The Role Of Moderating Audit Quality On Income Smoothing

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ABSTRACT

This study seeks to provide empirical data on the impact of cash holding, income tax, and dividend policy on income smoothing with audit quality as moderation in companies included in the LQ 45 index traded on the Indonesia Stock Exchange from 2019 to 2023. Based on the purposive sample method, sample of 158 companies was obtained within 5 years of research. Logistic regression and moderating analysis are used as data analysis techniques in this study. The findings of this study prove that income tax has a positively affects income smoothing, however cash holding and dividend policy do not impact on income smoothing. Furthermore, on basis of contingency theory, this study utilizes the audit quality metric score which comprises audit firm size, audit firm industry specialization, audit tenure, client importance, and going-concern audit opinion. This study empirically reveals that audit quality can moderating the effect of cash holding and dividend policy on income smoothing.

Keywords: Cash Holding; Income Tax; Dividend Policy; Income Smoothing; Audit Quality

PERAN MODERASI KUALITAS AUDIT TERHADAP INCOME SMOOTHING

ABSTRAK

Penelitian ini bertujuan untuk menunjukan bukti secara empiris mengenai adanya pengaruh kepemilikan kas, pajak penghasilan, dan kebijakan dividen terhadap perataan laba dengan kualitas audit sebagai moderasi pada perusahaan yang termasuk dalam Indeks LQ 45 yang diperdagangkan dalam Bursa Efek Indonesia dari tahun 2019 sampai dengan 2023. Berdasarkan metode purposive sample, diperoleh sampel sebanyak 158 perusahaan dalam kurun waktu 5 tahun penelitian. Analisis regresi logistik dan moderasi digunakan sebagai teknik analisis data dalam penelitian ini. Temuan penelitian ini membuktikan bahwa pajak penghasilan memiliki pengaruh terhadap perataan laba, sedangkan kepemilikan kas dan kebijakan dividen tidak memiliki pengaruh terhadap perataan laba. Selanjutnya dengan dasar teori kontigensi, penelitian ini menggunakan kualitas audit metrik skor yang terdiri ukuran firma audit, spesialisasi industry firma audit, audit tenure, client importance, dan opini audit going concern. Penelitian ini secara empiris mengungkapkan bahwa kualitas audit memoderasi pengaruh kepemilikan kas dan kebijakan dividen terhadap perataan laba.

Kata Kunci: *Kepemilikan Kas; Pajak Penghasilan; Kebijakan Dividen; Perataan Laba; Kualitas Audit*

e-ISSN 2302-8556

Vol. 35 No. 6
Denpasar, 30 Juni 2025
Hal. 1677-1569

DOI:
10.24843/EJA.2025.v35.i06.p11

PENGUTIPAN:
Widyawati, I., & Trisnawati, R. (2025). The Role Of Moderating Audit Quality On Income Smoothing. *E-Jurnal Akuntansi*, 35(6), 1677-1569

RIWAYAT ARTIKEL:
Artikel Masuk:
22 Maret 2025
Artikel Diterima:
23 Juni 2025

Artikel dapat diakses : https://ojs.unud.ac.id/index.php/Akuntansi/index

INTRODUCTION

Income smoothing is considered to be a form of the earnings management methods carried out by companies. Income smoothing which could be defined as deliberate fluctuations in certain levels of earnings that are perceived as typical or stable for companies (Beidleman, 1973). Positive, stable, and increasing profits can describe the strong performance of the company, which is attractive to external parties. Income smoothing is because management prefers to maintain a stable earnings value compared to fluctuating earnings (Khoirul Kabib et al., 2020). There is a lot of debate among accounting practitioners and academics regarding income smoothing. Accounting practitioners consider income smoothing practices as fraud, while academics consider income smoothing not to be part of fraud because efforts to stabilize profits are carried out based on applicable accounting principle procedures. Income smoothing practices are safe to carry out in the short term as long as they do not violate the law whose purpose is to shift income and expenses incurred across different accounting cycles that are intended to serve the company's beneficial interests (Suyono et al., 2023).

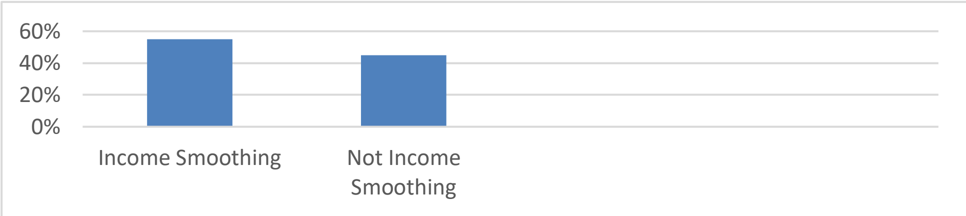

Figure 1. Index Eckel Companies LQ 45 Period 2020-2023

Source: Research data, 2024

The strategy of stabilizing reported income practices can occur in various countries. The Enron case is an example of fairly phenomenal report manipulation involving audit firm Arthur & Andersen on an international scale. The results of the eckel index calculation can be said that 11 companies included in the LQ 45 index still tend to flatten profits so that reported profits do not fluctuate. Numerous elements influence income smoothing practices such as cash holding, income smoothing, dan dividend policy.

