors tended to manage earnings by increasing earnings, with values of approximately 0.3105 and 0.0E+00, respectively. During the pandemic, both sectors, on the other hand, engaged in earnings management by decreasing earnings, with values of approximately -1.4893 and -0.1895. Similar patterns of earnings management were also observed in the pharmaceutical and telecommunications sectors from the data in Table 1. Overall, both sectors engaged in

earnings management by decreasing earnings. However, the telecommunications sector exhibited a significantly larger decrease in earnings compared to all the sectors studied. According to the research on DA as a whole for the pharmaceutical and telecommunications sectors, companies in these sectors tended to engage in earnings management by decreasing earnings, as indicated by the average DA values of approximately -0.5320 and -3.0240, respectively. Before the pandemic, both sectors also managed earnings by decreasing earnings, with values of approximately -0.4292 and -2.8725, respectively. During the pandemic, companies in these sectors tended to manage higher earnings by decreasing earnings, with values of approximately -0.5321 and -3.1763, respectively.

Before conducting data analysis (which involves numerical data) using parametric statistics, it is necessary to assess the normality assumption of the data. To test whether the research sample follows a normal distribution, the Kolmogorov-Smirnov test was employed, with the following test results.

Table 2 Result of Normality Data

	p-value	Result	Analysis/Decision of Test Results
DA	0.000	Not normally distributed	Nonparametric/Mann-Whitney test
DA Chemical Sector	0.000	Not normally distributed	Nonparametric/Mann-Whitney test
DA Pharmacy Sector	0.000	Not normally distributed	Nonparametric/Mann-Whitney test
DA Telecommunication Sector	0.000	Not normally distributed	Nonparametric/Mann-Whitney test
DA Health Sector	0.000	Not normally distributed	Nonparametric/Mann-Whitney test

Based on the normality test results (Table 2), it can be seen that the variables DA and DA for each sector (chemical, pharmaceutical, telecommunications, and health) had p-values of 0.000, less than 0.05 ($p < 0.05$). According to the test results, it can be concluded that the data for DA and DA in each sector did not follow a normal distribution. Therefore, nonparametric statistics (Mann-Whitney test) should be used for the analysis.

Based on Table 3, during the pre-pandemic period, the average DA was -0.068, with a standard deviation 36.73. In the pandemic, the average DA was -1.183, with a standard deviation of 29.92. The comparison of DA between the pandemic and pre-pandemic periods using the Mann-Whitney test resulted in a p-value of 0.788 ($p > 0.05$). Therefore, it can be concluded that there was no significant difference in DA between the pandemic and pre-pandemic periods. In other words, the degree of earnings management projected through DA before and during the pandemic did not significantly differ. Thus, the hypothesis was not supported.

Table 3 Result of Mann-Whitney Test for DA

	Before Pandemic		On Pandemic		p-value
	Mean	Std Deviation	Mean	Std Deviation	
DA	-0.688	36.738	-1.183	29.921	0.788

Discussion

In previous research involving similar situations where government regulations impact certain companies, Cahan et al. (1997) suggested that legal uncertainty can influence a company's decisions regarding discretionary accruals, making the results statistically insignificant. Companies tend to make discretionary accrual decisions only when the regulation is in effect, but these decisions become less significant after regulatory revisions. According to Key (1997), examining the hypothesis of political costs through accounting data has limited explanatory power in depicting the political process. This is because the discretionary accrual system, as Key (1997) proposed, allows managers to accelerate the recognition of losses, which discretionary accruals cannot capture.

However, Ardiani and Sudana (2018) stated that the practice of earnings management is not always caused by political cost theory. This was revealed in the hypothesis that high political costs tend to provide opportunities for engaging in earnings management activities, but this was not reflected in the research conducted by Ardiani and Sudana (2018). They asserted that disclosure and reporting obligations are not solely for earnings management activities. On the other hand, according to a study by Nalarreason et al. (2019), earnings management activities conducted by companies are higher when the company faces a threat of bankruptcy. It was also emphasized that if there is an elevated level of asymmetrical conflict within the company, it leads to more significant earnings management. Hence, earnings management activities aimed at avoiding political costs are not always the primary consideration for companies.

