

THE EFFECT OF INSTITUTIONAL OWNERSHIP ON EARNINGS MANAGEMENT, WITH CORPORATE SOCIAL RESPONSIBILITY (CSR) DISCLOSURE AS A MEDIATING VARIABLE

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Abstract

This study examines the effect of institutional ownership on earnings management with Corporate Social Responsibility (CSR) disclosure as a mediating variable in basic material sector companies listed on the Indonesia Stock Exchange (IDX) during the 2021–2024 period. The study employed an associative quantitative approach using path analysis and the Sobel test. The research sample consisted of 32 companies with a total of 128 observational data. The results indicate that institutional ownership does not have a significant effect on earnings management, but has a positive and significant effect on CSR disclosure. CSR disclosure also has a negative and significant effect on earnings management and is proven to fully mediate the relationship between institutional ownership and earnings management. These findings indicate that institutional ownership has not been able to directly reduce earnings management practices, but can encourage greater corporate transparency through CSR disclosure.

Keywords: Earnings Management, Institutional Ownership, Corporate Social Responsibility (CSR) Disclosure

INTRODUCTION

The increasingly competitive business environment has encouraged companies to strengthen corporate governance in order to maintain competitiveness and gain stakeholders' trust. One of the primary manifestations of good corporate governance is the preparation of high-quality financial statements that provide reliable information for economic decision-making. Among the information disclosed in financial reports, earnings are considered the most important indicator because they reflect a company's financial performance and future prospects. Consequently, investors, creditors, and other stakeholders rely heavily on earnings information when evaluating corporate performance and making investment decisions (Putri & Wirakusuma, 2022). However, the separation of ownership and management creates agency conflicts that

may motivate managers to engage in opportunistic behavior, including earnings management.

Earnings management refers to managers' deliberate intervention in financial reporting by exploiting the flexibility of accounting standards to influence reported earnings without necessarily changing the company's underlying economic performance (Khairunnissa et al., 2020). Although accounting standards provide managers with discretion in selecting accounting methods, excessive earnings management reduces earnings quality, increases information asymmetry, and potentially misleads investors and other stakeholders (Putri & Kodriyah, 2019). Consequently, earnings management remains one of the most widely discussed issues in accounting research because it directly affects the credibility and transparency of financial reporting.

The phenomenon of earnings management has frequently occurred among Indonesian listed companies. One notable example involved PT Timah Tbk, which restated its 2018 financial statements by significantly reducing its previously reported earnings. The substantial discrepancy between the original and restated earnings raised concerns regarding the credibility of the company's financial reporting and strengthened allegations of earnings manipulation (Christian et al., 2022). Furthermore, previous studies identified repeated earnings management practices among companies included in the LQ45 Index, such as PT Bank Tabungan Negara Tbk, PT Vale Indonesia Tbk, PT Telekomunikasi Indonesia Tbk, PT Indofood CBP Sukses Makmur Tbk, and PT Unilever Indonesia Tbk (Khairiyah & Sari, 2024). These cases demonstrate that opportunistic financial reporting remains a significant issue in Indonesia and highlight the importance of effective corporate governance mechanisms capable of limiting managerial discretion.

One important corporate governance mechanism that has received considerable attention is institutional ownership. Institutional investors generally possess substantial ownership stakes, extensive financial resources, professional expertise, and stronger monitoring capabilities than individual shareholders (Elvina & Karnawati, 2024). According to Agency Theory, institutional investors play an important monitoring role by reducing agency conflicts between shareholders and managers (Jensen & Meckling, 1976). Their ability to supervise managerial decisions is expected to discourage opportunistic behavior and improve the quality of financial reporting. Consequently, higher institutional ownership should reduce managers' incentives to manipulate accounting information and engage in earnings management (Munawar et al., 2024).

