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The Effect of Good Corporate Governance on Financial Reporting Quality of BEI Listed Banking Companies

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ABSTRACT

Good Corporate Governance (GCG) reflects a company's commitment to transparency, accountability, and integrity in achieving corporate goals. The implementation of GCG mechanisms such as audit committees, independent commissioners, and boards of commissioners plays an important role in building stakeholder trust and ensuring the credibility of financial reporting. In recent years, GCG has gained attention as a major factor influencing the quality of financial reporting and controlling earnings management practices. This study aims to examine the effect of GCG on the quality of financial reporting in Indonesian banking companies, emphasizing its role in improving corporate accountability and performance. The method used is a systematic literature review by examining various previous studies on the effectiveness of GCG mechanisms in improving financial reporting transparency. The results show that the independence of the board of commissioners has a positive effect in suppressing earnings management, while the audit committee and board of commissioners often show limited or inconsistent effects. Overall, the effectiveness of GCG is highly dependent on the competence, independence, and active involvement of governance bodies, so strengthening the implementation of GCG is necessary to improve the credibility of financial reports and stakeholder trust.

INTRODUCTION

Good Corporate Governance (GCG) is a governance standard applied by companies to manage, control, and supervise operational activities in a transparent, accountable, and responsible manner. In recent years, the implementation of GCG has become an important issue in the Indonesian banking sector as awareness of the importance of integrity and quality of financial reporting has increased (Rahayu et al., 2024; Wicaksono et al., 2024). The implementation of GCG is expected to minimize earnings management practices that can undermine the credibility of financial reports and harm stakeholders(Handoyo et al., 2022).

The role of GCG mechanisms such as audit committees, boards of commissioners, and independent commissioners is very important in improving the transparency and accountability of financial reporting through effective oversight functions. However, the effectiveness of these mechanisms still varies between companies. Several studies have found that audit committees have a significant negative effect on earnings management, while the role of independent commissioners and boards of commissioners is often insignificant (Kustono, 2021).

In addition, GCG also plays an important role in maintaining the sustainability of the company because weak governance can reduce investor confidence and the company's image in the capital market (Citra et al., 2021). Contextual factors such as company size, audit quality, and the implementation of new accounting standards such as PSAK 71 or IFRS

9 also influence the effectiveness of GCG in improving the quality of financial reporting (Aufa et al., 2024).

Within the framework of agency theory, GCG mechanisms serve to reduce conflicts of interest between management and capital owners by providing an independent and measurable monitoring system. Meanwhile, according to stakeholder theory, the implementation of GCG reflects the company's responsibility to its stakeholders to ensure credible financial reporting that is in accordance with business ethics principles (Yogyakarta, 2017).

However, previous studies have shown inconsistent results. Some studies report that independent commissioners have a positive effect on the quality of financial reporting, while audit committees and the size of the board of commissioners do not always have a significant impact on earnings management control (Manajemen et al., 2021). These differing findings indicate the need for a review of the effectiveness of GCG implementation in the Indonesian banking sector. Therefore, this study aims to re-examine the influence of GCG mechanisms, particularly audit committees, board of commissioners independence, and board of commissioners size, on financial reporting quality and *earnings management* practices through a *systematic literature review* approach.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Good Corporate Governance (GCG)

Good Corporate Governance (GCG) is a system that regulates and controls companies to create added value for all stakeholders (Manajemen et al., 2021). The implementation of GCG is important to ensure transparent, accountable, and efficient decision-making processes. GCG includes oversight mechanisms through audit committees, boards of commissioners, and board independence to minimize earnings management practices and improve the credibility of financial reports (Prawida, 2021). According to (Tanjung, 2023), GCG serves as an instrument to control opportunistic management behavior, ensure the reliability of financial reporting, and maintain investor confidence.

Financial Reporting Quality

Financial Reporting Quality reflects the extent to which a company's financial statements provide relevant, reliable, and manipulation-free (earnings management) information (Zulfikar et al., 2021). According to (Aufa et al., 2024), quality financial statements enable stakeholders to make sound economic decisions based on honest and accurate data. Factors such as the effectiveness of the audit committee, the independence of the board of commissioners, and the transparency of corporate governance have a significant influence on the quality of financial statements (Prawida, 2021).