During the COVID-19 pandemic, this study did not support examining earnings management by decreasing income. Companies did not immediately take the opportunity to decrease income during the pandemic. This finding contradicts the notion presented by Han and Wang (1998), where companies did reduce their income in the third and fourth quarters of 1990 during a politically sensitive time to minimize the extraordinary increase in income. Companies facing unusual product price hikes were incentivized to decrease reported income to minimize political sensitivity and associated costs. Nonetheless, companies did not immediately reduce their income in this study due to the COVID-19 pandemic.

This situation will incentivize the government to counterbalance it by optimizing state revenue from the tax sector, particularly focusing on taxes paid by industries that have benefited during the pandemic. The government may enact policies to ensure that companies contributing significantly to the COVID-19 recovery and those thriving in the pandemic shoulder a proportionate tax burden. Given the inherent profit-maximizing nature of businesses, companies often seek ways to minimize their tax liabilities. This

behavior prompts the government to bolster tax collection mechanisms and close potential loopholes businesses might exploit.

In that situation, companies tend to avoid optimizing state revenue from the tax sector. There is a tendency for companies to reduce their performance, hoping to evade government tax optimization efforts. This phenomenon underscores the importance of strong regulatory oversight and enforcement to ensure tax compliance. Governments must remain vigilant, adapting and enhancing tax regulations to stay ahead of evolving corporate strategies to minimize tax obligations.

For that reason, as stated above, this research aims to investigate whether earnings management practices are characterized by profit reduction patterns undertaken by companies unaffected by this pandemic. These companies, which are not eligible for the tax incentives provided by the government, could potentially be targeted by the government to optimize revenue collection in the tax sector. By understanding the strategies employed by these companies to reduce their taxable income, the government can refine tax policies and enforcement to address potential gaps and promote a fair and equitable tax system. Additionally, this research aims to shed light on the broader implications of such earnings management practices, both for government revenue and overall economic stability, helping to guide policy decisions and regulatory actions in the post-pandemic landscape.

Practical implications of this research involve informing tax policy reforms that enhance revenue collection, ensuring a fair distribution of tax burdens, and discouraging tax evasion strategies. Governments can use these findings to streamline tax codes and enforcement mechanisms, fostering a more efficient tax system. Further, theoretical implications lie in advancing our understanding of corporate behavior during crises and their responses to government policies. Exploring earnings management practices sheds light on the complex interplay between businesses and regulatory frameworks, contributing to the academic discourse on taxation, corporate governance, and public policy. This research also extends theoretical foundations, providing a basis for future studies on tax optimization strategies and their consequences on fiscal health and economic growth.

Conclusion

The COVID-19 pandemic has resulted in various changes in human needs and lifestyles. One notable impact is the significant surge in certain businesses due to COVID-19, including chemical, pharmaceutical, telecommunications, and healthcare companies. These companies played crucial roles during the pandemic; those in the chemical, pharmaceutical, and healthcare sectors collaborated to provide necessary healthcare services to combat COVID-19, while telecommunications companies played a vital role in shifting many offline activities to online platforms. Concurrently, governments needed revenue from the taxation sector for COVID-19 containment efforts.

The findings of this study provide empirical evidence that companies across all observed sectors tended to engage in earnings management activities. However, it was not proven that all companies in the observed sectors managed earnings with an income-decreasing pattern. The discrimination test results indicated that earnings management conducted by companies in the observed sectors before and during the pandemic was insignificant. Based on these conclusions, the hypothesis regarding earnings management related to political costs was not supported. In addition, this research has limitations due to the availability of complete company data, as the required data is quarterly, and not all of it is available consecutively. The available research results also do not comprehensively depict other industries' overall conditions.

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Conflicts of Interest

The author declares no conflict of interest. The funders had no role in the design of the study; in the collection, analyses, or interpretation of data; in the writing of the manuscript, or in the decision to publish the results.



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