THE 12TH MALAYSIA-INDONESIA INTERNATIONAL CONFERENCE ON ECONOMICS, MANAGEMENT, AND ACCOUNTING 2011

MIICEMA

"Borderless Economy: Opportunities and Challenges for Businesses in Southeast Asia"

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Magister Perencanaan Pembangunan
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PROCEEDINGS

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HISTORY OF MIICEMA

After successful the Malaysia-Indonesia International Conference on Economics, Management and Accounting 2010 (MIICEMA 2010) hosting by the Faculty of Economics and Business, Universiti Kebangsaan Malaysia, this year 2011, Universitas Bengkulu will host the same conference for the third time. At 12th conference with theme "Borderless Economy: opportunities and challenges for Enterprises in Southeast Asia", new members, Universitas Padjajaran, Bandung and Universitas Malikussaleh take part on the collaboration.

Here the list of detail history of MIICEMA from 1993 until 2010:

1993	The first conference was co-organized by the Faculty of Economics and Faculty of Business Management (UKM) and Universitas Syiah Kuala Banda Aceh. With a theme "Economics and Business Issues (Isu-isu Ekonomi dan Perniagaan)", the conference was held on 5 – 6 June 1993 at Universitas Syiah Kuala Banda Aceh.
1994	The second conference was co-organized by the Faculty of Economics and Faculty of Business Management (UKM) and Universitas Syiah Kuala Banda Aceh. The conference theme was "Economics Prospects and Challenges in Industrial Development (Prospek dan Cabaran Ekonomi dalam Pembangunan Industri)". The conference was held on 19 – 20 July 1994 at Universiti Kebangsaan Malaysia.
1995	The third conference was co-organized by the Faculty of Economics and Faculty of Business Management (UKM) and Universitas Syiah Kuala Banda Aceh. The conference theme was "Strengthening Malaysia and Indonesia Cooperation: To Succeed the 2020 IMT-GT (Memperkukuhkan Kerjasama Malaysia dan Indonesia: Mensukseskan IMT-GT Tahun 2020)". The conference was held in August 1995 at Universitas Syiah Kuala Banda Aceh.
1996	The fourth conference, which was upgraded to an international level, was again co-organized by the Faculty of Economics and Faculty of Business Management (UKM) and Universitas Syiah Kuala Banda Aceh. The conference theme was "Globalization Issues in Economics and Business (Isu-isu Globalisasi dalam Ekonomi dan Perniagaan)". The conference was held on 12 – 13 November 1996 at Puri Pujangga, Universiti Kebangsaan Malaysia.
1997	The fifth conference was co-organized by the Faculty of Economics and Faculty of Business Management (UKM), Universitas Syiah Kuala Banda Aceh and a new member university, Universitas Bengkulu. The conference theme was "Managing Growth and Changes". The conference was held on 23-25 June 1997 at Universitas Bengkulu.
2002	The sixth conference was co-organized by the Faculty of Economics and Faculty of Business Management (UKM), Universitas Syiah Kuala Banda Aceh and Universitas Bengkulu. The conference theme was "The Role and Harmonization of Economics and Business Disciplines in Global Competitiveness". The conference was held on 14-15 October 2002 at Universitas Syiah Kuala, Banda Aceh.
2003	The seventh conference was co-organized by the Faculty of Economics and Faculty of Business Management (UKM), Universitas Syiah Kuala Banda Aceh and Universitas Bengkulu. The conference theme was "Sustainable Economics and Business Development in an Era of Globalization". The conference which was hosted by the Faculty of Economics and Faculty of Business Management (UKM) was held on 13-14 October 2003 at Equatorial Hotel, Bangi.
2004	The eighth conference witnessed the collaborative effort of the trio universities was further strengthened by the involvement of Brunei Darussalam. The conference theme was "Asian Competitiveness in Economics and Business Sector Towards an Era of Globalization". The conference was held on 2-6 October 2004 at Universitas

	Bengkulu.
2005	The ninth conference was welcome another new member university, Universitas Muhammadiyah Surakarta, as the co-organizer of the conference. The conference theme was “Empowering Economic and Business in the Free Trade Era”. The conference was held on 13-14 December 2005 at Universitas Muhammadiyah Surakarta.
2008	The tenth conference was co-organized by the Faculty of Economics and Business Management (UKM), Universitas Syiah Kuala Banda Aceh, Universitas Bengkulu and Universitas Muhammadiyah Surakarta. The conference theme was “Developing Regional Economy through Networking: Role of Small Medium Enterprises (SMEs)”. The conference was held on 27-28 October 2008 at Universitas Syiah Kuala Banda Aceh.
2010	The eleventh conference was co-organized by Faculty of Economics and Business, Universiti Kebangsaan Malaysia, National University of Malaysia, Universitas Syiah Kuala Banda Aceh, Universitas Bengkulu, Universitas Muhammadiyah Surakarta, and Institut Pertanian Bogor. The conference theme was “Regional Development in an Era of Global Innovation Economy””. The conference was held on 25-26 October 2010 at Universiti Kebangsaan Malaysia.

Greeting from the Rector

Assalamu'alaikum wr.wb. dan salam sejahtera

Dear participants, guesses and colleagues

First of all, I would like to express my gratitude to each and every one of you for your participation on this 12th Malaysian-Indonesian International Conference on Economics, Management and Accounting 2011 here in Bengkulu. I also would like to give my highly appreciation to the organizing committee, the faculty of Economics, University of Bengkulu, in cooperation with Universiti Kebangsaan Malaysia, Universitas Syiah Kuala Aceh, Universitas Muhammadiyah Surakarta, Institut Pertanian Bogor, and Universitas Padjajaran, Bandung. With their strong will and hard work, this conference can be successfully held.

Since it began in 1993, MIICEMA has been a huge success, providing a great opportunity to develop our knowledge on Economics, Managements and Accounting through networking, studies and researches - not to mention the opportunity to make new friends, meet old acquaintances and discover new places in both countries, Indonesia and Malaysia. And with this year's theme "Borderless Economy: Opportunities and Challenges of Business in Southeast Asia", It is my sincere expectation that there is also borderless collaboration between Indonesia and Malaysia and other countries as well in the future.

I hope that you will find the conference both enjoyable and valuable and also enjoy the cultural and natural beauty of Bengkulu. For all our guesses, national and international, may you have a pleasant stay in Bengkulu.