Audit Committee

Audit committee plays an important role in ensuring the transparency and reliability of a company's financial reports. According to (Arif et al., 2020), the audit committee is tasked with overseeing the internal audit process, assessing compliance with accounting standards, and ensuring that internal controls are effective. However, research shows that the size or frequency of audit committee meetings is not always significantly related to a decrease in earnings management (Sari & Widaninggar, 2020). This indicates that the

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effectiveness of audit committees is more influenced by the quality of their resources and independence than simply their structural existence (Zulfikar et al., 2021).

Independent Commissioner

Independent commissioner is a member of the board of commissioners who is not affiliated with the company's management, controlling shareholders, or other parties that could influence decision-making, ensuring objective supervision over management activities (Aufa et al., 2024; Kirana et al., 2020). The role of independent commissioners is crucial in maintaining transparency and accountability, as they are expected to reduce opportunistic managerial behavior such as earnings management and improve the credibility of financial statements (Prawida, 2021). According to (Tanjung, 2023), the higher the proportion of independent commissioners, the lower the likelihood of earnings manipulation, since their independence provides more objective oversight of financial reporting. .

Board of Commissioners

Board of commissioners has the primary function of providing strategic direction and ensuring that management carries out operational activities in accordance with good governance principles. However, (Rafika et al., 2021) found that the size or frequency of board of commissioners meetings does not always correlate positively with improvements in financial reporting quality. This shows that the effectiveness of the board of commissioners is determined by their competence, activeness, and ability to carry out their supervisory functions professionally (Nanda & Somantri, 2020).

Agency Theory

Agency theory explains the relationship between capital owners (principals) and management (agents) where potential conflicts of interest may arise due to differences in objectives (Prawida, 2021). In this context, GCG mechanisms serve as a supervisory tool that can reduce information asymmetry and opportunistic behavior by management. Audit committees and boards of commissioners play a role in ensuring the transparency and accuracy of financial reports, thereby protecting the interests of shareholders (Hidayat, 2015).

Stakeholder Theory

Stakeholder theory posits that companies must be accountable not only to shareholders but also to all parties affected by corporate activities, including employees, customers, and the public (Tanjung, 2023). Transparent and credible financial reporting is an essential part of fulfilling stakeholder expectations and maintaining trust. When companies implement GCG effectively, they improve stakeholder relations, strengthen reputation, and ensure long-term sustainability (Indah Rafika, Husaini, 2021; Prawida, 2021).

Signaling Theory

Signaling theory explains that management uses financial reports to convey information about the company's performance and prospects to investors (Zulfikar et al.,

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2021). High-quality financial reports serve as a positive signal, reflecting management's integrity and commitment to transparency. Conversely, poor disclosure or aggressive earnings management can send negative signals that reduce investor confidence (Tanjung, 2023). Therefore, effective implementation of GCG ensures that the signals sent to the market are credible and not easily imitated by low-quality firms (Hidayat, 2015).

METHODS

This study uses a literature study method. A literature study is a type of library research that involves collecting, reviewing, and synthesizing information from relevant books, journals, reports, and previous research related to *Good Corporate Governance* (GCG) and financial reporting quality. This method is used because the topic has been widely studied in various contexts, allowing researchers to analyze, compare, and summarize existing findings to produce a comprehensive understanding (Prawida, 2021). The literature study approach also helps identify patterns, similarities, and inconsistencies in prior research results (Indah Rafika, Husaini, 2021).

This research aims to understand the relationship between *Good Corporate Governance* mechanisms such as the audit committee, board independence, and the board of commissioners and their effect on financial reporting quality and *earnings management* in Indonesian banking companies. The first step involves identifying the research problem and gathering relevant and credible literature through systematic database searches. Then, the selected literature is reviewed and analyzed to obtain an objective and in depth discussion regarding how GCG mechanisms influence transparency, accountability, and credibility in financial reporting.