Despite this theoretical expectation, previous empirical studies have produced inconsistent findings regarding the relationship between institutional ownership and earnings management. Several studies reported a significant negative relationship, suggesting that institutional investors effectively constrain managerial opportunism (Potharla et al., 2021; Wahyuningsih, 2023). Conversely, other studies found no significant relationship between institutional ownership and earnings management (Febrina & Lekok, 2021; Valensia & Trisnawati, 2022). These inconsistent findings imply that the influence of institutional ownership may operate indirectly through other corporate governance mechanisms rather than solely through direct monitoring.

Therefore, identifying the mechanism through which institutional ownership affects earnings management remains an important research issue.

Corporate Social Responsibility (CSR) disclosure may serve as an important mediating mechanism in explaining this relationship. CSR disclosure reflects a company's commitment to social and environmental responsibilities while simultaneously enhancing corporate transparency and accountability (Akbar & Humaedi, 2020). Stakeholder Theory argues that companies are responsible not only to shareholders but also to broader stakeholder groups whose interests are affected by corporate activities (Freeman, 1984). Institutional investors, as influential stakeholders, increasingly emphasize sustainable business practices and transparent reporting. Consequently, firms with higher institutional ownership are expected to disclose CSR information more extensively in response to investors' demands for greater accountability and sustainability (Rohman, 2024; Prasetyo, 2024).

CSR disclosure has become an increasingly important component of corporate reporting because it communicates companies' environmental, social, and governance commitments beyond financial performance. Comprehensive CSR disclosure reduces information asymmetry, strengthens corporate transparency, and improves stakeholders' confidence in managerial decisions. Previous studies have consistently reported that companies with higher CSR disclosure tend to exhibit lower levels of earnings management because transparent disclosure limits managers' opportunities to manipulate financial information (Nabila & Saiful, 2023; Wati & Malik, 2021). Ethical corporate behavior reflected through CSR activities is therefore expected to complement internal governance mechanisms in reducing opportunistic managerial practices.

Although previous studies have independently examined the relationships among institutional ownership, CSR disclosure, and earnings management, limited research has investigated CSR disclosure as the mechanism through which institutional ownership influences earnings management. Most prior studies focused primarily on direct relationships and provided limited explanation regarding how institutional investors encourage higher financial reporting quality. Accordingly, this study proposes CSR disclosure as a mediating variable that explains the causal process linking institutional ownership to earnings management. Institutional investors may encourage companies to improve CSR disclosure as part of broader corporate governance practices, and greater transparency resulting from CSR disclosure may subsequently reduce managers' incentives to engage in earnings management. This mediating perspective extends previous literature by providing a more comprehensive explanation of how corporate governance mechanisms influence financial reporting quality.

The selection of CSR disclosure as a mediating variable is supported by both Agency Theory and Stakeholder Theory. Agency Theory explains that institutional investors function as monitoring mechanisms capable of reducing agency conflicts between managers and shareholders (Jensen & Meckling, 1976). Meanwhile, Stakeholder Theory emphasizes that companies should maintain accountability toward all stakeholders through transparent and responsible business practices (Freeman, 1984). CSR disclosure therefore represents the practical implementation of

stakeholder accountability while simultaneously reducing information asymmetry, thereby indirectly constraining earnings management.

This study focuses on companies in the basic materials sector listed on the Indonesia Stock Exchange during the 2021–2024 period. The sector was selected because its business activities are closely associated with natural resource utilization, environmental impacts, and public scrutiny regarding sustainability practices. Furthermore, the post-pandemic period has intensified stakeholders' expectations regarding corporate transparency and sustainability reporting. Therefore, the basic materials sector provides an appropriate setting for examining the relationships among institutional ownership, CSR disclosure, and earnings management.

Based on the theoretical arguments, empirical inconsistencies, and practical phenomena discussed above, this study aims to examine the effect of institutional ownership on earnings management, investigate the influence of institutional ownership on CSR disclosure, analyze the effect of CSR disclosure on earnings management, and evaluate the mediating role of CSR disclosure in the relationship between institutional ownership and earnings management. The findings are expected to contribute to the corporate governance literature by providing empirical evidence regarding the indirect role of CSR disclosure in improving financial reporting quality and offer practical implications for corporate managers, investors, and regulators.

