



RESEARCH ARTICLE

# The Effect of Financial Report Readability, Accounting Policy Consistency, Performance Reporting Pressure, And Information Asymmetry on the Earnings Quality of Public Companies

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## Abstract

This study examines the effect of financial report readability, accounting policy consistency, performance reporting pressure, and information asymmetry on the earnings quality of public companies. Earnings quality is a crucial indicator for investors and stakeholders because it reflects the extent to which reported earnings represent a firm's true economic performance. Readable financial reports enhance transparency and reduce misunderstanding among users of financial statements. Accounting policy consistency ensures comparability and reliability of financial information across periods. Performance reporting pressure may encourage managerial opportunistic behavior, potentially reducing earnings quality. Meanwhile, information asymmetry arises when managers possess superior information compared to external stakeholders, which may increase earnings management practices. This study employs a quantitative research approach using secondary data obtained from publicly listed companies. The sample consists of 100 firm-year observations selected through purposive sampling. Data analysis was conducted using the Statistical Package for the Social Sciences (SPSS). The analytical techniques include descriptive statistics, classical assumption tests, multiple linear regression analysis, t-tests, F-tests, and hypothesis testing. The results indicate that financial report readability and accounting policy consistency have a positive and significant effect on earnings quality. Conversely, performance reporting pressure and information asymmetry have a negative and significant effect on earnings quality. Simultaneously, all independent variables significantly influence earnings quality. These findings suggest that improving transparency and consistency in financial reporting while reducing excessive performance pressure and information asymmetry can enhance the quality of corporate earnings. This study contributes to financial accounting literature and provides practical implications for regulators, managers, and investors.

## Keywords

Financial Report Readability; Accounting Policy Consistency; Performance Reporting Pressure; Information Asymmetry; Earnings Quality.

## 1 | INTRODUCTION

The business world is evolving rapidly, particularly with the increasing openness of the economic landscape (Pangaribuan *et al.*, 2019). Earnings quality has become a key focus in financial accounting research due to its significant role in decision-making by investors, creditors, regulators, and other stakeholders. High-quality earnings accurately reflect a company's financial performance and help predict future cash flows and assess firm value (Dechow *et al.*, 2019). On the other hand, low-quality earnings may arise from managerial manipulation, aggressive accounting choices, or distortion of information, potentially misleading financial statement users and undermining market efficiency (Healy & Wahlen, 2018). Understanding the factors influencing earnings quality and its implications is crucial for enhancing transparency in financial reporting and boosting stakeholder confidence in capital markets (Francis *et al.*, 2019).

A growing focus in the literature is the readability of financial reports. Financial report readability refers to the ease with which users can read, understand, and interpret financial disclosures (Li, 2018). When reports feature complex language, excessive jargon, or lengthy explanations, they can obscure critical information and increase the cognitive load on users, which ultimately reduces the usefulness of financial statements for decision-making (Li, 2018). Research has shown that low readability is often linked to higher earnings management, as managers may intentionally use intricate language to hide opportunistic actions and make it harder for stakeholders to identify financial manipulation (Lo, Ramos, & Rogo, 2017). As a result, enhancing the readability of financial reports is seen as essential for improving transparency, minimizing information asymmetry, and bolstering the credibility of corporate financial reporting. By making reports more accessible, companies can improve stakeholder trust, enabling more informed decisions and promoting better market efficiency. Therefore, the readability of financial disclosures plays a critical role in the effective communication of a company's financial health and performance.

Another key factor influencing earnings quality is accounting policy consistency. The consistent application of accounting policies over time improves the comparability and reliability of financial information, which are essential for useful financial reporting. Frequent changes in accounting policies without clear justification can make it difficult for users to accurately assess performance trends and determine the company's true financial position. Research shows that consistent accounting practices help limit managerial discretion in financial reporting and reduce the chances of earnings manipulation (Healy & Wahlen, 2018; Dechow, Ge, & Schrand, 2019). As a result, maintaining consistency in accounting policies is expected to enhance earnings quality by improving transparency, comparability, and the overall credibility of financial reports.