RESULTS

Table 1. Results

No	Title	Authors	Year	Results
1	The Impact of Good Corporate Governance Mechanism and Firm Size on Earnings Management	Nisa Tanjung & Bunga Syahzuni	2023	Board independence has a significant negative effect on earnings management, while the audit committee and board of commissioners have no significant influence. Firm size strengthens the relationship between GCG and financial reporting quality.
2	Leverage, Profitability, Corporate Governance Mechanism, and Earning Management: Cases in Manufacturing Company in Indonesia Stock Exchange	Novria Prawida & Sutrisno	2021	GCG mechanisms (audit committee and board independence) have no significant impact on earnings management, indicating that governance practices are not yet fully effective in enhancing reporting quality.
3	Pengaruh Implementasi Good Corporate Governance terhadap Manajemen Laba Bank yang Terdaftar di Bursa Efek Indonesia	Indah Rafika, Husaini & Nur Sari	2021	Audit committee, board size, and board meeting frequency have no significant effect on earnings management, showing that the implementation of GCG in Indonesian banks remains formalistic.

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4	Effect of Board of Commissioners and Audit Committee on Earning Management	Ulfa Luthfia Nanda & Yuli Somantri	2020	Both the board of commissioners and audit committee have an insignificant effect on earnings management, reflecting weak internal monitoring in banking governance.
5	The Role of Corporate Governance in Constraining Earning Management	Dewi Kirana, Evi Wibawaningsih & Ayu Wijayanti	2020	Independent commissioners significantly reduce earnings management and improve financial reporting quality, while board size and committee activity show insignificant influence.
6	Bid-Ask Spread on Earnings Management with Good Corporate Governance as Moderation Variables: Banking Sector in Indonesia	Imam Ghozali, Hersugondo, Wahyudi, Prabuwono & Pamungkas (Ghozali et al., 2022)	2022	GCG moderates the relationship between bid-ask spread and earnings management, reducing information asymmetry and increasing market transparency.
7	Analisis Pengaruh Profitabilitas, Growth, Leverage dan Komite Audit terhadap Manajemen Laba Perusahaan Sektor Perbankan yang Terdaftar di BEI	Rahma Chaniago & Rina Trisnawati	2021	Profitability and growth significantly influence earnings management, while audit committee variables are not significant, showing limited oversight effectiveness.
8	Loan Loss Provision, Good Corporate Governance dan Manajemen Laba Bank di Indonesia dan Malaysia	Nita Sari & Nining Widaninggar	2020	GCG affects earnings management through loan loss provisions; however, its effectiveness differs between Indonesian and Malaysian banks due to regulatory environments.
9	Earnings Quality Determinants in Pre-Corona Crisis: Another Insight from Bank Core Capital Categories	R. Valdiansyah & E. Murwaningsari	2022	Bank capital structure and audit quality improve earnings quality, while GCG mechanisms show a limited direct effect on financial reporting quality.
10	Manajemen Laba Perbankan (Studi Pada Bank Terdaftar di Bursa Efek Indonesia)	Taufik Hidayat & Olfa Amouri	2020	Independent commissioners reduce earnings management, supporting the agency theory that strong governance mitigates opportunistic behavior.
11	Corporate Governance Management towards Companies Including in LQ45 Index	Desi Wahyuni & Muhammad Hamidi (Wahyuni & Hamidi, 2020)	2020	Transparency and independence in governance improve financial stability and investor confidence in listed companies.
12	Corporate Governance Mechanism and Financial Performance: Role of Earnings Management	Endah Savitri, Andreas Syahza, Gumanti & Abdullah (Almaqtari et al., 2020)	2020	GCG indirectly affects financial performance through reduced earnings management, indicating that governance quality drives profitability via transparent reporting.

DISCUSSION

The Relationship between Good Corporate Governance and Financial Reporting Quality

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Good Corporate Governance (GCG) is one of the main mechanisms used to ensure that a company operates transparently, accountably, and responsibly (Kirana et al., 2020). The implementation of GCG aims to strengthen oversight and reduce opportunistic behavior by management that may distort financial information. Financial reporting quality reflects the extent to which financial statements provide relevant, reliable, and unbiased information to stakeholders (Hidayat, 2015). Therefore, a strong governance structure is expected to minimize earnings management and enhance the credibility of financial statements.

According to research by (Prawida, 2021), GCG mechanisms such as the audit committee, board of commissioners, and independent commissioners play an important role in improving the transparency of financial reports. The study found that effective supervision can reduce the tendency of management to manipulate earnings. Similarly, (Tanjung, 2023) explain that the independence of the board of commissioners contributes to the improvement of reporting quality, as independent members are more objective in monitoring management's actions.