Cash holding are an important aspect of corporate financial policy (Khatib et al., 2022). It can encourage companies to meet short-term obligations, take advantage of investment opportunities, manage risk, and flatten profits. The nature of cash holding is easily managed by managers who can motivate managers to carry out their personal interests (Fadillah & Luthan, 2023). A higher level of cash holdings provides greater flexibility for the company in managing cash flow and income, which can be utilized for income smoothing over time. The outcomes of the analysis undertaken by (Fadillah & Luthan, 2023) and (Musyafa & Kholilah, 2023) show that cash holding has no statistically significant effect on income smoothing. This statement contradicts as shown in the research led by (Nirmanggi & Muslih, 2020) which provides evidence that cash holding contributes positively and significantly to income smoothing.

Regulations within the tax system significantly influence the selection of accounting policies and methods employed by companies (Firnanti, 2019). The tax amount is determined by both the income level and the relevant tax rate. Income tax can be one of the factors motivating income smoothing, as a way to avoid high progressive tax rates when substantial profits are generated within an accounting period. Companies carry out income smoothing practices usually to minimize the tax burden. One technique applied to lower the level of taxation is by adding expenses to the company, thereby decreasing profit and reducing the amount of deferred income tax (Mahendra & Jati, 2020). The outcomes from the research by (Nirmanggi & Muslih, 2020) and (Wulan, 2022) state that income tax does not significantly affect income smoothing. In comparison with the outcomes of the research conducted by (Firnanti, 2019), (Palupi, 2020), and (Mahendra & Jati, 2020) state that income tax exerts a positively and significantly effect on income smoothing.

Dividend policy exerts an impact on the management of the company profits paid to stakeholders or using it for the company's operational needs. Fluctuating profits can lead to fluctuating dividend payments which are generally not favored by investors. The stability of dividend payments can be achieved, for example through the strategy of income smoothing. Implementation of income smoothing techniques is intended to ensure the stability or increase of dividends from year to year, creating a positive impression on external parties. The outcomes of the research conducted by (Safira et al., 2022) and (Suwaldiman & Lubis, 2023) state that dividend policy exerts a significantly and positively effect on income smoothing. There is a different according to the analysis undertaken by (Putri & Lutfillah, 2020) and (Sesilia et al., 2021) state that the dividend policy does not impact on income smoothing.

Good audit quality tends to be stricter in auditing financial statements. A high-quality auditor can reduce or prevent income smoothing practices through strict supervision, maintaining independence, utilizing advanced technology, and applying extensive expertise and experience. The Enron and WorldCom cases had a significant impact on the audit quality of well-known public accounting firms. External auditors are also considered to be less sensitive to risks faced by clients, lacking independence, objectivity, and professional responsibility, all of which affect audit quality (Sumiadji et al., 2019). Audit quality can reduce earnings management in audited companies, particularly in companies audited by the BIG4 firms in the United States (Santos-Jaén et al., 2023). The outcomes of research performed by (Oktavinawati & Herawaty, 2022) state that audit quality significantly weakens the association among cash holding and income smoothing. Good audit quality can detect information asymmetry by management, which leads to increased cash holding due to agency costs, making it more difficult for the company to participate in income smoothing practices.

Several previous studies have shown inconsistencies in their conclusions, which has led the researcher to conduct further research on the factors influencing income smoothing. This study builds upon the research conducted by (Oktavinawati & Herawaty, 2022). This study differs from previous research by including by income tax and dividend policy as independent variables.

The reason for including income tax as an independent variable indicates that companies tend to minimize their tax burden by applying accounting policy strategies and complying with applicable tax regulations. Higher profit levels result in higher tax expenses. The final distinction is this study focuses regarding firms listed on the LQ 45 Index, which are considered to represent firms with strong performance and high investor interest. The reason for including dividend policy as an independent variable is that dividend distribution reflects a company's performance, which can influence investor's decisions. Companies tend to be involved in income smoothing to maintain consistent dividend distributions, aiming to send positive signals about their performance to investors. Moreover, dividend smoothing can serve as a substitute for weak corporate governance or be a result of free cash flow absorption behavior (Tran, 2024). A company's dividend smoothing can also be driven by both internal microeconomic factors and external macroeconomic environmental factors. This study aims to examine the effect of cash holding, income tax, and dividend policy on income smoothing, and to evaluate audit quality as a moderating factor in these relationships.

