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# THE EFFECT OF BOARD OF DIRECTORS NARCISM, THE BOARD OF DIRECTORS' BONUS SCHEME, AND THE CEO'S DUALITY ON FINANCIAL REPORTING QUALITY

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**Abstract:** This study aims to explain the effect of Board of Directors Narcissism on Financial Reporting Quality; the effect of the Board of Directors Bonus Scheme on the Quality of Financial Reporting; and The Effect of CEO Duality on Financial Reporting Quality. This research method is quantitative causal type which is asymmetric. The research locations are all state-owned companies listed on the Indonesia Stock Exchange for the 2017-2020 period. The technique of collecting data is through surveys on secondary data on the IDX official website (www.idx.co.id). The data analysis technique is linear regression of panel data with the help of Eviews 9.0 software. The results showed that the Narcissism of the Board of Directors had a negative and significant effect on the Quality of Financial Reporting; The Board of Directors Bonus Scheme has a positive and insignificant effect on the Quality of Financial Reporting; and CEO Duality has a negative and insignificant effect on the Quality of Financial Reporting. The results of this study as input for the company are that the Narcissism of the Board of Directors, and Dualism of the CEO are not good for the company, so they must be prevented or minimized.

**Keywords:** Board of Directors Narcissism, Board of Directors Bonus Scheme, CEO Duality, Quality of Financial Reporting

## INTRODUCTION

The importance of financial reporting quality cannot be overstated. According to financial literature, the quality of the company's financial information (financial reporting quality) released in the company's financial statements has a large influence on investment decisions. Companies' financial information is used by the capital market to make investment decisions (Atuilik & Salia, 2016). The Government Accounting Standards Committee (2005: KK-10) defines qualitative financial reporting characteristics as normative measures that must be embodied in accounting information in order to achieve its objectives.

Soemarso (2004) identifies two indicators of financial reporting quality: the reporting process and financial reporting quality. Financial reporting is said to be of high quality if it meets the qualitative characteristics of information, which include fundamental qualitative characteristics such as relevance and faithful representation, as well as enhancing qualitative characteristics such as comparability, verifiability (verifiability), timeliness (timeline), and understanding (understandability) (Gautama et al., 2017).

Based on this description, it appears that the variables of CEO narcissism, CEO bonuses, and CEO duality are related to financial reporting quality. CEO narcissism, CEO bonuses, and CEO duality are assumed to affect financial quality independence, despite the fact that this aspect of independence is important in influencing financial reporting quality and audit quality (Haeridistia & Fadjarenie, 2019). CEO narcissism, CEO bonuses, and CEO duality are thought to influence a variety of other factors, including investment decisions, funding decisions, and dividend policy (Triani & Tarmidi, 2019).

It is interesting to investigate SOEs, specifically the quality of SOE financial reporting. Because, despite the fact that these SOEs are highly regulated, there have been numerous high-profile cases involving the financial reporting quality of SOEs. There are several issues concerning the reporting quality of SOEs. Consider the case of PT Garuda Indonesia (Persero) Tbk, which was accused of financial engineering in 2019. This case began with the Supreme Audit Agency's (BPK) findings that there had been financial reporting manipulation (financial engineering within the company, BPK discovered the recognition of the company's receivables in financial reporting, demonstrating that the audit process of Garuda Indonesia's financial reporting does not fully follow the applicable accounting standards) (Hariyanto, Suganda, and Soft, 2020). Ari Askhara's financial reporting has been "polished," so that the news "Certificate of CT's Story Rejects Garuda's Financial Reporting Polesan Ari Askara" appears (Idris, 2020).

The case of revealing state losses in a number of SOEs is inextricably linked to the issue of poor reporting quality. Corruption occurred in PT Asuransi Jiwsraya (Persero), resulting in a loss of Rp 16.8 trillion. There was poor financial reporting, with the strategy of buying low-quality stocks and mutual funds, resulting in tens of trillions of dollars in losses. In the case of Jiwasraya, there are indications of engineering in the formation of share prices (Idris, 2020). PT Asabri (Persero) caused the state even more losses, totaling Rp. 22.78 trillion. The loss to the state is the result of share mismanagement. Given that the large state losses were only discovered after the losses had been running for a long time, this demonstrates that the two SOEs' financial reporting is of poor quality (Sari, 2021).