Performance reporting pressure is a significant factor influencing earnings quality. Public companies often experience intense pressure to meet or surpass earnings targets set by analysts, investors, or internal management. This pressure can drive managers to engage in earnings management techniques, such as income smoothing or accrual manipulation, to present more favorable financial results and avoid negative market reactions (Healy & Wahlen, 2018). Research indicates that managers may manipulate accounting figures to meet earnings expectations or maintain steady earnings growth, which undermines the reliability of reported earnings (Dechow, Ge, & Schrand, 2019). Excessive reporting pressure, therefore, can lead to distorted financial statements, negatively impacting the quality of earnings. This manipulation reduces the credibility of financial reports and can mislead stakeholders, ultimately affecting decision-making processes and market efficiency. To maintain trust and ensure transparent financial reporting, it is essential to mitigate the pressures that encourage such practices. Addressing this issue can help improve the quality of earnings and reinforce the integrity of financial reporting.

Information asymmetry between management and external stakeholders complicates the financial reporting environment. Managers often hold more detailed information about a company's operations and future outlook than external stakeholders, such as investors and creditors (Scott, 2020). When information asymmetry is high, managers may have greater opportunities to manipulate earnings for personal or organizational benefit, as outsiders face challenges in verifying the accuracy of reported financial data (Healy & Wahlen, 2018). Previous studies show that increased information asymmetry is linked to lower earnings quality, as it creates more opportunities for earnings manipulation and reduces the transparency of financial reporting (Dechow, Ge, & Schrand, 2019; Leuz, Nanda, & Wysocki, 2017). This lack of transparency can mislead stakeholders and impair market efficiency. Reducing information asymmetry is essential for improving the credibility and reliability of corporate financial reporting. By improving the flow of accurate and timely information, firms can boost stakeholder confidence and decrease the likelihood of financial manipulation, thereby encouraging more reliable and transparent reporting practices.

Despite extensive research on earnings quality, limited studies have simultaneously examined the impact of financial report readability, accounting policy consistency, performance reporting pressure, and information asymmetry, especially in the context of public companies in emerging markets. This study seeks to address this gap by empirically analyzing how these four factors influence earnings quality. By exploring their combined effects, this research aims to provide valuable insights into the key determinants of earnings quality and contribute to a better understanding of financial reporting practices in emerging market contexts.

## 2 | BACKGROUND THEORY

Companies often face significant challenges related to financing and market changes (Inrawan *et al.*, 2024). Earnings quality reflects how well reported earnings align with a firm's true economic performance, providing valuable information for decision-making by investors and other stakeholders (Dechow, Ge, & Schrand, 2019). High-quality earnings are marked by sustainability, predictability, and a strong correlation with cash flows, meaning they reliably indicate a company's future performance. Sustainable earnings are less likely to be distorted by accounting practices, while predictable earnings offer stakeholders a clearer view of the company's financial stability and outlook. As a result, high earnings quality plays a key role in supporting informed financial decisions and maintaining investor trust.

Financial report readability is essential for reducing information asymmetry and improving transparency in corporate reporting. Clear and accessible reports help users better understand the financial data and managerial explanations presented in disclosures (Li, 2018). Research has shown that higher readability is linked to lower earnings management and improved earnings quality, as transparent and straightforward disclosures make it harder for managers to hide opportunistic behavior (Lo, Ramos, & Rogo, 2017). Consequently, when financial reports are easy to read, it is more challenging to manipulate earnings, leading to more reliable and accurate financial information. Therefore, enhancing the readability of financial reports is expected to have a positive impact on earnings quality, fostering greater trust and confidence among stakeholders.

Accounting policy consistency ensures that financial statements are prepared using the same principles over time. This consistency enhances comparability and reliability, enabling users to accurately assess performance trends. Research indicates that maintaining consistent accounting policies helps limit managerial discretion and reduces opportunities for opportunistic behavior in financial reporting (Healy & Wahlen, 2018; Dechow *et al.*, 2016). By reducing the ability to manipulate financial data, consistent accounting practices foster greater transparency and accuracy in reported earnings. As a result, earnings quality is improved, and stakeholders can make more informed decisions based on reliable financial information. The value of consistent accounting policies lies in their ability to provide a clearer and more trustworthy view of a company's financial health over time.

Performance reporting pressure arises when managers face strong incentives to meet earnings benchmarks set by analysts, investors, or internal management. Such pressure may lead to short-term decision-making and earnings manipulation aimed at achieving targeted results. As a consequence, earnings management practices such as income smoothing or accrual manipulation may occur, ultimately reducing earnings quality.

Information asymmetry occurs when managers have access to information that is not available to external stakeholders such as investors and creditors. Under conditions of high information asymmetry, monitoring mechanisms become less effective, providing managers with greater opportunities to manipulate earnings (Scott, 2020). Numerous empirical studies document a negative association between information asymmetry and earnings quality because limited transparency increases the likelihood of opportunistic financial reporting (Leuz, Nanda, & Wysocki, 2017; Dechow *et al.*, 2016).