Agency theory proposed by (Jensen, Michael C. Meckling, 1976) describes the relationship established between shareholders as principals and management as agents. This relationship can influence managerial behavior and company performance. The relationship arises when shareholders entrust management with the authority to operate the company on their behalf. Agency theory acknowledges the existence of conflicting priorities among the shareholders (principals) and the management (agents). This conflict arises because the company does not act to maximize investor welfare, but instead tends to favor the interests of company (agents). Agency conflicts can be addressed by introducing agency costs, which are borne by both shareholders and management. The divergence of interests between principals and agents can trigger agency conflicts, which may lead to information asymmetry whereby one party possesses more detailed information than the others. As indicated by (Scott, 2015), information asymmetry is categorized into two types, adverse selection and moral hazard. Agency theory is reflected in binding contracts between investors and management that define rights, responsibilities, and benefits. This theory serves as foundation for explaining the actions of principals in engaging in earning management through smoothing practices for various purposes, such as cash flow management, minimizing tax burdens, and maintaining dividend stability, all of which influence agent investment decisions.

Contingency theory is a theoretical concept that addresses leadership effectiveness in relation to group performance, which depends on situational factors that can either enhance or diminish the influence of a leader's characteristics. The contingency model of leadership effectiveness is measured using the Least Preferred Co-Worker (LPC) scale to identify leadership characteristics and their impact on group performance (Fiedler, 1981). Different leadership styles can predict their effectiveness by classifying groups based on relevant situational factors. The contingency approach to management accounting is based on the principle that no single accounting system is universally suitable for all organizations across every situation (Otley, 1980). The implementation of an adequate accounting system depends on specific organizational factors, reflecting the principle that no idea accounting system suits every company. This explicit consideration influences the selection of a suitable for research methodology, grounded in cumulative knowledge to clarify theoretical aspects. Based on this contingency concept, audit quality is applied as situational moderating variable that influences the application of income smoothing policies. Financial distress conditions cause companies to experience a decline in revenue, while during periods of high sales, companies will experience a significant increase in revenue. This results in income fluctuations that affect investor's decisions regarding their investment, prompting management to participate in income smoothing strategies. The identification of specific information is necessary for explaining and predicting the effectiveness of such practices (Fiedler, 1981). Effective audit quality is expected to detect and prevent income manipulation in relation to the effect on earnings management policies with income smoothing.

Management and shareholders have different perspectives on the costs and value considerations of retaining cash within the firm. Agency problems are an important factor in corporate cash holdings. When shareholders protection is weak, it can encourage higher cash holdings for investment opportunities and results in asymmetric information in controlling capital market developments (Dittmar et al., 2003). Cash holdings for management can increase power in policy management and reduce the risk of company (Opler et al., 1999). Companies can manage accounting method policies utilized for improving management performance which may lead to information asymmetry for the principal. Poor earnings quality, due to weak regulatory oversight and the presence of losses can lead to increased information asymmetry which in turn affects the company's cash balance (Farinha et al., 2018). Companies tent to increase cash holdings to deal with high uncertainty in operations or unforeseen future investment activities (Jung & Choi, 2024). Adequate cash holdings can be used to anticipate potential risks and take advantage of available investment opportunities. In the event of a revenue decline during financial distress, companies tend to use their cash holdings to cover losses in order to maintain stable reported earnings. According to the empirical evidence provided by (Nirmanggi & Muslih, 2020), (Kusmiyati & Hakim, 2020), (Tiningsih & Mubarok, 2021), and (Asri & Popi, 2022) state that cash holding has a significant and positive effect on income smoothing.

H_1: Cash holding positively affects income smoothing

The emergence of agency conflicts due to differing interests between management and investors can be a factor that drives companies to engage in income smoothing. Earnings management policies aimed at maintaining stable profits are also used to reduce the tax burden the company has to pay in a given fiscal year. Companies that engage in income smoothing practices often do so with opportunistic motives, whereby management reports earnings in a way that maximizes the company's interests such as income tax motives (Kustono, 2021). Companies may use tax planning strategies that take advantage of loopholes within the tax laws. One of which is the deferral or shifting of tax payments. According to the analysis performed by (Palupi, 2020), (Mahendra & Jati, 2020), (Amin et al., 2021), and (Delia & Abbas, 2024) state that income tax positively affects income smoothing.