The delay in submitting financial reporting is an example of financial quality. This occurred, among other things, in 2019. Financial reporting should be submitted to the Ministry of BUMN no later than February 15, according to the Joint Regulation of the Ministers of Finance Number 23/PMK.01/2007 and the Regulation of the Ministers of SOEs Number PER-04/MBU/2007. Meanwhile, two major SOEs in the energy sector, PT Pertamina (Persero) and PT PLN, do not appear to have collected financial reports (Persero). Previously, Pertamina (Persero) submitted a financial report submission delay from the expected schedule because they were still auditing subsidies (CNN, 2019).

Because the performance of SOEs in 2020 was adversely impacted by the Covid-19 pandemic, it is interesting to look at the quality of SOE financial reporting. As a result, on average, SOE companies produced consolidated financial reports. From a profit of Rp. 124 trillion in 2019 to Rp. 28 trillion in 2020, all SOEs' profits decreased by 77%. The majority of profits (90.7%) from the 104 state-owned businesses were made by just five SOEs: BRI (26.4%), Bank Mandiri (22.2%), Pertamina (19.1%), Telkom (17.8%), and BNI (5.2%) (Pranoto, 2021).

Internal control, which is influenced by the board of directors, management, and other personnel, is another issue related to the quality of financial reporting in state-owned enterprises. BUMN firms adhere to the Statement of Audit Standards No. 62 (PSA 62), particularly in terms of internal control. PSA 62 is a problem for SOEs that go public because listed companies must also follow capital market rules and Law No. 199 concerning SOEs. Some listed SOEs are conservative while still complying with PSA 62; some even issued three reports in addition to Bapepam PSA 29 rules, resulting in four independent auditor reports. The Indonesian Institute of Accountants (IAI KAP) has published an exposure draft of PSA 75 as an amendment to PSA 62, but its status is still pending (BPKP.go.id, 2021).

There have been a number of previous studies that are relevant to the theme of financial reporting. The author traces 23 previous research journals, both domestic and international, with a publication period of 2017-2020, as shown in table 2.1. The following are known based on 23 previous studies, as summarized in table 2.1: First, three independent variables influence the same dependent variable (Firm Performance, with Financial Performance Proxy). The three variables that both affect the same dependent variable are (1) CEO Narcissism (X1) variable affects Firm Performance (with Financial Performance Proxy) (Uppal, 2020); (2) CEO Bonus/

Compensation (X2) variable affects Firm Performance (with Financial Performance Proxy) (Teti et al., 2017); (3) CEO Duality (X3) variable affects Firm Performance (with Financial Performance Proxy) (Mubeen et al., 2020).

Second, with the dependent variable "Quality of Financial Reporting," the independent variable is not one of the three independent variables (CEO Narcissism, CEO Bonus/Compensation, and CEO Duality), indicating a research gap that this study can fill. This study combines three independent variables that were previously studied separately. As a result, the study will introduce three independent variables (CEO Narcissism (X1), CEO Bonus/CEO Compensation (X2), and CEO Duality (X3) to see if they affect Financial Reporting Quality.

In recent years, psychologists and business scholars have begun to regard narcissism as a personality trait rather than a disorder. The significance of narcissism as a research construct stems from its relationship to individuals' categorization of themselves, others, and the environment, as well as the interpretation of the phenomena they perceive and how their perception and processing of information can influence the decisions they make (Al-Shammari et al., 2019)

According to (Al-Shammari et al., 2019)research on 134 CEOs of Fortune 500 companies from 2008 to 2013, there is a link between CEO narcissism and corporate social responsibility (CSR). The positive effect of CEO narcissism on CSR is also supported by research conducted by (Uppal, 2020)on 373 CEOs in the Indian automotive industry, which found that CEO narcissism has a curvilinear effect on company performance. This means that while CEO narcissism can be beneficial to company performance, it can also be detrimental outside of the company's performance environment. The research of also shows that CEO narcissism has a positive effect on CSR.