RESEARCH METHOD

This study employed an associative quantitative research design to examine the direct and indirect relationships among institutional ownership, Corporate Social Responsibility (CSR) disclosure, and earnings management. A quantitative approach was considered appropriate because the research aimed to test hypotheses derived from Agency Theory and Stakeholder Theory through statistical analysis of secondary financial data. Path analysis was employed to estimate both direct and indirect effects among the variables, while the mediating role of CSR disclosure was evaluated using the Sobel test. Path analysis is an extension of multiple regression that enables researchers to examine causal relationships involving mediating variables.

The study was conducted using secondary data obtained from annual reports and sustainability reports of companies in the basic materials sector listed on the Indonesia Stock Exchange (IDX). The observation period covered four consecutive years, from 2021 to 2024. This period was selected because it represents the post-COVID-19 recovery phase, during which companies experienced increasing pressure to improve corporate governance, sustainability reporting, and financial transparency. The research focused on the basic materials sector because companies in this sector are highly dependent on natural resources and are subject to greater environmental and social scrutiny, making CSR disclosure particularly relevant.

The population consisted of all basic materials companies listed on the Indonesia Stock Exchange during the 2021–2024 period. The sample was selected using a purposive sampling technique to ensure that only companies meeting predetermined research criteria were included. The sampling criteria included companies that were consistently listed during the observation period, published complete annual reports and sustainability-related information, and provided all financial data required to measure the research variables. Based on these criteria, the final sample comprised 32 companies, resulting in 128 firm-year observations.

This study used secondary quantitative data collected through documentation techniques. Financial information, ownership structure, and CSR disclosure data were obtained from publicly available annual reports and sustainability reports published by each company through the Indonesia Stock Exchange and the companies' official websites. Documentation was selected because it provides objective, reliable, and verifiable information that has been publicly disclosed by the sampled companies.

The research involved three variables. Institutional ownership served as the independent variable, earnings management as the dependent variable, and CSR disclosure as the mediating variable. Institutional ownership was measured by the proportion of shares owned by institutional investors relative to total outstanding shares. CSR disclosure was measured using the Global Reporting Initiative (GRI Standards 2021) disclosure index by comparing the number of disclosed CSR items with the total applicable disclosure items. Earnings management was measured using discretionary accruals as a proxy because discretionary accruals are widely recognized as an effective indicator for detecting earnings management practices in accounting research.

Data analysis was performed using IBM SPSS Statistics. The analysis began with descriptive statistics to describe the characteristics and distribution of the research variables. Prior to hypothesis testing, classical assumption tests were conducted, including normality, multicollinearity, autocorrelation, and heteroscedasticity tests, to ensure that the regression models satisfied the assumptions required for path analysis.

Hypothesis testing was conducted using path analysis through two regression equations. The first regression model examined the effect of institutional ownership on CSR disclosure, while the second regression model examined the effects of institutional ownership and CSR disclosure on earnings management. The direct effects were evaluated using regression coefficients and t-tests at a 5% significance level. The coefficient of determination (R^2) was also calculated to evaluate the explanatory power of each regression model. Path analysis is appropriate for estimating both direct and indirect causal effects among variables within a mediation model.

Finally, the mediating role of CSR disclosure was assessed using the Sobel test. The Sobel test evaluates whether the indirect effect of institutional ownership on earnings management through CSR disclosure is statistically significant. A significant Sobel test statistic indicates that CSR disclosure mediates the relationship between institutional ownership and earnings management. The mediation effect was interpreted based on the significance of both the indirect effect and the direct effect after the inclusion of the mediating variable..

RESULT AND DISCUSSION

Findings

This study examines the effect of institutional ownership on earnings management, with Corporate Social Responsibility (CSR) disclosure serving as a mediating variable. The research was conducted on basic materials sector companies listed on the Indonesia Stock Exchange (IDX) during the 2021–2024 period. Using a purposive sampling technique, 32 companies met the established criteria, resulting in 128 firm-year observations. The sample consisted of companies that consistently published annual reports and sustainability reports and provided complete data for all research variables.