H_2: Income tax positively affects income smoothing

The distribution of dividends to shareholders can give rise to agency conflicts due to the differing interest of principals and agents in maximizing their own welfare. The divergence of interests among principal and agent gives rise to information asymmetry, which can be exploited by management in determining corporate policies. Investors desire high dividend payouts, while companies tend to reduce dividends in order to increase retained earnings and minimize future risks. A high dividend payout ratio can lead to earnings fluctuations that affect the company's long-term financial stability. This encourages firms to engage in earning management through income smoothing to mitigate the impact of such fluctuations. Investors generally expect stable returns on their investments and the presence of earnings volatility can influence their decision-making considerations. Based on the research conducted by (Gunawan & Hardjunanto, 2020), (Safira et al., 2022), and (Suwaldiman & Lubis, 2023) state that dividend policy has a significant and positive effect on income smoothing.

H_3: Dividend policy positively affects income smoothing.

Effective audit quality can detect violations committed by client companies in their accounting systems. Auditors verify that the audit procedures adhere to relevant accounting standards. High audit quality can lead to lower level of income smoothing practices, thereby enhancing the reliability of the company's financial reports for their users. Holding a large amount of cash influences management's policies in managing the company's cash resources. Competent and independent auditors are expected to ensure the accuracy of financial statements in order to reduce income smoothing practices that may harm investors in the long term. The outcomes of research performed by (Oktavinawati & Herawaty, 2022) state that audit quality is capable of moderating the negative effect of cash holding on income smoothing. Good audit quality can detect information asymmetry committed by management, which leads to increased cash holdings due to agency costs, thereby making it more difficult for the company to engage in income smoothing practices.

H_4: Audit quality is capable of moderating the negative effect of cash holding on income smoothing.

A competent and independent external audit will conduct a more detailed analysis of the potential risks of tax violations committed by the company. Companies with high profits tend to engage in income manipulation to reduce the amount of taxes paid. In practice, many companies with low tax compliance levels implement tax avoidance strategies. Tax burdens can be reduced through various tax strategies that comply with applicable tax regulations. Higher audit is expected to detect companies committing income tax violations, which may be influenced by income smoothing strategies. The outcomes of study performed by (Sunetri et al., 2022) state that audit quality has a negative effect on income smoothing. An auditor with strong reputation tends to maintain that reputation in order to uphold the trust of financial statement users ensuring that the company has presented its financial reports in accordance with its actual condition. Effective audit quality is assumed to prevent income smoothing practices related to income tax.

H_5: Audit quality is capable of moderating the negative effect of income tax on income smoothing.

Audit quality plays a crucial role in ensuring the transparency of financial statements in publicly listed companies. Investors tend to rely on the financial statements provided by companies when making investment decisions. Well-audited financial information reflects the true conditions of the company and results in accurate financial reports for users of financial statements. This condition enhances investor confidence, encouraging investment and potentially bringing about an increase in the company's stock price which can generate capital gains. High audit quality helps prevent income smoothing practices that could determine the company's readiness to issue dividends to investors. The outcomes of study performed by (Al Farooque et al., 2021) state that audit quality has a positive and significant influence on corporate dividend payment decisions. Companies with indications of high audit quality tend to pay higher dividends, however opportunistic behavior by managers in decision-making cannot be entirely avoided by investors. Effective audit quality is assumed to be associated with lower information asymmetry and greater transparency (Bakri, 2021). Effective audit quality is assumed to reduce income smoothing practices related to the company's dividend policy management.

H_6: Audit quality is capable of moderating the positive effect of dividend policy on income smoothing

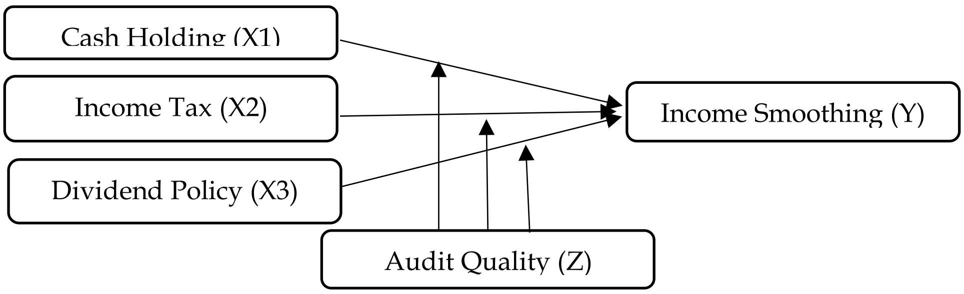

Figure 2. Framework Conceptual

Source: Research Data, 2024

RESEARCH METHODS

This research uses quantitative methods by analyzing the formulated hypotheses and secondary information gathered from the Indonesia Stock Exchange or the company's official websites. The population of this study includes companies listed in the LQ 45 index on the Indonesia Stock Exchange during the period 2019-2023. The research data is tested and analyzes using Microsoft Excel and IBM SPSS 29 software. The independent variables include cash holding, income tax, and dividend policy, while the outcome variable in this research is income smoothing. The moderating variable is audit quality. Sample of this research selection employs a purposive sampling method, with 158 companies that are part of the LQ 45 index and registered on the Indonesia Stock Exchange, regulary disclosure financial statements throughout the research period, have complete financial data, and report positive earnings throughout the study period. This research employs descriptive statistical methods, logistic regression, and moderating regression analysis to examine the relationship among variables. The regression equation model that will be testes in this research:

$$\mathrm{LN}\frac{\mathrm{PL}}{1-\mathrm{PL}} = \alpha + \beta1\mathrm{CH} + \beta2\mathrm{Tax} + \beta3\mathrm{DPR} + \mathrm{e} \ldots\ldots(1)$$

$$\mathrm{LN}\frac{\mathrm{PL}}{1-\mathrm{PL}} = \alpha + \beta1\mathrm{CH} + \beta2\mathrm{Tax} + \beta3\mathrm{DPR} + \beta4\mathrm{CH} * \mathrm{Z} + \beta5\mathrm{TAX} * \mathrm{Z} + \beta6\mathrm{DPR} * \mathrm{Z} + \mathrm{e} \ldots\ldots(2)$$

Income smoothing is proxied by the ratio of the Coefficient Variation (CV) of earnings variable and the sales variable of company (Eckel, 1981).

$$\text{Index Eckel} = \frac{\mathrm{CV}\,\Delta\mathrm{I}}{\mathrm{CV}\,\Delta\mathrm{S}} \ldots\ldots(3)$$

Calculation of CV ΔI and CV ΔS formulas can be formulated:

$$\sqrt{\frac{\sum(\Delta x-\Delta\bar{x})^2}{n-1}} : \Delta\bar{x} \ldots\ldots(4)$$

Description:

$\mathrm{CV}\,\Delta\mathrm{I}$ = Coefficient of variation of earnings change
$CV\,\Delta S$ = Coefficient of variation of sales change
Δx = Change in profit (I) or sales (S) variables between the current year and the previous year
$\Delta\bar{x}$ = Average Change in profit (I) or sales (S) variables between the current year and the previous year
N = Number of years research

Income smoothing in this research uses dummy variables, if $\mathrm{CV}\,\Delta\mathrm{I} < \mathrm{CV}\,\Delta\mathrm{S}$ then the company can be categorized as income smoothing. Companies are categorized as not income smoothing if $\mathrm{CV}\,\Delta\mathrm{I} > \mathrm{CV}\,\Delta\mathrm{S}$.

Cash holding is proxied by comparing the volatility of cash flows divided by overall assets held by the company (Opler et al., 1999).

$$\text{Cash Holding} = \frac{\text{Cash+Cash Equivalents}}{\text{Total Assets}} \ldots\ldots(5)$$

Income tax is proxied by the amount of tax on income borne by a company obtained in the financial statements through income before tax minus income tax after tax (Mahendra & Jati, 2020).

$$\text{Income Tax} = \text{Profit before Income Tax} - \text{Profits for the Year} \ldots\ldots(6)$$

The dividend payout ratio can be measured by comparing dividend per share with earning per share (Gunawan & Hardjunanto, 2020).

$$\text{Dividend Payout Ratio} = \frac{\text{Dividend per Share}}{\text{Earning per Share}} \ldots\ldots(7)$$

Audit Quality Metric Score (AQMS) is a comprehensive audit quality measurement with the sum of scores from 5 proxies from the competency dimension (audit firm size, industry specialization, and audit tenure) and the independence dimension (client importance and going concern audit opinion) (Herusetya, 2012).

Table 1. Criteria Audit Quality Metric Score

Proxies	Operational
Audit Firm Size	Given a score value of 1 if the company is audited by the BIG4 (PWC, EY, KPMG, Delloite) and a score value of 0 for audit firm other than BIG4 (Becker et al., 1998), (Krishnan, 2003).
Audit Firm Industry Specialization	Score 1 if it has industry share and score 0 otherwise. Industry market share size calculation can use sales or total assets and has an auditor market share exceeding 15% (Krishnan, 2003). $$\text{Industry Market share} = \frac{\sum_{J=1}^{Jik} \text{Total Aset}_{ijk}}{\sum_{i=1}^{I_K} \sum_{J=1}^{Jik} \text{Total Aset}_{ijk}}$$
Audit Tenure	Given a value score of 1 if the Audit Firm-j assignment period is in the interval >3 years and < 9 years which indicates high audit quality and given a value score of 0 if the otherwise (Francis & Yu, 2009); (Van Johnson et al., 2002); (Gul et al., 2009).
Client Importance	Score 1 if Audit Firm has no economic dependence on the client and score 0 for others. Utilizing the natural logarithm of total client assets as a substitute for measuring client economic importance (Chen et al., 2010). $$\text{CI}_{it} = \frac{\text{SIZE}_{it}}{[\sum_{i=1}^{n} \text{SIZE}_{it}]}$$
Going-Concern Audit Opinion	A value score of 1 is given if the company fulfills one of the conditions and a value score of 0 for the others. Going concern issues are more prominent in companies experiencing financial distress, specifically those reporting negative earnings or negative operating cash flows during the current fiscal year (Reynolds & Francis, 2000).