In contrast to previous research, the purpose of this study is to investigate the impact of CEO narcissism on financial reporting. According to (Al-Shammari et al., 2019), CEO narcissism can influence the decisions they make, as evidenced by the research of (Chen et al., 2021), and (Al-Shammari et al., 2019), which proves CEO narcissism can affect CSR. According to (Uppal, 2020) research, CEO narcissism has an impact on company performance. Based on these findings, the authors intend to investigate the impact of CEO narcissism on financial reporting quality.

Previous research has shown that the CEO Bonus has an impact on other aspects of the company. (McNichols & Stubben, 2008)discovered that CEO bonuses have an effect on earnings management. The research of (Cho et al., 2019)demonstrates that CEO bonuses have an impact on shareholder returns. Both studies show that CEO bonuses can have an impact on other aspects of a company. As a result, the authors of this study wanted to investigate the impact of CEO bonuses on the quality of financial reporting. Because, as suggested by (Gan et al., 2020), the relationship between CEO compensation and performance can be biased in favor of the CEO at the expense of shareholders if the compensation committee is influenced by insiders, the CEO Bonus is assumed to affect the Quality of Financial Reporting.

Previous research has shown that CEO Duality can have an impact on other aspects of the business. According to (Uppal, 2020) research on 373 CEOs in India's automotive industry, CEO duality has an impact on company performance. (Broye et al., 2017)demonstrate the effect of CEO Duality on Compensation. (Mubeen et al., 2020)found that CEO Duality has an impact on company performance. Based on these two studies, the author wishes to investigate the impact of CEO Duality on other aspects of the business, specifically the Quality of Corporate Reporting. The authors believe that CEO duality will have an impact on the quality of corporate reporting because CEO duality is the practice of combining CEO and Board positions into a single role. This practice reduces the CEO's monitoring capacity while increasing the CEO's discretion, which can have both positive and negative consequences for the company. On the one hand, there will be greater managerial wisdom that comes with the duality of the CEO because it provides firmer and more decisive corporate leadership. As a result, it is understandable that CEO Duality may have an impact on Financial Reporting Quality.

## MATERIALS AND METHODS

This study is intended to be applied research rather than basic research . To differentiate it from an experimental study, this type of research is a survey study (Cooper et al., 2006).

This is a quantitative research method (Creswell & Creswell, 2017). The type of quantitative research used in this study is causal studies, or research based on the concept of cause. More specifically, the causal study in this study is asymmetrical (asymmetrical relationship), which means it has only one effect, namely the influence of the independent variable on the dependent variable (Cooper et al., 2006). This study investigates the effect of four variables, including three independent variables, namely board narcissism (X1), director bonus scheme (X2), and CEO duality (X3), and one dependent variable, namely financial reporting quality (X3) (Y).

The operational definition of variable measurement is as follows:

| No | Vari-abel | Definition | Measurement | Ratio |
|---|---|---|---|---|
| 1. | Narcissism of the Board of Directors (X1) | Narcissists seek excellence, have very high self-confidence, are often considered arrogant, and pursue recognition and affirmation (Ahn | CEO narcissism uses a four-item index developed by (Chatterjee & Hambrick, 2007). These include: 1) advantages photo of the CEO in the annual report of the company; (2) THE CEO stands out in the company's press release; (3) relative cash | Ratio |