Wassalamu'alaikum wr.wb.

Sincerely,

Prof. Ir. Zainal Muktamar, M.Sc.

Greeting from the Dean

First and foremost, I wish to express my utmost gratitude to God for bestowing upon us His blessing to successfully organize the 12th Malaysia-Indonesia International Conference on Economics, Management and Accounting 2011. Welcome or *Selamat Datang* to Bengkulu and welcome to the Land of Rafflesia. Rafflesia is the biggest flower in the world existing in Bengkulu. I would like to express my gratitude to the Universiti Kebangsaan Malaysia, Universitas Syiah Kuala Banda Aceh,

Universitas Muhammadiyah Surakarta, and Universitas Pertanian Bogor for graciously co-organizing this International Conference. In the future, there some other universities will join as co-organizers in this conference.

The main objective to hold this seminar is to exchange ideas and information, and to promote the understanding and cooperation among participants from various countries. Hopefully friendship and understanding can be achieved through this seminar. The theme of this conference is "Borderless Economy: Opportunities, Challenges for Business in Southeast Asia." This theme is highly appropriate to assist regional development to ensure the success of business in the region. The thought share in this conference would benefit policies for the future.

Last but not least, my greatest appreciation goes to all who have contributed to the success of this conference, in particular the presenters, participants, sponsors, the organizer and its committee members. I wish you all have a fruitful discussion. To our special guests from Malaysia, Thailand, UK, Iran, India, and Australia, I hope you have a pleasant stay in Bengkulu the home of Rafflesia Arnoldi.

Warmest regards,

Dr. Ridwan Nurazi, SE., M.Sc., Akt

Greeting from the Conference Chair

Welcome to the 12th Malaysia-Indonesia International Conference on Economics, Management, and Accounting 2011 **(MIICEMA)** in the University of Bengkulu, Indonesia. It is the third time the Faculty of Economics of the University of Bengkulu proudly hosts the conference. It is the first time that participants are coming from seven countries around the world such as Malaysia, Thailand, Australia, India, Iran, United Kingdom, and Indonesia. It seems that the conference has attracted researchers around the globe to share their ideas in our conference.

The theme of "Borderless Economy: Opportunities and Challenges for Businesses in Southeast Asia'' was chosen to anticipate the impacts of volatility in the recent global economy trends toward South East Asia economy. I believe that the theme is relevant since the world economy is becoming borderless and what happen in other parts of the world to some extent will greatly influence our regional business and economy.

One hundred and twenty three papers from thirty seven universities and seven countries will be presented by academicians and researchers. The researchers will exchange ideas derived from their studies and practices. It is expected that the conference would provides significant contributions to policy makers in the region.

I would like to thank the Director of Center for Central Banking Education and Studies of Bank Indonesia, Mr. Rizal A. Djaafara, and Vice President of RMUTSV Thailand, Prof. Aswin Promsopa for becoming our keynote speakers. My deepest appreciation goes to the deans of the conference co-organizers: Universiti Kebangsaan Malaysia, Universitas Syiah Kuala Banda Aceh, Universitas Muhammadiyah Surakarta, Institut Pertanian Bogor, and Universitas Padjajaran. I would like to express my gratitude to our sponsors: Bank Indonesia, Bank Bengkulu, Telkomsel, Pemda Provinsi Bengkulu, Pemda Kota Bengkulu, Bengkulu Ekspress, and ISEI Cabang Bengkulu who have provided endless support for the conference. Last but not least, I thank all committee members for their effort and commitment to the success of the conference. I hope all participants have sweet memories of visiting our city, Bengkulu. Thank you very much.

Sincerely yours,

Prof. Lizar Alfansi, PhD

SEASONED EQUITY OFFERINGS: BETWEEN *AGENCY THEORY, WINDOWS OF OPPORTUNITY,* AND FIRM PERFORMANCE

By:
RIDWAN NURAZI
FITRI SANTI
LIANA DESWITA

ABSTRACT

The purpose of this study was to examine the effect of discretionary total accruals (earnings management) to operating performance and stock return of companies doing seasoned equity offerings (SEO) in the Indonesia Stock Exchange. This research was also to know the signifacant differences in operating performance and stock performance between SEO firms and non-SEO firms. Tests were conducted against 23 SEO going public firms and 25 non SEO going public firms during the years 1996-2006, with the period of observation for three years before SEO, as SEO, and three years after SEO. Model used to test earnings management is using a Modified by Jones Model.

Proxies used to measure earnings management is the discretionary total accrual, operating performance measured by return on assets and stock performance measured by cumulative abnormal return. This study uses a simple linear regression and different test using independent sample t-test.

This research found that the sample firms in this study perform earnings management with the pattern of income decreasing at the SEO. The study also found evidence that earnings management affects the operating performance and stock performance of SEO firms. However, researchers found no evidence that there are significant differences between operating performance and stock performance among SEO companies compared to non-SEO firms.

Key words: Earnings management, SEO, Operating performance, Stock performance.

INTRODUCTION

There are several reasons why a company re-offers shares to the public. First to obtain additional funds in order to finance and develop its business (investment decisions). Second to change the debt with equity (funding decisions) (Husnan, 2001, Keown *et al*., 2001, and Brigham, 2001). SEO is an additional equity offering the company made public outside equity offered to the public through *initial public offerings* (IPO) (Megginson, 1997, Fidyati, 2004).

Performance degradation is a phenomenon that often occurs at the time of SEO. This decreasing performance can be expalined by *agency theory* and *windows of opportunity.* The concept of *agency theory* states that the company is a contract between the owner (as principal) and management (as agent) (Jensen and Meckling, 1976, Brigham and Houston, 2001, Keown *et al*., 2001). Although information regarding companies that conduct *seasoned equity offerings* available in the market, information asymmetry still occur when bidding is done. This is what encourages and motivates managers to behave opportunistically. Manipulation, known as *earnings management* performed by the manager before doing SEO. *Earnings management* can be explained by the *discretionary accruals,* which is the pattern of the company's financial performance prior to the SEO, SEO is going to increase, peaking at SEO and decreased after the SEO.

Corporate managers that manipulate the financial statements cannot maintain the situation in the long run and result in performance degradation *(underperformance)* post SEO offerings (Loughran & Ritter, 1997; Rangan, 1998).