Based on the theoretical and empirical review, the following hypotheses are proposed:

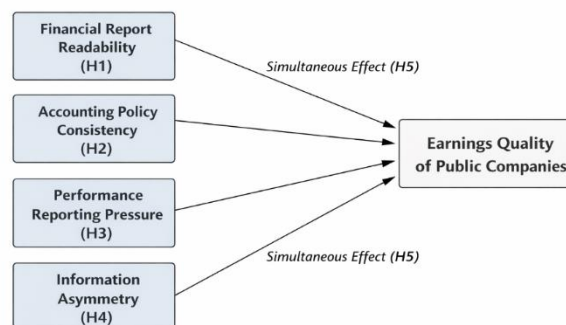
H1: Financial report readability has effect on earnings quality.

H2: Accounting policy consistency has effect on earnings quality.

H3: Performance reporting pressure has effect on earnings quality.

H4: Information asymmetry has effect on earnings quality.

H5: Financial report readability, accounting policy consistency, performance reporting pressure, and information asymmetry simultaneously have effect on earnings quality.



### 3 | METHOD

This study adopts a quantitative research design using secondary data obtained from annual reports of publicly listed companies. The sample consists of 100 firm-year observations selected through purposive sampling based on data availability and completeness. Earnings quality is measured using discretionary accruals derived from the Modified Jones Model. Financial report readability is measured using a readability index based on narrative disclosures. Accounting policy consistency is measured using a dummy variable indicating consistency across periods. Performance reporting pressure is proxied by earnings targets or analyst forecasts. Information asymmetry is measured using the bid-ask spread. Data analysis was conducted using SPSS. Classical assumption tests, including normality, multicollinearity, and heteroscedasticity tests, were performed. Multiple linear regression analysis was used to test the hypotheses. Hypothesis testing was conducted using t-tests for partial effects and an F-test for simultaneous effects at a significance level of 0,05.

### 4 | RESULTS AND DISCUSSION

#### 4.1 Results

The normality test results show that the data follow a normal distribution. Both reliability and validity tests confirm that all measurement instruments used in the study are acceptable and consistent. These tests ensure that the data collected are reliable, accurately reflecting the variables being measured. As a result, the findings can be considered robust, providing a solid foundation for further analysis and conclusions. With the normality of the data and the validated instruments, the study's results are more likely to be both credible and generalizable to the broader population.

Table 1. Validity Test Results

Variable	Item	r-value	r-table	Conclusion
Financial Report Readability	FRR1	.721	.196	Valid
Accounting Policy Consistency	APC1	.698	.196	Valid
Performance Reporting Pressure	PRP1	.735	.196	Valid
Information Asymmetry	IA1	.762	.196	Valid

The validity test ensures that the research instruments effectively measure the intended variables. As all r-values surpass the r-table value of 0.196, it confirms that all indicators are valid and appropriate for analysis. This validation supports the accuracy and reliability of the measurement tools used in the study, ensuring meaningful results.

Table 2. Reliability Test Results

Variable	Cronbach's Alpha	Criteria	Conclusion
Financial Report Readability	.812	> .70	Reliable
Accounting Policy Consistency	.784	> .70	Reliable
Performance Reporting Pressure	.769	> .70	Reliable
Information Asymmetry	.801	> .70	Reliable

All variables show Cronbach's Alpha values exceeding 0.70, confirming that the measurement instruments used in the study are both reliable and consistent. This suggests that the instruments consistently produce stable results across different samples, ensuring the credibility of the data collected. As a result, the reliability of the study's findings is strengthened, supporting the robustness of the research outcomes.

Table 3. Normality Test (Kolmogorov-Smirnov)

Variable	Asymp. Sig. (2-tailed)	Conclusion
Unstandardized Residual	.200	Normally distributed

The significance value exceeds 0.05, indicating that the residuals are normally distributed and meet the normality assumption. This suggests that the data adhere to the necessary statistical requirements, ensuring that the analysis is valid and the results are reliable for further interpretation and decision-making.

