CHAPTER I
INTRODUCTION

1.1. Research Background

The application of accrual accounting hoped to show the actual condition of company financial condition. Accrual accounting is reflecting the current condition the firm's financial condition because accrual accounting not only consider the financial transaction but also recognize the non financial transaction that caused the changes in asset, liabilities, and equities. However, the bad side is accrual basis gives flexibility to the manager. Management use the flexibility to met their own interest. This flexibility is an advantageous thing for management if the desired profit target is not achieved. Management pretend to choose accounting methods that will give them benefit as long as they do not violate from Financial Accounting Standards.

The manager utilizes the discretionary principle to intervening in the financial reports for the interests of several parties. This intervention activity is referred to as earnings management. Even though it is in the conceptual framework issued by the FASB, the Objective of financial reporting must provide information that is useful to users in making decisions. The financial statements will categorize as useful to users when it meets the fundamental qualitative characteristics belong to FASB Conceptual framework. The information in financial statements must be relevant information and it is faithful representation. The relevant information means the information contain the information that need by users for what the purpose of the financial statement prepared. Relevance also means the information can make a difference to decision based on the interest of the user. The information can classified as relevance when it has predictive value, confirmatory value and present in material. The faithful representation means the information must be present honestly. The company reported all of material information that will affect in decision making without any information which is hidden. The information can classified faithfull representation

when it present completely , neutral, and free from error (IFRS : Conceptual Framework, 2018)

Healy and Wahlen (1999) argued that earnings management that done by management that provide wrong information would mislead the stakeholder. However, SFAC No 1 stated that financial reporting that prepared by company should provide the information that will beneficial in helping investors and creditors, and other users to assess the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from the sale, redemption, or maturity of securities or loans. So it very important that the earning information is correct and shows the real condition of the company because the quality of earnings is the center of attention for investors, creditors, accounting policymakers, and the government, in this case, the Directorate General of Taxes in decision making.

Earnings management is taken by management to meet the expected earnings of shareholders that are related to the compensation plans because the main management responsibility is to optimize the owner's principal. By doing their duties properly manager hoping to gets higher compensation. According to Murphy (1999), the reported earning is the main criterion to assess the CEO performance because the others such as stock return and stock prices are affected by macroeconomic events and other external factors that managers cannot control. Healy (1985) also investigates motivation do earnings management is related to the bonus plans. The manager would manage the firm's earnings to their advantage to maximize their bonuses under their compensation contract with the firm. Healy's study supports the agency theory, while there an overlapping interest between shareholder and manager. Sincethere are two different interests in the company, each party tries to achieve or maintain the desired level of their prosperity.

Even though almost all the studies argued that earnings management is bad but a specified level earnings management with has advantage for the firm. Scotts (2015) claim that earnings management does not only have a bad side but also has a good

side. Earnings management can be as a tool to reduce blocked communication between management and external financial statement users. Earnings management also used by management to protect the firm from unforeseen event that did not stated in contract that are rigid and incomplete (Scotts, 2015)

In the effort to maximize the firm's earnings the manager try to reduce the expense included reducing the tax burden because the tax directly reduces the company's earnings. Law No. 28 2008 stated that tax is a mandatory contribution to a country that is payable by individuals or entities of nature that regulatate and its witholding forces based on the Law, by not get directly rewarded and used for the state's needs as much as possible prosperity of the people (Law No. 28 2007, PP.1). As the main source of state revenue, the government keeps on increasing tax revenue. In the 2019 National Budget, the government has budgeted Rp.1,780 trillion or about 83.5% of total State revenue. As the largest source of state revenue, the Director-General of Taxes continues to maximize the tax revenue realization. This condition is very contrary to the expectation of taxpayers who want to pay the minimum tax. So, the taxpayers and government have different interests in terms of paying taxes.

For taxpayers, tax can reduce the company's net profits directly after getting operating profit. Therefore, management to reduce the tax burden that must be paid to state , many companies try to manage their tax. The tax manager tries to find the loophole which can be utilized to minimize the firm’s tax. Thus, the manager’s effort to minimize tax payment is called tax planning. Pohan (2013) defines that the tax planning as the efforts made by manager to manage the amount of tax of the company to make the tax burden that should be paid are truly efficient by find gaps between tax regulation and financial statement standard but still in the corridor of tax regulations. The managament hope by doing tax planning , they can pay the company’s as minimize as the can paid. By minimizing the tax payment the manager can maximixe profit after tax. For government side tax planning is very opposite with their goals to optimize the state revenue. Tax planning objective is very opposite with the government goals that willing to collect higher tax from taxpayers. (Suandy, 2008)