Income increasing as a form of earnings management can be done by sliding the future income to current period, and the current cost be shifted to future cost. As a result, current profit around the SEO be reported higher than it should. High level of profits can not be maintained to future period since management has been shifting future profit to current profits, so that the current period earnings in future period tend to decrease. Decline in earnings in the future periods will eventually cause a decline in operating performance after the SEO. This may imply that earnings management can not be done continuously. Earnings management will affect the company's operating performance whether in the short run or in the long run.

Windows of opportunity are conceptually describe that managers seeking to use the opportunity at the time knowing the market has assessed the company *overvalued* (Cai and Loughran, 1998). In the long run these assessments cannot be sustained because the market make corrections to the company's stock price so that the company's stock price finally will drop significantly.

Research on *seasoned equity offerings* has been done several times in Indonesia (Sulistyanto and Wibisono, 2003; Mardiyah, 2003; Fidyati, 2004: Fidyati and Machfoedz, 2004). Based on the results of research conducted by previous researchers, this research is interested in re-test the research using period 1996 to 2006.

Specifically, this research aims: (1). To prove that if managers behave opportunistically, then the *total discretionary accruals* can predict the decline in operating performance. (2). To prove that if managers behave opportunistically, then the *total discretionary accruals* can predict the decline in stock performance. (3). To prove that there are significant differences in operating performance between companies that do SEO and companies that do not perform SEO. (4). To prove that there are significant differences in stock performance between companies that do SEO with the companies that do not do SEO.

Literature Review and Hyphothesis Development

Seasoned Equity Offerings

Seasoned Equity Offerings (SEO) is an additional equity offered to public, outside equity offered to the public through *initial public offerings* (IPO) (Megginson, 1997; Ross, 2001; Ross *et al,* 2002). SEO mechanism can be done in two ways, first, through right issues or sell the right to the existing shareholders to buy additional shares at a certain price at any given moment. This mechanism is usually done by a company whose ownership is concentrated, with the aim to protect the interest of existing shareholders and to maintain their equity the same as before (*preemptive right*) (Jones, 2004). Second, through selling *second offerings* or *third offerings*, and so on to any investors interested to buy (Megginson, 1997, Brigham and Houston, 2001).
Sharpe *et al.,* (1995) explains that the announcement of SEO seems to result in a decrease of share price. Chiu (2006) describes the company plans to publish the SEO should be

noted on the *Securities Exchange Commission* (SEC) for approval. Chiu (2006) also mentions that SEO is usually offered under price before announcement.

Agency Theory and Earnings Management

Agency Theory states that the company is a contract between the owner as a *principal* and management as an *agent* (Jensen and Mecklin, 1976, Brigham and Houston, 2001). The process and the implementation of the contract may cause a conflict of interests and *dysfunctional behavior* (agents often do the deed deviant). Jensen and Meckling (1976), mentioned that *agency problem* occured when *principal* or the owner delegates its authority to the management as an *agent*. According to Ross, *et al* (2002); (Scott, 2000) conflict of interest happened when each individual try to maximize their own wealth. The effect of this situation is the existence of asymmetry information between *principal* and *agent* (Teoh *et al*., 1998, Keown, *et al*., 2001).

Scott (2000) argued that, there are two kinds of information asimmetry, namely: (1), *Adverse Selection*, describe that managers and insider people typically know more about the state and the firm's prospect than outside investors. (2), *Moral Hazard,* describe that the activities carried out by a manager is not fully known by shareholders and lenders. Managers may violate the contract and the actual ethics or norms.

There are several motivations that encourage managers to do *earnings management.* One of them, according to Scott (2000), is a motivational communication information to investors at the SEO. *Earnings management* is done in order to make company's performance look good and will ultimately increase the value of firms which is reflected in its stock price. Earnings management can be done by selecting particular accounting policies that are used for specific purposes (Scott, 2000). Earnings management practices can be implemented as: (a). *Taking a Bath.* (b). *Income minimization.* (c). *Income Maximization,* and the most popular one (d). *Income Smoothing.*

Manipulation of performance ahead of *seasoned equity offerings* is a logical explanation of why companies cannot afford maintain its performance. Managers to manipulate the performance using *discretionary accruals,* namely accounting policy that provides flexibility in management to determine the number of transactions accrued. Manipulation known as *earnings management* is opportunist attitude as a reflection of the manager to return a profit to himself. So cyclical patterns is as follows: the increase in earnings before offer stocks, peaking at the time of bidding and decreased after the offering *(Underperformance).* This indicates the opportunist attitude of managers to raise the share price offers (Kim and Shin, 2001).

Motivations that drive managers to implement earnings management (Scott, 2000) namely: (1). *Bonus Plan Hypothesis*: Managers with bonus plans are motivated to choose accounting procedures by shifting profits from future periods to current period. (2). *Debt Covenant Hypothesis* (hypothesis debt agreement): The closer a firm will violate its debt agreements, it will motivate managers to choose accounting procedures by shifting the income from future periods to current period. (3). *Political Cost Hypothesis*: The greater the political costs faced by the company it will motivate managers to shift current income into earnings coming period.

According to Scott (2000) there are other motives that motivate managers to do earnings management, namely: (1). *Political Motivation*: many companies secretly has a political vision. It can encourage managers to conduct the practice of earnings management in order to cover up or hide the political vision they have. One is by doing the selection of accounting methods and procedures that can minimize their net income while they experience high rates of return. Reporting higher profits will encourage the public to ask the government to change regulation. (2). *Taxation Motivation*: tax revenue is expected to be the most obvious motivation for managers to practice earnings management. For tax purposes, managers tend to choose policies and procedures regarding the accounting rules that could reduce corporate earnings are taxed, for example the firm will change inventory methods from FIFO to LIFO when preparing financial statements. (3). Change of CEOs *(chief executive officers):* based on the *bonus plan hypothesis,* when the CEO which will expire assignment or retirement, they will make a strategy to maximize profits to boost bonus. Similarly, the CEO whose performance is less good, will tend to maximize profits in order to prevent or undo from the dismissal. (4). *Initial Public Offering* (IPO): Information on the company's net income can be used as a signal to prospective investors about the value of the company. Companies that *went public* tend to manage their reported earnings in the prospectus with the hope of receiving high-share offering price. (5). Providing Information to Investors: rational investors are more interested in the performance of major companies in the future, and investors will use the current reported earnings to predict the likely performance of the company in the future. Management is a party that knows well about the *inside information* about future earnings or prospects of the companies.