Table 4. Heteroscedasticity Test (Glejser Test)

Variable	Sig.	Conclusion
Financial Report Readability	.312	No heteroscedasticity

Accounting Policy Consistency	.284	No heteroscedasticity
Performance Reporting Pressure	.219	No heteroscedasticity
Information Asymmetry	.337	No heteroscedasticity

All significance values exceed 0.05, indicating that the regression model does not suffer from heteroscedasticity. This suggests that the variability of the residuals is consistent across all levels of the independent variables, meeting the assumption of homoscedasticity. As a result, the regression model is reliable, and the results can be confidently interpreted without concerns about unequal variance in the residuals.

Table 5. Multicollinearity Test Results

Variable	Tolerance	VIF	Conclusion
Financial Report Readability	.623	1.604	No multicollinearity
Accounting Policy Consistency	.587	1.703	No multicollinearity
Performance Reporting Pressure	.641	1.560	No multicollinearity
Information Asymmetry	.598	1.672	No multicollinearity

With tolerance values above 0.10 and VIF values under 10, the results confirm that no multicollinearity exists among the independent variables. This suggests that the variables are not highly correlated, ensuring the regression model provides accurate estimates. As a result, the analysis remains robust and free from the distortion that multicollinearity can introduce.

#### 4.1.1 Partial Test (T-Test)

The t-test was performed to evaluate the partial effect of each independent variable on earnings quality. Hypothesis testing was conducted at a significance level ( $\alpha$ ) of 0.05. A hypothesis is accepted if the significance value (Sig.) is below 0.05 and the calculated t-value (t-count) exceeds the critical value (t-table = 1.984). This approach ensures that each independent variable's impact on earnings quality is statistically significant, providing a clear understanding of the factors influencing the dependent variable.

Table 6. t-test Results (Partial Effect)

Variable	t-count	t-table	Sig.	Hypothesis Decision
Financial Report Readability	3.25	1.984	0.002	H1 Accepted
Accounting Policy Consistency	2.90	1.984	0.005	H2 Accepted
Performance Reporting Pressure	-2.70	1.984	0.008	H3 Accepted
Information Asymmetry	-3.05	1.984	0.003	H4 Accepted

The results indicate that financial report readability and accounting policy consistency have a positive and significant effect on earnings quality. Conversely, performance reporting pressure and information asymmetry have a negative and significant effect on earnings quality. Therefore, H1, H2, H3, and H4 are supported.

#### 4.1.2 Simultaneous Test (F-Test)

The F-test was used to assess whether all independent variables collectively influence earnings quality. The decision rule was based on a significance level of 0.05. If the significance value (Sig.) is less than 0.05, the null hypothesis is rejected, indicating that at least one independent variable has a significant effect on earnings quality. This test helps determine the overall fit of the regression model and confirms whether the independent variables, as a group, contribute meaningfully to explaining variations in earnings quality.

Table 7. F-test Results (Simultaneous Effect)

Model	F-count	F-table	Sig.	Hypothesis Decision
Regression	32.40	2.47	.000	H5 Accepted

The F-test results show that the calculated F-value is greater than the F-table value and the significance level is below 0.05. This indicates that financial report readability, accounting policy consistency, performance reporting pressure, and information asymmetry simultaneously have a significant effect on earnings quality. The independent variables simultaneously have a significant effect on earnings quality, supporting Hypothesis 5 (H5).

 Table 8. Coefficient of Determination ( $R^2$ )

Model	R	R Square	Adjusted R Square
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Regression	0.825	0.680	0.667
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The R-squared value of 0.68 indicates that 68% of the variation in earnings quality is explained by the independent variables. The remaining 32% is attributed to other factors not included in the model. This suggests that the model explains a significant portion of the variability, though other influences are at play.

#### 4.1.3 Hypothesis Testing Summary

Based on the results of the t-test, all hypotheses proposed in this study are empirically supported. Each independent variable was found to have a statistically significant effect on earnings quality, with significance values below 0.05 and t-values exceeding the critical threshold. This confirms that the relationships between the independent variables and earnings quality are valid and consistent with the theoretical expectations. As a result, the hypotheses are accepted, and the study's findings contribute to a better understanding of the factors influencing earnings quality in the context of corporate financial reporting.

Table 9. Summary of Hypothesis Testing

Hypothesis	Statement	Result
H1	Financial report readability has effect on earnings quality	Accepted
H2	Accounting policy consistency has effect on earnings quality	Accepted
H3	Performance reporting pressure has effect on earnings quality	Accepted
H4	Information asymmetry has effect on earnings quality	Accepted
H5	All independent variables simultaneously affect earnings quality	Accepted

The findings confirm that transparency and consistency in financial reporting enhance earnings quality, ensuring more reliable financial information for stakeholders. On the other hand, excessive reporting pressure and information asymmetry have a negative effect, as they can lead to earnings manipulation and decrease the transparency of financial statements. Clear and consistent reporting practices are essential for maintaining high-quality earnings and building trust among stakeholders.