Source: (Herusetya, 2012)

RESULT AND DISCUSSION

Descriptive statistics provide insight into the distribution of data for each variable and identify the relationships and variability levels of the data within the framework of this research.

Table 2. Descriptive Statistics

	Minimum	Maximum	Mean	Std. Deviation
Income Smoothing	0	1	.30	0.461
Cash Holding	0.47	54.18	13.698	9.58064
Income Tax	33577	4863	3,823,716.96	7,303,675.141
Dividend Policy	0.100	11,850.000	365.057	1,839.470450
Valid N (listwise)				

Source: Research Data, 2025

Based on the table, the income smoothing as dummy variable, has a minimum value of 0 and maximum value of 1. A value of 0 indicates that the firm does not engage in income smoothing practices while a score of 1 indicates that the company engages in such practices. Income smoothing has a mean of 0,30 with a standard deviation of 0,461, indicating that the income smoothing data has a large variation, with values dispersed from the average. The cash holding variable has minimum value of 0,470, recorded by TOWR in 2022. Its maximum value is 54,18, recorded by ITMG in the same year. Cash holding has a mean of 13,6987 with a standard deviation of 9,58064, suggesting that the cash holding variable is clustered data. The Income tax variable has minimum value of 33.577, recorded by CTRA in 2019. Its maximum value is 48.639.122, recorded by BBCA in 2023. Income tax has a mean of 3823716,96 with a standard deviation of 7303675,141, showing a significant variation and values dispersed from the mean. The dividend policy has minimum value of 0,100, recorded by SMGR in 2019. Its maximum value is 11,850, recorded by ITMG in 2020. Dividend policy has a mean of 365,05762 with a standard deviation of 1839,470450, indicating a large variation and values dispersed from the mean.

Table 3. Overall Model Fit Test

Overall Model Fit (-2LogL)	
	Value
-2 Log Likehood (Block Number = 0)	194,039
-2 Log Likehood (Block Number = 1)	169,458

Source: Research Data, 2025

The overall model testing is used to evaluate whether the hypothesized model fits the research data. The results of the overall model fit shows that the -2 Log Likehood (Block Number = 0) is 194,039, which is greater than the -2 Log Likehood (Block Number = 1) which is 169,458. This indicates a descrease of 24,581 suggesting that the hypothesized model fits the data better. Futhermore, the inclusion of the variables cash holding, income tax, and dividend policy significantly improves the model fit.

Table 4. Goodness of Fit Test

Step	Chi-Square	Df	Sig.
1	9.117	8	0.333

Source: Research Data, 2025

Hosmer and Lemeshow's Goodness of Fit Test is employed to evaluate the null hypothesis that the research data adequately fits the proposed model. The test results show a significance value of 0,333. Since this significance value is greater than the threshold of 0,05, it indicates that the model is a good fit for the data and can be appropriately used to predict the observed values. Therefore, the model is considered suitable for use in this research.

Table 5. Coefficient of Determination (R^2)

Step	-2 Log Likehood	Cox & Snell R Square	Nagelkerke R Square
1	169.458	.144	0.204

Source: Research Data, 2025

In logistic regression, the coefficient of determination is evaluated using the Nagelkerke R Square value, which measures the proportion of variance in the dependent variable that can be explained by the independent variable included in the model. The Nagelkerke R Square is 0,204, indicating that 20,4% of the variation in the dependent variable is accounted for by cash holding, income tax, and dividend policy. The remaining 79,6% is attributed to other variables not captured within the scope of this model**.**

Table 6. Clasification Matrix

Observed			Predicted Income Smoothing: Not Income Smoothing	Income Smoothing	Percentage Correct
step 1	Income Smoothing	Not Income Smoothing	106	4	96.4
		Income Smoothing	36	12	25.0
Overall Percentase					69.6

Source: Research Data, 2025

The classification table serves as an analytical tool to assess the performance of the regression model in accurately classifying cases. The classification matrix shows that the model correctly predicts non income smoothing cases with an accuracy of 96,4% and predicts income smoothing cases with an accuracy of 25%. The overall accuracy of the model is 69,6%, indicating that the model correctly classifies 69,6% of the total predictions made.