Windows of Opportunity

Nizar (2000) defines *windows of opportunity* as the use of limited time on the opportunity. For example, when a number of new shares issued, society only have a few months or a maximum of one year to execute, after that period the opportunity will lost forever, that period is called *windows of opportunity.* Conceptually, the *windows of opportunity* make the manager tried to take advantage of the opportunity at the time knowing the market has assessed the company *overvalued.* In the long run these assessments cannot be sustained because the market will make corrections to the company's stock price, then the company's stock price will drop significantly. Clarke *et al.,* (1998) and Cai and Loughran (1998) mentioned that *insiders* seek to exploit *windows of opportunity* by trying to offer equity when *overvalued.*

The decreasing performance may be caused by the insider, who is usually the people who have private access to information systems, such as managers, company officers, directors or majority shareholder of the issuer. They may know more about the company information compared to other outsiders. This is consistent with the concept of information asymmetry between managers and markets, namely the concept that explains the benefits managers have because they control more than the *private information* of investors, so that managers will only issue additional equity if the manager believes that the company *overvalued.*

Hypothesis

1. Opportunistic Attitudes of Managers and Performance Degradation.

Decrease in performance *(underperformance)* do tend to follow the initial public offering (IPO) and *seasoned equity offerings* (SEO). Performance degradation occurs because of the efforts of management to manipulate the company's reported performance before and during the bidding period by shifting profits to come to the present period and shift the cost of current period into future periods in order to give a positive impression to investors that the shares offered responded positively by the market. A decline in future corporate performance due to companies are not able to continue the manipulation carried out at the time of SEO.

Based on Rangan's research (1998) which examines the phenomenon of the decline in stock *returns* after the publication of SEO, and research by Fidyah and Machfoedz (2004) who examine earnings management carried out before the SEO, found that there is a negative relationship with performance in the period after the SEO. Research by Sulistyanto and Wibisono (2003) on the company that publishes the SEO period 1994-1997 showed that the decrease in performance after *seasoned equity offerings* are caused by the *opportunist* attitude of corporate managers. Research by Sulistyanto and Midiastuti (2002) suggested a decline in financial performance after the SEO, then the variable ROA strengthen these allegations. Based on some previous research, the hypothesis formulated in this study are as follows:

H_1 : If managers behave opportunistically, then the *discretionary accruals* can predict the decline in operating performance.

H_2 : If managers behave opportunistically, then the decrease in *discretionary accruals* can predict the decline in stock performance.

The Performance of SEO and non-SEO Companies

Operating performance and stock performance of SEO firms in the period after the SEO will perform significantly lower when compared with non-SEO firms. This is due to manipulation of managers namely *income increasing. Income increasing* in the form of manipulation is done by shifting the future income to current period and the current cost will be shifted as the cost to come, so the earnings period at about SEO is reported to be higher than it should. But the high rate of profit cannot be shown in the next year as the management has been shifting income to future periods so that the current period earnings in future periods tend to decrease. Decline in future earnings will eventually cause a decline in operating performance after the SEO. Teoh *et al* (1998) examine the phenomenon of earnings management performed by a company that does SEO and companies that do not perform SEO. Issuers and non-issuer companies perform the same *income* in the prior year. Harto (2001) tested the hypothesis that there was no significant difference in financial performance and stock performance of companies that do the *right issues* and companies that do not do the *right issues.* The results of the analysis on the performance of stock returns by Harto (2001) consistently demonstrated the performance of the stock issuer company that *underperformance* compared with non issuer company and in comparison with the market.

Loughran and Ritter (1997) conducted research on the SEO company. The research looked at the performance of the company's operations before and after five years of SEO by using six financial ratios namely *OIBID (operating income before depreciation, amortization, and taxes plus interest income) / Assets, Profit Margin, ROA, OIBID / Sales, CE (capital expenditure) + RD (research and development) / Assets, Market / Book.* Loughran and Ritter (1997) using a 1338 sample of firms from Nasdaq, Amex and NYSE under the period 1979-1989. Other data are obtained from CRSP *(Chicago Center for Research in Security Prices).* The survey results revealed that all financial ratios used in this study has increased ahead of supply, especially for ROA and decreased at the time after the offering. *Profit margins* and return on assets fell by half over four years after the offering. The decline was statistically significant compared to non-issuer companies. Based on previous research that found some evidence that operating performance and stock performance of SEO firms are significantly decreased in the long run compared to non-issuer firms. The hypothesis formulated in this study are as follows:

H_3: There are significant differences in operating performance between companies that do SEO and companies that do not perform SEO.

H_4: There are significant differences in stock performance between companies that do SEO and companies that do not do SEO.

RESEARCH METHOD

This research can be classified as empirical research. *Empirical research* is an empirical study of the facts obtained by observation or experience (Indriantoro and Supomo, 2002, Sekaran, 2009).

Sampling methods

This study took a sample of the population of companies listed on the Indonesia Stock Exchange that does SEO in the form of *a rights issue* in 1996 until 2006. Selection of samples using *sampling* methods that are classified as *judgment* or *purposive sampling method.* The use of *judgment sampling* method means that elections are not conducted in a random sample whose information is obtained by using certain considerations, this is generally adapted to the purpose or research problem. As for the consideration of sample selection in this study are as follows: (1). SEO Company made between 1996 to 2006. (2). SEO companies do at least have made IPO *(initial public offerings)* within two years earlier. (3). SEO companies do more than once should have a period of time between the SEO for a minimum of four years. This is to see the influence of an SEO activities within three years. (4). Data publishing financial reports are available for seven consecutive years beginning three years before up to three years after the events of SEO, so the total available financial statement data from 1996 to 2006.

Based on these criteria, the final sample obtained were 23 companies. For the comparison sample (non SEO) company that *matched* the selected sample based on some predetermined criteria. These criteria are the company that is not doing SEO activities during the period 1996-2006. Another criterion is the company's industry has characteristics similar to the sample and the total equity firms in the same range. If not available in a single company the same industry, then sampled in an adjacent industry. Based on these criteria was selected as many as 25 non-SEO firms.