| | | | | |
|---|---|---|---|---|
| | | et al., 2020). | CEO compensation; and (4) the CEO's relative non-cash compensation. These items represent one or more common aspects of the narcissistic personality (see Chatterjee & Hambrick, 2007): superiority/arrogance, exploitative/entitlement, self-absorption/self-admiration, and leadership/authority. (Ahn et al., 2020). | |
| | Board of Directors Bonus Scheme (X2) | COMP_PCT = EQUITY_TOT, equity-based compensation ratio (limited number of options and shares) for total compensation; or OPTION_TOT, the ratio of the option given to the total compensation in one year; or RESTRICTED_TOT, the ratio of restricted shares granted to total compensation (Gan et al., 2020). | $Net\ Profit\ Trend\ Index = \frac{Net\ Incon}{Net\ Income}$ (Indriaswari & Nita, 2018) | Ratio |
| | Dualit as CEO (X3) | CEO duality is the practice of consolidating ceo positions and Board seats into a single role (Wang et al., 2018: 172) | The measurement of CEO Duality (*CEOduality)* uses dummy, the value of one if the CEO is the chairman of the board, and zero if it is the other way around (Gan et al., 2020). | Nominal |

| | | | | |
|---|---|---|---|---|
| | Quality of Financial Reporting (Y) | ΔΔRi,t is the annual change in the receivables of the company i in year t; Δ Slaesi,t is the annual change in the company's revenue i in year t. All variables are divided by the total assets of the previous year (McNichols & Stubben, 2008) (Gautama et al., 2017). | Where:<br><br>ΔΔRi,t is the annual change in the receivables of the company i in year t; Δ Slaesi,t is the annual change in the company's revenue i in year t. All variables are divided by the total assets of the previous year (McNichols & Stubben, 2008)(Gautama et al., 2017). | |

The general public (Sekaran & Bougie, 2016). This study includes all state-owned enterprises listed on the Indonesia Stock Exchange (IDX). All state-owned companies listed on the Indonesia Stock Exchange (IDX) with complete data according to the research variables and the 2017-2020 period comprise the affordable population (Sekaran & Bougie, 2016). The sample consists of all state-owned companies that are listed on the Indonesia Stock Exchange (IDX) and are part of the affordable population. The sampling technique used was purposeful sampling. (Cooper et al., 2006)distinguishes two types of purposive sampling techniques: judgment sampling and quota sampling. This study employs judgment sampling, in which the researcher selects the sample based on criteria determined by the researcher's consideration, state-owned companies that, in addition to being listed on the IDX, have gone public at least one year before 2018 and are still listed on the IDX at least until 2020; and has complete data for four research variables from 2017 to 2020. The data in this study is collected on a yearly basis (yearly).

The data in this study is secondary data (Kuncoro, 2011; (Sugiyono, 2013). As a result, the library research method was used to collect secondary data on all variables via the IDX official website (www.idx.co.id), the Financial Services Authority (www.ojk.go.id), and the websites of each of the sampled companies.

The data analysis method in this research is descriptive method and multiple linear regression. The multiple linear regression equation model in this study uses panel data (Widarjono, 2015) as follows:

$$Y_{it} = \alpha + \beta_1 X1_{it} + \beta_2 X_{2it} + \beta_3 X_{3it} + \varepsilon_{it}$$

Where:

$Y_{it}$ = Quality of Financial Reporting

$X1_{it}$ = Directors Narcissism

$X2_{it}$ = Directors Bonus Scheme

$X3_{it}$ = CEO Duality

$B_{1,2,3}$ = Slope regression

coefficient

t= Period t

i= 1st Entity

a= Constant

e= Variable outside this research model

The t-test was used for the partial model and the F-test for the simultaneous model in this study. If the p-value is less than 0.10, the effect of the independent variable on the dependent variable is significant; otherwise, the effect is not significant.

Data analysis in this study is aided by the advanced Eviews 9.0 software. Based on sensitivity analysis using Chow, Hausman, and the Lagrange Multiplier, one of three alternative models (common effect, fixed effect, or random effect) terpilih model etimasi yang terpilih adalah common effect model. Because of this, the primary assumptions used are heteroskedastisitas and multikolinearitas

## RESULTS AND DISCUSSION

The regression results of this study indicate that

1. **Influence of the Board of Directors (X1) on the Quality of Financial Statements (Y)**

The influence of the Board of Directors' narcissism (X1) on Financial Reporting Quality (Y) has a coefficient of influence of -318.478 and a t value of -1.811029, with a p-value of 0.0741. Hypothesis 1 is accepted because the p-value of the board of directors' narcissism variable is 0.0741 and less than 0.10, indicating that the board of directors' narcissism has a significant effect on the quality of financial reporting. The coefficient value of -318.478 indicates that the direction of influence is negative, indicating that the board of directors' narcissism has a significant negative impact on the quality of financial reporting.