Descriptive Statistics

Descriptive statistics were employed to provide an overview of the characteristics of the research variables, namely institutional ownership, CSR disclosure, and earnings management. The results indicate that institutional ownership among the sample firms was relatively high, suggesting that institutional investors remained the dominant shareholders in basic materials companies. This ownership structure reflects the substantial role of institutional investors in corporate governance within the Indonesian capital market.

The average CSR disclosure index was **0.4760**, indicating that, on average, companies disclosed approximately 47.60% of the indicators specified in the GRI Standards 2021. Although this level suggests that firms have implemented sustainability reporting practices, the disclosure remains below full compliance, implying considerable room for improvement. Among the three CSR dimensions, environmental disclosure exhibited the highest average score (**0.5039**), followed by the social dimension (**0.4913**) and the economic dimension (**0.3911**). These findings suggest that companies operating in the basic materials sector place greater emphasis on environmental issues due to the industry's direct environmental impact.

The average value of earnings management was **0.1147**, indicating that earnings management practices still existed among the sampled companies, although the magnitude was relatively low. Furthermore, the variability observed across all

variables demonstrates sufficient heterogeneity among firms, supporting the suitability of the data for subsequent statistical analyses.

Path Analysis

Path analysis was conducted to examine both the direct and indirect relationships among the research variables. The first structural equation assessed the effect of institutional ownership on CSR disclosure. The results revealed that institutional ownership had a **positive and statistically significant** effect on CSR disclosure ($\beta = 0.370$, $p = 0.000$). The Adjusted R^2 value of **0.165** indicates that institutional ownership explained approximately **16.5%** of the variation in CSR disclosure.

The second structural equation evaluated the direct effects of institutional ownership and CSR disclosure on earnings management. Institutional ownership exhibited a coefficient of **-0.009** with a significance level of **0.622**, indicating that institutional ownership did not significantly influence earnings management. In contrast, CSR disclosure showed a **negative and statistically significant** effect on earnings management ($\beta = -0.067$, $p = 0.002$). This finding suggests that companies with more extensive CSR disclosure tend to engage in lower levels of earnings management.

The coefficient of determination for the overall structural model was **0.256**, implying that the proposed model explained **25.6%** of the variation in earnings management, while the remaining **74.4%** was attributable to other variables not included in this study.

Mediation Analysis

The Sobel test was employed to determine whether CSR disclosure mediates the relationship between institutional ownership and earnings management. The results demonstrate that the indirect effect of institutional ownership on earnings management through CSR disclosure was **-0.025**, while the total effect was **-0.034**. These findings confirm that CSR disclosure serves as a **full mediating variable**, indicating that institutional ownership influences earnings management indirectly through enhanced CSR disclosure rather than through a direct governance mechanism.

Analysis/Discussion (1000-1500 words)

H1: The Effect of Institutional Ownership on Earnings Management

The empirical findings indicate that institutional ownership does not have a statistically significant effect on earnings management. Therefore, the first hypothesis is not supported. Although institutional investors are generally expected to possess greater monitoring capabilities due to their financial resources, expertise, and voting power, the findings suggest that these advantages do not necessarily translate into effective oversight of managers' financial reporting behavior.

From the perspective of Agency Theory, institutional ownership is expected to reduce agency conflicts by strengthening monitoring mechanisms and limiting managerial opportunism. However, the insignificant relationship observed in this study

implies that institutional investors may prioritize investment performance and long-term financial returns rather than actively monitoring accounting policies or earnings reporting practices. In addition, some institutional investors may behave as passive shareholders, reducing their direct involvement in managerial decision-making.

This finding is consistent with previous studies by Valensia and Trisnawati (2022) and Febrina and Lekok (2021), which also reported that institutional ownership does not significantly constrain earnings management. Consequently, institutional ownership alone may not be sufficient to improve financial reporting quality without complementary governance mechanisms.

H2: The Effect of Institutional Ownership on CSR Disclosure

The results demonstrate that institutional ownership has a positive and significant effect on CSR disclosure, supporting the second hypothesis. This finding indicates that firms with higher institutional ownership tend to disclose more comprehensive CSR information.