Data Collection Methods

The data used in this study is secondary data. Indriantoro and Supomo (2002), and Sekaran (2006) states that secondary data is the source of the data obtained indirectly through the media intermediaries, which are generally in the form of evidence, records or historical reports that have been arranged in the archives (documentary data) whether published or not published. The required data in this study are as follows: (1). Net income and cash flow from operating activities which are used to calculate the total *accrual.* (2). The book value of fixed assets and depreciation which are used to calculate gross PPE *(property, plant and equipment)*. (3). Total *assets,* total *sales,* total *accounts receivable* in the period a year before the SEO that is used for the calculation of delta fixed assets, the value 1/TAt-1, *sales delta,* delta *accounts receivable.* (4). *Return on assets of* the period before the SEO which are used to calculate the change in *return on assets.* (5). Company’s *monthly closing price* to calculate the company's stock *return.*

Variable Measurement

Earnings Management

Level of earnings management done by managers can be measured using a measuring instrument in the form of *discretionary total accruals.* Analysis of *discretionary total accruals* in this research is implemented using the *modified Jones model.*

This model uses total *accruals* (TAC), which then classified into component *Discretionary Total Accrual* (DTAC) and *Nondiscretionary Total Accrual* (NDTAC). Total *accruals* (TAC) is defined as the difference between the reported *income* from continuing operations and operating cash flow. To obtain the value of DTAC, the first step have to do is find the value of the TAC by using the formula as follows:

Total *accruals* (TAC) consist of *current accruals* (CA) or *working capital accruals,* and *long-term accruals* (LA). TAC is calculated such as:

$$\begin{aligned} \textbf{TAC} &= \textbf{CA + LA} \\ &= \textbf{\textit{Net Income - Cash Flows from Operations}} \end{aligned} \qquad \textbf{A.1}$$

Where:

TAC = Total *accrual* period t
NI = Net Income
CFO = Cash flow from operational

Then, calculate the value of total *accrual* that are estimated using *Ordinary Least Square* (OLS) regression, as follows:

$$\frac{TCA_t}{TA_{t-1}} = \alpha_0\left(\frac{1}{TA_{t-1}}\right) + \alpha_1\left(\frac{\Delta SALES}{TA_{t-1}}\right) + \alpha_2\left(\frac{PPE_t}{TA_{t-1}}\right) + \varepsilon_t \qquad \textbf{A.2}$$

Where:

Ta t -1 = Total Asset period t – 1
SALest = Changes in net sales in period t
PPE = *Property, Plant and Equipment Gross*
= Regression coefficient
ε = *error term*

Using the above regression coefficient (α0, α1, α2), so the formula value NDTAC can be calculated with:

$$NDTAC = \alpha_0\left(\frac{1}{TA_{t-1}}\right) + \alpha_1\left(\frac{\Delta SALES_t - \Delta A/R_t}{TA_{t-1}}\right) + \alpha_2\left(\frac{PPE_t}{TA_{t-1}}\right) \qquad \textbf{A.3}$$

Where:

NDTAC = *Nondiscretionary total accrual*
RECt = Changes in net account receivables in period t
$\alpha_0, \alpha_1, \alpha_2$ = Regression coefficient
ε = *error term*

DTAC is the difference quotient between total *accruals* to total assets of the previous period with a value of nondiscretionary accruals. DTAC is calculated using the formula:

$$DTAC = \left(\frac{TAC_t}{TA_{t-1}}\right) - NDTAC \qquad \textbf{A.4}$$

Where:
DTAC= *Discretionary total accrual*

Operating Performance

Operating performance in this study were measured by the change of *Return On Asset* approach. *Return On Assets* (ROA) is a ratio that measures the ability of companies to make a net profit based on a certain level of assets (Halim and Hanafi, 2003).

$$\mathbf{ROA_{it} = LBSE_{it} / TA_{it-1}} \qquad \textbf{A.5}$$

Where :
ROA it = *Return on Asset* firm i at period t
LBSE it = company's net income i at period t
TA it – 1 = company's fixed assets i at period t-1

In order to find out whether the company's performance declined after the SEO, then the change of ROA will be compared between before and after the SEO. Then it will be testing the relationship between the changes in *Return on Assets* (ΔROA) with variable *discretionary total accruals* (DTAC). This is done to look at the ability of these variables to predict the performance of the company after the SEO. The relationship between earnings management and changes in ROA is measured by the following equation (Rangan, 1998):

$$\mathbf{\Delta ROA_1 = \lambda_0 + \lambda_1\ DTAC_0 + \lambda_2\, SGRO_0 + \varepsilon} \qquad \textbf{A.6}$$

Dimana:

$\lambda_0, \lambda_1, \lambda_2$ = Koefisien regresi
ΔROA_1 = perubahan *return on asset* dalam periode setelah SEO
$DTAC_0$ = *Discretionary total accruals* di sekitar SEO
$SGRO_0$ = Pertumbuhan penjualan

Stock *Return*

The influence of earnings management by stock *returns* proved by using the following equation:

$$\mathbf{CAR_i = \beta_0 + \beta_1\ DTAC_i + \beta_2\, \Delta ROA + \varepsilon} \qquad \textbf{A.7}$$

Dimana:

CAR_i = *Cummulative abnormal return* perusahaan
$\beta_0, \beta_1, \beta_2$ = Koefisien regresi

Cumulative abnormal return (CAR) in this study was calculated with *the adjusted market model approach.* Using this model, the *cumulative abnormal return* calculated based on the following formula:

$$\mathbf{CAR_{it} = \Sigma((1 + R_{it} / 1 + R_{mt}) - 1)} \qquad \mathbf{A.8}$$

Dimana:

R_{it} = *Return* saham perusahaan i pada periode t
R_{mt} = *Return* pasar pada periode t

Return perusahaan i pada periode dihitung dengan rumus berikut:

$$R_{it} = \frac{P_t - P_{t-1}}{P_{t-1}}$$

Dimana:
R_{it} = *Return* perusahaan i pada bulan t
P_t = Harga saham penutupan perusahaan pada bulan t
P_{t-1} = Harga saham penutupan perusahaan pada bula sebelumnya (t - 1)