The findings revealed that the Board of Directors' Narcissism had a negative and significant impact on the Quality of Financial Reporting. These findings demonstrate that the more narcissistic the board of directors, the lower the quality of financial reporting. These findings also support the notion that the narcissistic Board of Directors is highly motivated to ensure that the company they manage always looks good, with the goal of improving their personal image as a result of the company's success. Because of the board of directors' high narcissism, companies tend to engage in unfavorable practices such as earnings management, which has a negative impact on the level of financial statement quality.

These findings support the work of (Salehi et al., 2020), who found that CEO narcissism is linked to corporate risk taking. CEOs with high levels of narcissism have an unfavorable impact on company decision making, posing risks to the company.

2. **The Impact of the Bonus Scheme (X2) on Financial Reporting Quality (Y)**

The coefficient of influence for the Board of Directors Bonus Scheme on Financial Reporting Quality is 0.270436, the t value is 0.253385, and the p-value is 0.8007. The p-value of the Board of Directors Bonus Scheme variable is 0.8007, which is greater than 0.10, indicating that the Board of Directors bonus scheme has no significant effect on financial reporting quality, and thus hypothesis 2 is rejected. The coefficient value 0.270438, on the other hand, explains that the direction of influence is positive, implying that the board of directors bonus scheme has no significant positive effect on financial reporting quality.

According to the findings, the Board of Directors Bonus Scheme had a positive but not statistically significant effect on the Quality of Financial Reporting. These findings demonstrate that, while the bonus scheme for the board of directors may make the board of directors happy or unhappy, it does not necessarily have an impact on the practice of preparing high-quality financial reporting. The high influence of other factors on financial reporting quality is thought to have contributed

The findings of this study contradict those of (Tahir et al., 2019), who investigated the effect of CEO bonuses on earnings management and found negative results, as well as (Cho et al., 2019), who investigated the effect of CEO bonuses on shareholder return and found negative results, and (Armstrong et al., 2017), who investigated the effect of CEO incentives on earnings per share and found negative results.

**3. The Impact of CEO Duality (X3) on Financial Reporting Quality (Y)**

The coefficient of influence for CEO Duality on Financial Reporting Quality (Y) is -95.00431, the t value is -0.154568, and the p-value is 0.8776. The p-value for the CEO duality variable is 0.8776, which is greater than 0.10, indicating that CEO duality has no significant effect on financial reporting quality, and thus hypothesis 3 is rejected. The coefficient value -95,00431 indicates that the direction of influence is negative, implying that CEO duality has no significant negative effect on financial reporting quality.

The findings revealed that CEO Duality had a negative and insignificant effect on Financial Reporting Quality. These findings explain why, when CEO duality occurs in a company, the CEO has very high authority over company policies and has an impact on policy arbitrariness, including financial statement preparation. Nonetheless, this authority is not very strong in the process of preparing financial reporting because other factors have a greater influence on the quality of financial reporting.

The findings of this study contradict (Mubeen et al., 2020), who examined the effect of CEO Duality on Firm Performance and found significant positive results, (Broye et al., 2017), who examined the effect of CEO Duality on Compensation and found positive relationship findings, and (Teti et al., 2017), who discovered the effect of CEO Duality on M & A Performance

## CONCLUSIONS)

Narcissism of the Board of Directors (X1) has a negative and significant effect on the Quality of Financial Reporting (Y). It means that the first hypothesis is proven. The Board of Directors Bonus Scheme (X2) has a positive and insignificant effect on the Quality of Financial Reporting (Y). It means that the second hypothesis is not proven.

CEO duality (X3) has a negative and insignificant effect on the Quality of Financial Reporting (Y). It means that the third hypothesis is not proven.

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