Table 7. Binary Logistic Regression

Model 1

$$LN\frac{PL}{1-PL} = -0{,}386 + 0{,}010CH + 0{,}00\ Tax - 0{,}20DPR + e$$

	B	S.E.	Wald	Df	Sig	Exp(B)
Cash Holding	0.010	0.022	0.216	1	0.642	1.010
Income Tax	0.000	0.000	6.468	1	0.011	1.000
Dividend Policy	-0.020	0.032	0.375	1	0.540	0.980
Constant	-0.386	0.376	1.050	1	0.306	0.680

Model 2

$$LN\frac{PL}{1-PL} = -2{,}695 + 0{,}387CH + 0{,}000TAX - 9{,}283DPR - 0{,}121CH*Z + 0{,}000TAX*Z + 3{,}090DPR*Z + e$$

	B	S.E.	Wald	Df	Sig	Exp(B)
Cash Holding	0.387	0.136	8.117	1	0.004	1.472
Income Tax	0.000	0.000	0.014	1	0.907	1.000
Dividend Policy	-9.283	4.271	4.725	1	0.030	.000
Audit Quality	0.690	0.784	0.774	1	0.379	1.994
Cash Holding*Audit Quality	-0.121	0.042	8.238	1	0.004	.886
Income Tax*Audit Quality	0.000	0.000	0.525	1	0.469	1.000
Dividend Policy*Audit Quality	3.090	1.423	4.712	1	0.030	21.971
Constant	-2.695	2.478	1.182	1	0.277	0.068

Source: Research Data, 2025

The significance value of cash holding in the logistic regression test is 0,642, which exceeds the 0,05 of significance threshold with a regression coefficient 0,010. This indicates that the cash holding variable does not have a statistically significant partial effect on income smoothing. This finding is consistent with the research hypothesis and aligns with the results of previous studies conducted by (Sari & Darmawati, 2021), (Fadillah & Luthan, 2023), and (Musyafa & Kholilah, 2023) state that cash holding has no effect on income smoothing. Income smoothing can be carried out without direct cash flows through accrual-based accounting policies such as depreciation recognition, allowance for doubtful accounts, or amortization. High cash holdings provide operational flexibility but are not necessarily associated with financial statement manipulation. This research findings contradict agency theory, which suggest that managerial self-interest leads to agency problems. The level of cash holding does not necessarily indicate earning management, especially when effective oversight or corporate governance is present. Strong good corporate governance limits managerial discretion, preventing the use of cash reserves for financial manipulation.

The significance value of income tax in the logistic regression test is 0,011, which exceeds the 0,05 of significance threshold with a regression coefficient 0,000. This indicates that the income tax variable does have positive and statistically partial effect on income smoothing. This study is consistent with the research hypothesis and supports the findings of previous research conducted by (Palupi, 2020) and (Mahendra & Jati, 2020) state that income tax has a positive and significant effect on income smoothing. Income tax is a key factor considered by management in income smoothing strategies aimed at reducing the annual tax burden. High profit fluctuations may lead to higher tax liabilities in subsequent periods. To maintain earnings stability, management may adopt various accounting policies such as accruals, recognition of deferred tax expenses and the timing of expense and revenue recognition within an accounting period. The findings of this study support agency theory, which suggests that managers may manipulate financial statements to serve their own interests, such as reducing tax burdens. Income smoothing can be used as a strategic tool to minimize tax expenses and maintain a stable financial performance. Managers, with access to internal information and authority over reporting, may apply certain accounting methods to present consistent earnings. Tax-related accounting policies provide flexibility that can facilitate such practices. However, this information asymmetry effective governance mechanisms.

The significance value of the dividend policy variable in the logistic regression test is 0,540 which exceeds the 0,05 of significance threshold with a regression coefficient -0,020. This indicates that the dividend policy variable does not have a statistically significant partial effect on income smoothing. This finding is consistent with previous research conducted by (Putri & Lutfillah, 2020), (Khoirul Kabib et al., 2020), and (Sesilia et al., 2021) state that dividend policy has no effect on income smoothing. The amounts of dividends determined through the general meeting of shareholders (RUPS) and distributed to shareholders does not necessarily influence managerial decisions to carry out income smoothing strategies. The findings of this study contradict agency theory, which views that dividend policy can serve as a mechanism to reduce agency conflicts between managers and shareholders. In Indonesia, ownership structures are typically concentrated, giving controlling shareholders significant influence over major decisions, including dividend distribution through the general meeting of shareholders. Managers have limited incentives to engage in tend to prioritize long-term growth and sustainability. The presence of shareholders control, conservative dividend policies, and focus on long-term investment reduces the effectiveness of dividends as tool for mitigating agency conflicts.