Return used in the market is *the* market *return* calculated monthly, counted as follows:

$$\text{Rmt} = \frac{\text{IHSGt - IHSGt - 1}}{\text{IHSGt - 1}}$$

Dimana:
R_{mt} = *Return* pasar pada bulan ke t
P_t = Indeks harga saham gabungan penutupan pada bulan ke t
P_{t-1} = Indeks harga saham gabungan penutupan pada bula sebelumnya (t - 1)

Classical Assumption Test
Classic assumption test is testing conducted prior to the testing of the regression equation on the assumption of disturbances that are classic for *time series* data. Test classical assumptions include normality test data, testing of heteroschedasticity problem, the problem of autocorrelation test, and testing of multicollinearity problems. Testing data for normality using the *Jarque-Bera test* model or the *JB test* indicates that the observed normal distribution of data. Multicollinearity test showed that there are no partial correlations (PAC) above 0.5, so the data is free from multicollinearity problems. Autocorrelation test is done by *Langrange Multiplier* test *(LM test),* the results indicate that the data is free from autocorrelation *problems.* Testing heteroschedasticity using *white test* also showed that there was no heteroschedasticity.

Hypothesis Testing Model

1. Hypothesis Testing 1 and 2.

The first hypothesis in this study will examine the effect of opportunistic behavior regarding the manipulation around the SEO of the company's operating performance after the SEO. To test the first hypothesis, regression testing against changes in *return on assets* (Δ ROA) with variable *discretionary total accruals* (DTAC) is implemented. If the *discretionary total accruals* negatively affect Δ ROA, then the hypothesis that indicates *the return on assets* at the time of the SEO firm is affected by the earnings management around SEO cannot be denied.

The second hypothesis is to determine the effect of earnings management towards stock *returns.* The second hypothesis in this study will be tested using a regression equation to see the effect of *total discretionary accruals* at the time of the SEO towards the *cummulative abnormal return* (CAR) of the company three years after the SEO. If the *discretionary total accruals* negatively affect the CAR, then stock *returns* of listed companies in Indonesia Stock Exchange is affected by the earnings management around SEO is shown low.

2. Hypotheses Testing 3 and 4.

Hypotheses three and four of this study will be tested using a different test. Different test in this study is to use the *independent sample t-test.* Different test for the third hypothesis aims to determine whether there are differences in operating performance between companies that do SEO *(issuer)* and companies that do not do SEO *(nonissuer).* If the results of different known that the *return on assets* (as a proxy for operating performance) company that does SEO differ significantly compared with the company's *return on assets* that do not do SEO, then the third hypothesis can not be rejected.

Different test for the fourth hypothesis aims to determine whether there is a difference between the stock performance of companies that do SEO *(issuer)* and companies that do not do SEO *(non-issuer).* If the results of different known that the *cumulative abnormal return* (as a proxy for performance shares) a company that does SEO differ significantly compared with the *cumulative abnormal return* companies are not doing SEO and the value of the fourth hypothesis cannot be rejected.

RESULTS AND DISCUSSION

1. Description of Variables

This reseach used a variable *discretionary total accrual* (DTAC) as a proxy of earnings management, variable *return on assets* (ROA) as a proxy for financial performance, stock *returns* as a proxy for stock performance, and sales growth variables (SGRO). Overview of the study variables, can be seen in the descriptive statistics table below:

TABEL 4.2
Statistik Deskriptif

	N	Minimum	Maximum	Mean	Std. Deviation
ROA	23	-0,06	0,31	0,0766	0,08828
DTAC	23	-1,65	4,41	-0,0296	1,21046
SGRO	23	-0,62	1,76	0,2625	0,52519
Rit	23	-0,09	0,18	0,0132	0,07584
Valid N (listwise)	23				

Sumber: data sekunder diolah (2008)

The descriptive statistics above shows that variable *discretionary total accrual* (DTAC) has a negative value of -0.0296 and a standard deviation of 1.21046. Negative mean values of DTAC indicates that the pattern of earnings management is carried out *decreasing income pattern.* The maximum value of 4.41 indicates that the companies sampled in this study practicing earnings management at the time of the SEO using.

increasing income pattern, and the minimum value of -1.65 indicates that the companies sampled in this study practicing earnings management at the time of SEO using *income decreasing pattern.*
The descriptive statistics *on return on assets* (ROA) at the SEO shows in a mean of 0.0766 with the standard deviation of 0.08828. Standard deviation values greater than the average ROA indicates that the financial performance for the companies sampled in the study varied greatly. The maximum value of 0.31 indicates that the companies sampled in this study had the highest financial performance, while the minimum value of -0.06 indicates that the companies sampled in this study had the lowest financial performance.

The descriptive statistics of variables stock *return* (Rit) shows the mean value of 0.0132 at the time of SEO. The minimum value of -0.09 indicates that although the shares have been offered in the primary market, not necessarily the shares will be purchased by investors. Descriptive statistics for sales growth (SGRO) yields an average value of 0.2625 and a standard deviation value of 0.52519. Standard deviation values greater than the SGRO average value showed that sales growth for the companies sampled in this study were highly diversified.

Results of Hypothesis Testing 1

1. Operating Performance

This study measures the performance of operations by using the change in *return on assets* (ROA Δ), it's based on research Rangan (1998). With this approach, if Δ ROA <0, then the operating performance of the period is lower than the previous period.

TABEL 4.4
Pengujian perubahan *return on asset* untuk periode -3 sampai +3

Perubahan *return on asset* (ΔROA)							
Tahun Ke	Mean	Median	Std. Dev	Min	Max	t-sat	Sig.
MIN3 (N=23)	0,1859	0,0707	0,53647	-0,0461	0,4179	1,662	0,111
MIN2 (N=23)	-0,1951	0,0041	0,95471	-0,608	0,2177	-0,980	0,338
MIN1 (N=23)	-0,0616	-0,0565	0,31266	-0,1968	0,0736	-0,945	0,355
NOL (N=23)	0,0766	0,0596	0,08828	0,0385	0,1148	4,164*	0,000
PLUS1 (N=23)	0,0076	0,0198	0,13761	-0,0519	0,0671	0,266	0,793
PLUS2 (N=23)	0,0497	0,0514	0,12197	-0,0031	0,1024	1,954***	0,064
PLUS3 (N=23)	0,0483	0,0351	0,1192	-0,0032	0,0999	1,944***	0,065
Sebelum (N=69)	-0,0236	0,0274	0,66702	-0,1839	0,1366	-0,294	0,770
Sesudah (N=69)	0,0352	0,0312	0,12619	0,0049	0,0655	2,318**	0,023

Ket: * Signifikan pada level 1%   *Sumber: data sekunder diolah (2008)*
** Signifikan pada level 5%
*** Signifikan pada level 10%

Table 4.4 shows that in a period of two years and one year before the SEO, mean value of Δ ROA is negative (-0.1951 and -0.0616), but not statistically significant. While on a three-year period before the SEO, and one year after the SEO mean value of Δ ROA is positive and statistically insignificant. Two years after the SEO, and three years after SEO significant at the level of 1% and 10%.