In contrast, several studies found that certain GCG components, particularly audit committees, have not shown a significant influence on financial reporting quality (Nanda & Somantri, 2020). This may occur due to the lack of expertise and independence among committee members, resulting in limited oversight effectiveness. Furthermore, Chaniago & Trisnawati (2021) found that the audit committee's presence alone is insufficient without active engagement and competency in financial matters.

Based on agency theory, GCG acts as a mechanism to reduce conflicts of interest between managers and shareholders through better monitoring and control systems (Zulfikar et al., 2021). Meanwhile, stakeholder theory explains that transparent and high-quality financial reporting is part of corporate accountability to meet stakeholder expectations (Hidayat, 2015). Thus, the implementation of GCG not only ensures compliance with regulations but also strengthens trust and investor confidence.

Overall, these findings indicate that the effectiveness of GCG mechanisms in improving financial reporting quality in Indonesian banks still depends on contextual factors such as company size, audit quality, and regulatory implementation (Sari & Widaninggar, 2020). Therefore, improving the independence, competence, and commitment of supervisory boards and audit committees is essential to achieving credible and transparent financial reporting.

The Relationship between Independent Commissioner and Earnings Management

Independent Commissioner is a crucial component of Good Corporate Governance (GCG) that functions to maintain objectivity and reduce management's opportunistic behavior in financial reporting (Kirana et al., 2020). Independent commissioners are expected to perform effective monitoring and protect shareholders' interests by preventing earnings manipulation that could mislead stakeholders. Theoretically, according to *agency theory*, independent commissioners can minimize information asymmetry by providing unbiased oversight over managerial actions (Zulfikar et al., 2021).

Empirical evidence on the relationship between Independent Commissioner and earnings management in Indonesian banking companies, however, shows mixed results. Studies conducted by (Hidayat, 2015) and (Kirana et al., 2020) reveal that the proportion of

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independent commissioners has a negative effect on earnings management, indicating that stronger independence can improve reporting credibility. These findings are supported by Prawida & Sutrisno (2021), who found that independent oversight encourages transparency and accountability in financial reporting.

In contrast, (Tanjung, 2023) and (Indah Rafika, Husaini, 2021) report that Independent Commissioner does not always have a significant effect on reducing earnings management, particularly when the independence is only structural rather than functional. This occurs when independent commissioners have limited financial expertise, infrequent meetings, or insufficient authority in strategic decision-making (Nanda & Somantri, 2020).

From the perspective of *stakeholder theory*, the presence of independent commissioners also reflects a company's commitment to upholding ethical behavior and protecting the interests of broader stakeholders beyond shareholders (Hidayat, 2015). However, without genuine engagement and competence, their monitoring function becomes symbolic rather than substantive.

Overall, previous research suggests that while an Independent Commissioner can play a critical role in mitigating earnings management, its effectiveness depends on qualitative attributes such as integrity, expertise, and activeness rather than the mere proportion of independent members. Therefore, strengthening the competencies and empowerment of independent commissioners remains essential to achieving the intended benefits of GCG in enhancing financial reporting quality in Indonesian banks.

CONCLUSION

This study emphasizes the vital role of Good Corporate Governance (GCG) in ensuring transparency, accountability, and reliability of financial reporting within Indonesian banking companies. The findings highlight that while the independence of the board of commissioners contributes positively to reducing earnings management, other governance mechanisms, such as audit committees and the board of commissioners as a whole, often demonstrate limited or inconsistent effectiveness. This indicates that the success of GCG depends not only on its structural presence but also on the quality of implementation, including the competence, independence, and activeness of its members.

From a theoretical perspective, this study reinforces *agency theory* by confirming that GCG serves as an effective mechanism to reduce information asymmetry and align managerial interests with those of shareholders. It also supports *stakeholder theory* by emphasizing that credible and transparent financial reporting is a form of corporate accountability that strengthens trust among investors and the public. Practically, these findings suggest that companies need to enhance the professionalism and authority of governance bodies, especially independent commissioners, to achieve sustainable reporting quality.

However, this study is limited by its reliance on secondary data and previous research findings, which may vary across contexts and time periods. Future research is recommended to empirically test the qualitative attributes of GCG such as expertise, diversity, and engagement frequency and their interaction with external factors like audit quality and regulatory frameworks. Such studies would provide deeper insights into how GCG mechanisms can effectively improve financial reporting credibility and long-term corporate sustainability in Indonesia's banking sector.

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