In Indonesia, two financial statements should be reported namely financial based on PSAK (Indonesian Accounting Standard) and financial statement based on tax regulation. Meanwhile, when reporting tax firm also should prepare the financial statement based on tax regulation. PSAK and Tax regulation have several differences for a specified term, for example in recognizing depreciation expense, tax regulation distinguishing into several levels based on economic value and economic life that already regulate by Tax Law. The difference of provision affected the firm's earnings. Then, the difference also has an effect to tax payable. The differences between commercial earning and fiskal earnings is commonly called as deferred tax expense (Yulianti, 2004). The difference between coomercial earning which come from financial statements based on PSAK and fiscal earning which come from the financial statement based on tax regulation is one of the instruments for managers to carry out earnings management and will reflect the level of managers' policies in manipulating earnings to be higher (Deviana, 2010; Phillip et al,2003),

One of the newest cases of earnings management in Indonesia is the case of PT. Garuda Indonesia in its 2018 annual report. PT Garuda Indonesia reported a net profit of USD809.85 thousand or equivalent to IDR 11.33 billion (assuming an exchange rate of IDR 14,000 per US dollar). This figure jumped sharply compared to 2017 which suffered a loss of USD216.5 million. Garuda Indonesia includes earnings from PT Mahata Aero Teknologi which has a debt to the airline with the red plate. PT Mahata Aero Teknologi itself has debts related to Wi-Fi installation that has not been paid.

Earnings management is an important topic to research because earning is the main concern of all stakeholders in assessing the performance of the company when in decision making. Based on that, this studyinterest to research with title “The Influences of Tax Planning and Deferred Tax Expense toward The Earnings Management (Empirical Study to The Stated Owned Enterprise that listed in Indonesian Stock Exchange for period 2017-2019)

1.2. Research Problem

Earnings management is an effort to intervene in the company's earning done because of the discretion of management in financial statement preparation. Earnings management because the financial statement loses its reliability. In general earnings, management is a view as a bad thing, because it will mislead shareholders. After all, the managers present wrong information. The wrong information also will make some stakeholder choose wrong decision, finally will make a loss for shareholders or other financial users. So, this study tries to give empirical evidence for earnings management practice by relating it with the tax purpose. The following are the problemof this research:

1. Does the tax planning have a significant influence on earnings management by state-owned enterprises that are listed on the Indonesian Stock Exchange?
2. Does the deferred tax expense have a significant influence on earnings management by state-owned enterprises that are listed on the Indonesian Stock Exchange?
3. Do the tax planning and deferred tax expense simultaneously have influence on earnings management by state-owned enterprises that are listed on the Indonesian Stock Exchange?

1.3. Research Objective

Earnings management can mislead stakeholders because the earning already intervened by them. This study can provide evidence for earnings management practice. So, the objective of this research:

1. To find the empirical evidence about the influence of tax planning on earnings management by state-owned enterprises that are listed on the Indonesian Stock Exchange.
2. To find the empirical evidence about the influence of deferred tax expense on earnings management by state-owned enterprises that are listed on the Indonesian Stock Exchange.

3. To find the empirical evidence that tax planning and deferred tax expense have simultaneous influence toward earnings management by state-owned enterprises that are listed on the Indonesian Stock Exchange.

1.4. Research Contribution

This research's result is expected to contribute to the empirical and practical aspects. For the empirical aspect, this study is expected to gives new insight and support the previous study by using research data that is recent than the previous study. In practical terms, this study is expected can be used as a new reference that can be used as information relating to accounting especially in earnings management by using tax planning and deferred tax as an indicator. It is expected to provide information aimed to give new evidence for earnings management practice so that the negative effect can be reduced.

1.5. Writing Systematics

The writing systematics of this research contains of five chapters, namely: the first chapter is the introduction. This chapter is an introduction to research that consists of background, problem formulation, research objectives, research benefits, and systematic writing. The secondchapter is the literature review. This chapter describes the theoretical foundations used, framework, and hypotheses from this research.

The third is the research methodology. This chapter contains research design, population and sample, types and sources of data obtained, research variables, data analysis methods with hypothesis testing.The next is the results and discussion chapter. This chapter contains a description of the research sample which consists of the resultdata analysis and discussion.The last is the conclusion and suggestion. This chapter contains conclusions, limitations of the research, and recommendations from this study.