Two different tests for each period Δ ROA in *cross sectional* and *pooled data* (Table 4.5) shows that Δ ROA over the period -3 greater than Δ ROA -2 and Δ ROA -1 with a significance value at the level of 10% and 5%. For the period of SEO, current Δ ROA has a greater value in the period Δ ROA -1 and +1 with level of significance of 5%. This indicates that the performance in the period before SEO has a low value and then increased significantly in the SEO period. Yet this increase does not continue in the next period. Low operating performance before the SEO is caused by manipulation income decreasing pattern (transform the current income period into future periods, so the performance at the SEO will appear larger when compared with previous performance).

2. Effect of Earnings Management Against Δ ROA

The first hypothesis of this study examined the effect of earnings management around SEO on the performance of the company's operations before and after the SEO. Regression equation in this hypothesis was tested using statistical tools called *eviews.* This hypothesis would be supported if the value of DTAC has a negative impact on ROA. Negative DTAC indicates that earnings management has an influence on the company's operating performance. The greater the earnings management of the company, the operating performance of companies will decrease (Saiful, 2002). Here is a table of regression results from the influence of *discretionary total accruals* (DTAC) and sales growth (SGRO) on financial performance before the SEO, as SEO, and after the SEO.

Table 4.6 shows that the DTAC has a negative effect to Δ ROA one year and two years to come (-0.0720 and -0.373), except between DTAC m3 with m1 Δ ROA (-0.1789 and 0.8128), DTAC m2 with ROA Δ n (0.1914), DTAC p1 m1 with Δ ROA (0.2506), and DTAC with Δ ROA p2 p3 (0.0249). Table 4.6 illustrates that *total discretionary accrual* variables showed a negative regression coefficient and significant at the level of 1%, 5% and 10% level. These results suggest that changes in *return on assets* in the period of one year after the SEO is affected by the *discretionary total accrual* at the time of the SEO and sales growth (SGRO) one year after the SEO company. The ability of *total discretionary accrual* variables at the time of the SEO and sales growth one year after the SEO as an independent variable in explaining the effect of changes in *return on assets* one year after the SEO is at 12:29 (29%) and the remaining 71% is explained by other variables that are not entered into the equation.

Based on the regression results, it can be concluded that the *discretionary total accruals* (DTAC) affect the company's financial performance before and after the SEO where the higher value of DTAC then the lower the company's financial performance. Thus, the first hypothesis (H1) which shows that if managers behave opportunistically, then the *discretionary accruals* can predict the decline in operating performance is acceptable.

TABEL 4.6

Hasil pengujian hubungan antara ΔROA dengan *discretionary total accrual* (DTAC)

Variabel Independen	Variabel Dependen										
	ΔROA_{m2}	ΔROA_{m1}	ΔROA_{n}	ΔROA_{p1}	ΔROA_{p2}	ΔROA_{p3}	ΔROA_{m1}	$\Delta ROA n$	ΔROA_{p1}	ΔROA_{p2}	ΔROA_{p3}
$DTAC_{m3}$	-0,1789	0,8128									
$DTAC_{m2}$			0,1914				-0,0060				
$DTAC_{m1}$				0,2506				$-0{,}0859^{***}$			
$DTAC_{n}$					$-0{,}0720^{*}$				$-0{,}0373^{**}$		
$DTAC_{p1}$						$-0{,}0130^{**}$				-0,1768	
$DTAC_{p3}$											0,0249
$SGRO_{m2}$	0,0392										

2. Results of Hypothesis Testing 2

The second hypothesis in this study examined the effect of *total discretionary accruals* (DTAC) with a *cumulative abnormal return* (CAR) before and after the SEO. If mean value of DTAC towards CAR is negative means that the low stock *returns* of SEO firms listed on the JSE is affected by the earnings management around SEO. Table 4.8 below represents the results of the regression of *total discretionary accrual* variables and changes in *return on assets* of the *cumulative abnormal return:*

TABEL 4.8
Hasil pengujian hubungan antara CAR dengan *discretionary total accrual* (DTAC)

Variabel Independen	Variabel Dependen						
	CAR_{m1}	CAR_{p1}	CAR_{p2}	CAR_{p3}	CAR_{p1}	CAR_{p2}	CAR_{p3}
$DTAC_{m2}$	-2,4219***						
$DTAC_{m1}$		-0,2351					
$DTAC_{n}$			0,3809*		0,0154		
$DTAC_{p1}$				-0,0766		-2,2653*	
$DTAC_{p2}$							0,6957
$SGRO_{m1}$	1,9143*						
$SGRO_{p1}$		2,1019*			1,7951*		
$SGRO_{p2}$			3,6605*			0,8199	
$SGRO_{p3}$				1,9871*			1,8727*
Total obs	23	23	23	23	23	23	23
F	8,2739*	7,0340*	5,5481*	11,6491*	12,0858*	4,1641**	13,1532*
Adjusted R^2	0,4092	0,3542	0,2925	0,5285	0,5257	0,2233	0,5612

Ket: * Signifikan pada level 1% *Sumber: data sekunder diolah (2008)*
** Signifikan pada level 5%

Regression results indicate that the current DTAC done for the period of earnings management will affect negatively on the CAR of one year, two years, and three years to come, except between DTAC p2 n with CAR, CAR DTAC n with p1 and p2 with CAR DTAC p3. From the results of the regression, the CAR of one year before the SEO is affected by DTAC in the period two years before the SEO and SGRO during the year preceding the SEO. The ability of DTAC in the period two years before the SEO and SGRO a period of one year before the SEO as an independent variable in explaining the company's stock performance one year before the SEO is at 0,40 (40%) and the remaining 60% is explained by other variables that are not included in the equation.