According to Stakeholder Theory, institutional investors represent influential stakeholders who increasingly consider environmental, social, and governance (ESG) performance when evaluating corporate sustainability. Consequently, institutional shareholders encourage firms to enhance transparency and accountability by expanding CSR disclosure. Comprehensive CSR reporting enables companies to communicate their commitment to sustainable business practices and strengthens their legitimacy among stakeholders.

Institutional investors are generally more concerned with long-term corporate value than short-term financial performance. Therefore, they are likely to encourage management to adopt broader sustainability reporting practices as part of effective corporate governance. This result supports previous findings reported by Rohman (2024) and Prasetyo (2024), who found that institutional ownership positively influences CSR disclosure.

H3: The Effect of CSR Disclosure on Earnings Management

The third hypothesis is supported, as CSR disclosure negatively and significantly affects earnings management. This result suggests that companies with more extensive CSR disclosure are less likely to engage in opportunistic earnings manipulation.

From the perspective of Stakeholder Theory, extensive CSR disclosure reflects higher levels of corporate transparency and accountability. Companies committed to sustainability are expected to maintain consistency between financial and non-financial reporting. As transparency increases, opportunities for managerial opportunism become more limited because stakeholders can evaluate corporate performance more comprehensively.

Moreover, CSR disclosure enhances corporate credibility and reduces information asymmetry between management and stakeholders. Firms that voluntarily disclose broader sustainability information are likely to maintain higher reporting quality to preserve stakeholder trust. Consequently, managers have fewer incentives to manipulate accounting earnings. This finding is consistent with the

studies of Nabila and Saiful (2023) and Wati and Malik (2021), both of which concluded that CSR disclosure significantly reduces earnings management practices.

H4: The Mediating Role of CSR Disclosure

The Sobel test confirms that CSR disclosure fully mediates the relationship between institutional ownership and earnings management. Therefore, the fourth hypothesis is supported. The absence of a significant direct relationship between institutional ownership and earnings management, combined with the significant indirect relationship through CSR disclosure, indicates that institutional investors influence earnings management primarily by encouraging greater corporate transparency rather than through direct monitoring.

This finding provides empirical support for integrating Agency Theory and Stakeholder Theory. Agency Theory explains that institutional investors serve as monitoring mechanisms designed to mitigate agency conflicts. However, the results indicate that such monitoring becomes effective only when it is translated into stronger transparency practices through CSR disclosure. Stakeholder Theory further explains that broader CSR disclosure enhances accountability to stakeholders, thereby discouraging opportunistic managerial behavior.

The evidence suggests that CSR disclosure functions as an effective governance mechanism linking ownership structure and financial reporting quality. Institutional investors encourage companies to strengthen sustainability disclosure, which subsequently improves transparency and reduces earnings management practices. Accordingly, CSR disclosure represents an important governance channel through which institutional ownership contributes to higher financial reporting quality in Indonesian basic materials companies.

CONCLUSION

This study investigates the relationship between institutional ownership, Corporate Social Responsibility (CSR) disclosure, and earnings management in basic materials companies listed on the Indonesia Stock Exchange during the 2021–2024 period by examining both the direct effect of institutional ownership on earnings management and the indirect effect through CSR disclosure. Grounded in Agency Theory and Stakeholder Theory, the study seeks to explain how institutional investors, through their monitoring role, may encourage greater corporate transparency and accountability, thereby improving the quality of financial reporting. The findings are expected to contribute to the corporate governance literature by providing a better understanding of the mechanism through which CSR disclosure may mediate the relationship between institutional ownership and earnings management. Practically, the study offers insights for corporate managers, investors, and regulators regarding the importance of strengthening institutional monitoring and enhancing CSR disclosure to support transparent and reliable financial reporting. Nevertheless, this study is limited to companies in the basic materials sector and a four-year observation period; therefore, future research is recommended to examine other industrial

sectors, extend the study period, and incorporate additional corporate governance or Environmental, Social, and Governance (ESG) variables to provide a more comprehensive understanding of the determinants of earnings management.

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