The significance value of the interaction between cash holding and audit quality is 0,005, which fall below the 0,05 of significance threshold with a regression coefficient –0,121. Therefore, it can be concluded that audit quality moderated the effect of cash holding on income smoothing. This finding is in line with the study conducted by (Oktavinawati & Herawaty, 2022) state that audit quality can weaken the association among cash holding and income smoothing. High audit quality can restrict companies from engaging in practices that deviate from generally accepted accounting principles. This can reduce the potential for managers to manage cash inappropriately as part of income smoothing practices. This study supports contingency theory, which holds that policy effectiveness depends on specific organizational conditions. The link among cash holdings and income smoothing is influenced by audit quality. High audit quality limits earnings management through stronger oversight, while low audit quality allows greater discretion. Audit quality serves as a key contextual factor shaping managerial decisions, in line with contingency theory.

The significance value of the interaction between income tax and audit quality shows a value of 0,469 which exceeds the 0,05 of significance threshold with a regression coefficient 0,000. Therefore, it can be concluded that audit quality does not moderate the impact of the income tax on income smoothing. This study is in line with conducted by (Besoain Cornejo & Sepulveda-Velasquez, 2025) the findings show that income tax exhibits a significant positive association with income smoothing, however audit quality fails to moderate this association. High quality auditors, which include independence and competence, can increase the credibility of financial statements in minimizing managerial potential to take opportunistic actions. Tax regulation is a more dominant factor and is difficult to control only through the audit mechanism. High audit quality does not enhance the association among income tax and income smoothing due to the presence of legitimate tax planning and managerial decisions related to taxation that fall outside the scope of an audit. This study contradicts contingency theory, which suggests that policy effectiveness depends on firm-specific conditions. While audit quality can limit earnings manipulation, legal tax planning and complex managerial strategies have a stronger influence on income smoothing decisions. High audit quality may not fully detect tax-based smoothing, as audits primarily focus on compliance with accounting standards rather than the strategic use of tax planning.

The significance value of interaction between dividend policy and audit quality shows a value of 0,030 which fall below the 0,05 of significance threshold with a regression coefficient 3,090. It can be conducted that audit quality is able to moderate the positive influence of the dividend policy variable on income smoothing. Audit quality as a situational factor is in accordance with the concept of contingency in strengthening the control of a company taking actions that are adverse for financial statements users. This study is consistent with the research conducted by (Hendijani Zadeh, 2022) state that the audit quality received by a company is positively related to its dividend payment policy. Companies use dividend policy to accelerate adjustments toward their countries with ineffective financial regulations (Ellahie & Kaplan, 2021). High audit quality serve as a crucial additional instrument to strengthen the signal sent by the company through dividend payments. This study supports contingency theory, which argues that the effectiveness of managerial actions depends on specific contextual factors. While stable dividend policies may increase pressure to smoothing earnings, strong audit quality can limit such behavior by enhancing oversight. These findings highlight that the impact of corporate policies is shaped by the presence of external governance mechanisms.

CONCLUSION

The evidence from this study demonstrates that income tax has a positive and statistically significant influence on income smoothing, while cash holding and dividend policy have no significant effect on income smoothing. Audit quality is able to positively moderate the effect of cash holding and negatively moderating the impact of dividend distribution strategy on income smoothing practices. Nonetheless, audit quality does not to moderate the impact of the impact of income tax on income smoothing. In accordance with the significance values of each variable, the interaction between cash holding and dividend policy with audit quality categorizes as pure moderator, whereas the interaction between income tax and audit quality categorizes as homologizer moderator. Audit quality acts as effective oversight, but the effectiveness of oversight can be influenced by economic conditions and applicable regulations.

The findings highlight the importance of strong audit quality in limiting income smoothing, particularly through cash and dividend policies. Firms should enhance audit oversight to improve financial transparency, while investors may view audit quality as signal of earning credibility. The companies included in the criteria of this study consist of nine sectors, such as consumer cyclicals, consumer non-cyclicals, financials, basic materials, energy, industrials, properties and real estate, infrastructure, and healthcare, thus the research findings cannot be generalized to other sectors. The results of this study can serve as a consideration for management in decision-making related to income smoothing practices and can also provide useful knowledge for investors in making investment decisions, as company's financial statements do not always reflect its actual condition. There are limitations such as the use of variables that may not comprehensively explain all factors influencing income smoothing. Future research can consider other variables such as good corporate governance, managerial ownership, and leverage, which may also affect income smoothing practices. Additionally, the use of the eckel index model to detect income smoothing practices may be less accurate as each model has its own strengths and weaknesses and may be affected by the accounting methods applied by the company.

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