Table 4.8 shows that the low *cumulative abnormal return* in this study is influenced by the presence of earnings management at the time of the SEO will have an impact on the company operating performance. Thus, the second hypothesis (H2) is indicating that if managers behave opportunistically, then the *discretionary accruals* can predict stock performance degradation is acceptable.

3. Results of Hypothesis Testing 3

The hypothesis three does the different test by using *independent sample t-test* between the *return on* corporate *assets* and *return on assets* for SEO and non-SEO firms. The results of different test for non-SEO firms and SEO Companies are as follows:

TABEL 4.9
Perbedaan Kinerja Operasi (ROA) Perusahaan SEO dan Non SEO

	Panel A (Nilai Mean SEO)	Panel B (Nilai Mean Non SEO)	Panel C (Nilai t Statistik)
MIN3	0.1859	0.0577	1.181***
MIN2	-0.1951	0.0322	-1.170
MIN1	-0.0616	0.0546	-1.375
NOL	0.0766	0.0885	-0.292
PLUS 1	0.0076	0.0377	-0.600
PLUS 2	0.0497	0.0185	0.538
PLUS 3	0.0433	0.0228	0.652

Ket: *** Signifikan pada level 10% *Sumber: data sekunder diolah (2008)*

The different test in Table 4.9 shows that the test of difference between the operating performance (ROA) for SEO companies and *return on assets* for non-SEO firms in the period -1 have an average value of 0.1859 and 0.0577 and significant at the 10% level. The average ROA of SEO companies in the two-year period and the period of one year before the SEO have an average smaller value of -0.1951 and -0.0616 are not significantly when compared with the average ROA of non SEO company of 0.0322 and 0 , 0546.

The above results show that the performance of SEO firms in the three years before the SEO as well as a period of two years and three years after SEO is higher when compared with non-SEO firms. In the period up to two years before the SEO at SEO and one year after the SEO shows that operating performance of SEO firms is smaller when compared with non-SEO firms. It can be concluded that operating performance of SEO firms is higher than the operating performance of SEO firms, then this third hypothesis (H3) cannot be supported. Operating performance of SEO firms a period of two years and one year before the SEO low compared with non-SEO firm's performance is due to manipulation by the company in the period prior to the SEO with *decreasing income pattern.*

4. Results of Hypothesis Testing 4

The fourth hypothesis testing is done through an independent samples t test on the performance *returns* between SEO firms with non-SEO firms and markets. Results of hypothesis testing can be seen in Table 4:10:

TABEL 4.10
Perbedaan *Return* Saham (Rit) Perusahaan SEO dan Non SEO

Kinerja Return Saham				
	t - 1	t+1	t+2	t+3
SEO	0,0052	0,0140	0,0211	0,0264
Non SEO	0,0430	0,0621	0,0021	0,0232
Market Return	0,0125	0,0327	0,0138	0,0387
Market Adjusted				
Mean Difference	-0,0073	-0,0186	0,0073	-0,0123
t statistik	-0,0920	-0,5050	0,1490	-0,2030
p-value	0,9280	0,6180	0,8830	0,8410
Non SEO Adjusted				
Mean Difference	-0,0377	-0,0480	0,0190	0,0031
t statistik	-1,5450	-1,2200	1,6000	0,2200
p-value	0,1290	0,2290	0,1170	0,8260

Sumber: data sekunder diolah (2008)

Different test shows that mean value of Rit in the period a year before for the SEO firms and non-SEO firms is 0.0052 and 0.0430 with the value effect is not significant. It can be concluded that the performance of companies that do SEO lower in a period of one year and two years before the SEO better than the non-SEO firms and compared with the market. In the two-year period before the SEO performance of SEO firms is higher compared to non-SEO firms and markets. Likewise with a three-year period before the SEO, performance of SEO firms is higher compared to non-SEO firms. Thus the fourth hypothesis (H4) which says that there are significant differences between the stock performance of SEO firms and non-SEO firms can not be accepted.

CONCLUSION, LIMITATIONS, AND SUGGESTIONS

1. Conclusions

1. Earnings management with *income decreasing* patterns around the SEO influence the company's operating performance during SEO. The inluence of earnings management around SEO can be seen from negative *discretionary total accrual* to the change in *return on assets.* The *total* value of *discretionary accruals* in the period before the SEO is bigger compared to period after the SEO.

2. Earnings management affect the stock performance of SEO firms. This is proven from the negative value of *discretionary total accrual* towards the *cummulative abnormal return* of SEO firms.

3. Different test shows that operating performance of SEO firms is higher than the operating performance of SEO firms, but statistically not significant. This means the third hypothesis (H3) that

mention there are significanct differences in operating performance between SEO firms and non-SEO firms can not be accepted in this study.

4. Different test shows that mean value of stock return between the SEO firms and non-SEO firms is low and not significant. The performance of SEO companies is lower in a period of one year and two years before the SEO. However, this is better than the non-SEO firms and compared to the market. In the two-year period before the SEO, the performance of SEO firms is higher compared to the non-SEO firms and markets. Likewise with a three-year period before the SEO, performance of SEO firms is higher compared to non-SEO firms. Thus the fourth hypothesis (H4) which says that there are significant differences between the stock performance of SEO firms and non-SEO firms cannot be accepted.

2. Limitations of Research

The limitations in this study are as follows:

1. This study only used a sample of non-financial companies as much as 23 SEO firms and 25 non-SEO firms listed on the Indonesia Stock Exchange, this limited sample may be not representative of the population.

2. This study only uses the modified Jones model in detecting the presence or absence of earnings management, so comparison outcomes when earnings management is detected using other models such as the model of Healy, DeAngelo models and models Rangan can not be implemented.

3. Suggestions

Suggestions for further research are as follows:

1. Future studies are expected to increase the amount of sample that is closer to the population. The samples for further research using a sample of financial firms. This was done so that the results of further research can provide consistent results that at the time of SEO, both non-financial companies and financial firms practice earnings management.

2. Future studies should not only use the modified Jones model in detecting the presence or absence of earnings management of the company. Future studies may use three models of research that the modified Jones model studies, models Rangan, Model Healy and DeAngelo models simultaneously to see the difference in the results of the three models, so it can be seen which model is best at detecting the presence or absence of earnings management.

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