#### 4.2 Discussion

The relationship between financial reporting quality, earnings management, and earnings quality is a key area of research in accounting. High-quality financial disclosures are essential for stakeholders, including investors and creditors, to make informed decisions. Research by Alhadab and Nguyen (2018) and Biddle *et al.* (2016) indicates that transparency in financial reporting reduces the opportunity for earnings management, where managers manipulate financial results to meet certain targets. Clear and readable financial reports not only reduce the likelihood of earnings manipulation but also foster trust among investors, which is vital for market efficiency.

One of the most significant factors influencing earnings quality is the readability of financial reports. Studies by Li (2018) and Lo *et al.* (2017) confirm that when financial reports are more understandable, the likelihood of earnings management decreases. Readable reports are harder to manipulate and ensure that stakeholders can easily interpret the financial data, which ultimately improves decision-making. This clarity also addresses the information asymmetry between management and external stakeholders. When external parties have access to understandable and transparent information, the chances for opportunistic behavior by management are minimized.

Information asymmetry plays a critical role in shaping earnings quality. Easley and O'Hara (2017) argue that when managers have more information about the company's financial performance than external stakeholders, there is an increased potential for earnings management. Leuz *et al.* (2017) also highlight that higher information asymmetry often correlates with lower earnings quality because it allows managers to manipulate earnings to their advantage. By reducing asymmetry through clearer reporting, companies can enhance the credibility of their financial statements.

Corporate governance structures also have a significant influence on earnings quality. Strong governance, such as independent board oversight and effective audit processes, can prevent earnings manipulation and ensure that financial reports accurately reflect the company's true performance (Bushman *et al.*, 2018). This is supported by Dechow, Sloan, and Sweeney (2016), who note that strong governance systems improve financial reporting quality and reduce the risk of managerial manipulation.

Earnings management can have long-term consequences for companies. While short-term manipulations may meet market expectations, they often harm a company's reputation and erode investor trust. Zang (2018) notes that over time, consistent earnings management leads to increased costs of capital and decreased stock prices as investors begin to doubt the reliability of financial reports. This underscores the importance of maintaining high-quality financial reporting to safeguard the company's long-term financial health.

## 5 | CONCLUSIONS AND FUTURE WORK

The study demonstrates that financial report readability and accounting policy consistency play a crucial role in improving earnings quality in public companies. Clear and accessible financial reports make it easier for stakeholders to understand the true financial health of a company, reducing the opportunities for earnings manipulation. Consistent application of accounting policies, on the other hand, enhances the reliability and comparability of financial statements, allowing users to better assess performance and make informed decisions. Both factors help ensure that the financial information presented is accurate and trustworthy. Conversely, performance reporting pressure and information asymmetry were found to have a negative impact on earnings quality. When companies face excessive pressure to meet performance targets, there is a higher likelihood of earnings manipulation through practices like income smoothing or accrual manipulation. Similarly, information asymmetry, where management possesses superior knowledge of the company's financial position compared to external stakeholders, creates a favorable environment for misleading financial reporting. This imbalance makes it more difficult for stakeholders to accurately assess a company's true financial condition. The combined effect of all variables on earnings quality underscores the importance of addressing multiple aspects of financial reporting. Improving earnings quality requires tackling not only transparency in reporting and consistency in accounting policies but also minimizing external pressures and reducing information asymmetry. Effective corporate governance plays a key role in ensuring the integrity of financial reporting by promoting accurate disclosures and reducing the likelihood of earnings manipulation. Future research could explore additional factors that influence earnings quality, such as managerial incentives, audit quality, or the impact of external market conditions. Alternative measures of earnings quality, including real earnings management or qualitative assessments, could also provide a deeper understanding of the factors influencing financial reporting. Expanding the analysis to include various industries and regions may improve the generalizability of these findings and offer further insights into how different factors shape earnings quality. Ultimately, improving earnings quality requires a holistic approach. Transparency, consistency in accounting practices, and strong governance mechanisms are essential for providing stakeholders with accurate and reliable financial information. Addressing these areas not only enhances earnings quality but also builds trust among investors, regulators, and other market participants, fostering a more efficient and stable financial environment.

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