Accounting Conservatism: Antecedents and Consequence in Indonesia Manufacturing Companies

JACOBUS WIDIATMOKO[1], MARIA GORETI KENTRIS INDARTI[2], CAHYANI NUSWANDARI[3]
[123]Accounting Department, Faculty of Economics and Business, Stikubank University
Kendeng Street V, Bendan Ngisor, Semarang 50233
INDONESIA
jwidiatmoko@edu.unisbank.ac.id; kentris@edu.unisbank.ac.id; cahyani@edu.unisbank.ac.id

Abstract: - The aim of this research is to test and analyze factors that affect accounting conservatism and its impacts on the cost of equity capital. The populations of this study are all manufacturing companies listed on the Indonesia Stock Exchange (IDX) in the 2018-2020 period. The sample was selected using purposive sampling technique and obtained 241 observations. Using the linear regression analysis technique, the results of this study indicate that institutional ownership and profitability significantly positively influence accounting conservatism. Three other factors, namely managerial ownership, investment opportunity set, and leverage have no influence on accounting conservatism. In advance, accounting conservatism significantly negatively affects the cost of equity capital. Thus, the higher the institutional ownership and profitability, the higher the accounting conservatism and the lower the cost of equity capital. The results of this study imply that institutional ownership as an implementation of corporate governance will encourage management to apply conservative accounting principles. Companies with higher levels of conservatism will receive a positive response from the market, which will result in a lower cost of equity capital required by investors.

Key-Words: - share ownership, company characteristics, accounting conservatism, cost of equity capital, IDX

1 Introduction

Currently, the quality of company financial information, especially earnings, is still the most critical economic problem in developing country capital markets. Accounting earnings provide essential information about company performance and are the leading indicator for users as a basis for decision-making [1], [2]. Therefore, quality earnings will have an impact on the quality and accuracy of decision-making [3]. One indicator of quality earnings is earnings resulting from a conservative accounting process. Accounting conservatism is defined as the tendency of accountants to require a higher level of verification to recognize good news than bad news in financial statements [4], [5]. Accounting conservatism is also interpreted as a level of caution in assessing uncertain conditions with the aim of assets or profits not being inflated and liabilities or expenses not being reported lower [6].

Conservatism is still a vital accounting principle in the earnings measurement process [7], although the precautionary principle is no longer an element of the relevance and reliability of accounting information. In conditions of uncertainty, conservatism becomes a concept of accounting measurement and valuation desired by users of financial information and becomes a tool to limit management's opportunistic behaviour. From an agency perspective, accounting conservatism can also be a tool for overcoming problems that arise between agents and principals [8]–[10]. Investors and potential investors will consider investing in companies with more caution. Therefore, management needs to maintain the principle of conservatism when presenting information to investors, mainly because future losses from overly optimistic forecasts are much more severe than missed profitable opportunities caused by adopting an overly pessimistic (conservative) approach [5].

Even though accounting conservatism is essential in realizing transparency and information disclosure, phenomena show that there are still companies in the world and Indonesia that still need to apply the conservatism principle. It can be seen that there are still irregularities in the financial statements made by the company. Based on information from the Association of Certified Fraud Examiners (ACFE, 2022) in Report to the Nations: a global study on occupational fraud and abuse, there are three primary categories. One of the three main categories is financial statement fraud by 10%, which contributed to the most significant loss of $ 954,000. The phenomenon of financial statement fraud also occurs in Indonesia. Based on the 2019 Indonesia Fraud Survey report, financial statement fraud in Indonesia reached 22 out of 50 cases of misuse of state & company assets or assets. The number of losses incurred was 242,260,000,000 out of a total loss of 873,430,000,000 or around 9.2%.

Based on the above phenomena, it is necessary to study the factors that influence the implementation of the conservatism principle. This study examines the determinants of accounting conservatism from the aspects of corporate governance and company characteristics. Strong corporate governance is vital in creating shareholder value and is a mechanism for aligning management, shareholder interests, and insider expropriation [11]. This study examines corporate governance from the perspective of share ownership, namely managerial and institutional ownership. In addition, this study examines the characteristics of the company as a determinant of accounting conservatism practices in a company.

Managerial ownership shows the proportion of shares owned by managers to the total number of shares outstanding. Managers with higher share ownership will tend to apply conservative accounting because they are agents and owners, so they will try to maintain the company's sustainability rather than just thinking about bonuses and compensation [12]. In line with this thought, Indarti et al's research [13] proves that managerial ownership has a positive effect on accounting conservatism in manufacturing companies in Indonesia. The same results were also reported by Putra et al. [14]. However, several studies report that there is no effect of managerial ownership on accounting conservatism [12], [15], [16].

Institutional investors as parties who monitor the company's running, play an essential role in the corporate governance system because they have a financial interest and independence to assess the company's management and policies unbiasedly. Consequently, institutional investors need timely and reliable information that enables them to monitor company activities better and participate in making business strategies [2], [17]. Such financial information can be obtained from more conservative financial reporting. Therefore, institutional investors tend to demand more conservative accounting from managers. Conservatism also limits management's opportunistic behaviour so that they prioritize shareholders' interests and increase the company's value. Research by Alkurdi et al. [9] and El-Haq et al. [18] proves that institutional ownership positively affects accounting conservatism. In contrast, research by Hakiki & Solikhah [15] and Asiriuwa et al. [16] shows that institutional ownership does not affect accounting conservatism. Meanwhile, El-habhasy's research [12] shows the negative effect of share ownership by institutional investors on accounting conservatism.

The investment opportunity set is a variable used to indicate a company's investment decision, which can affect the company's financial aspects such as the company's capital structure, debt contracts, dividend policies, compensation contracts, and company accounting policies. Companies with high investment opportunities have profitable prospects and investment opportunities in the future. These investment opportunities cause a positive reaction to stock prices which in turn impacts increasing company value, which also means that the company's market-to-book ratio as a proxy for conservatism is also getting bigger [19]. Research by El-Haq et al. [18] and Murwawingsari & Rachmawati [19] proves that the higher the investment opportunity set, the higher the level of accounting conservatism. However, the research results of Indarti et al. [13] and Hakiki & Solikhah [15] show that there is no effect of the investment opportunity set on accounting conservatism.

Companies with high levels of debt have a high risk of survival. As the owner of the funds, the creditor has the right to obtain information about the security of the funds lent in the hope that they will get more benefits in the future. The higher the level of leverage owned by the company, the higher the possibility of disputes arising between shareholders and owners of funds. To anticipate this, management will be encouraged to apply conservative accounting [20], [21]. Research by Salehi & Sahat [2] and Sugiarto & Fachrurrozie [22] proves that leverage positively affects accounting conservatism. On the other hand, Alkurdi el al. [9] reports that leverage has no effect on conservative accounting practices, while El-Habhasy [12] finds a negative effect between leverage and accounting conservatism.

Profitability is an indicator used by a company to show its ability to generate profits during a financial reporting period, a specific time, and to provide insight into the efficiency of its operations. Companies with higher profitability will face higher tax burdens. Therefore, management tends to apply accounting policies that produce smooth profits. This logic aligns with the findings of Asiriuwa et al. [16] and Solichah & Fachrurrozie [21], which show that profitability positively affects accounting conservatism. However, several studies have shown that profitability has no effect on accounting conservatism [9], [18]. Conversely, Abdurrahman & Ermawati [23] show that profitability significantly negatively affects conservative accounting practices.

Inconsistent research results as described above prompted researchers to review the factors that influence accounting conservatism. **This study examines** the effect of corporate governance and company characteristics on accounting conservatism. Corporate governance is proxied by share ownership by managers and institutions, while corporate characteristics include investment opportunity sets, leverage, and profitability. **The difference between this study and previous research** lies in testing the impact of accounting conservatism on the cost of equity capital. Research on the usefulness of accounting conservatism using the cost of equity capital as a benchmark in the Indonesian capital market still needs to be explored. Companies with a higher level of conservatism have higher earnings quality, so the return required by investors in the form of cost of equity capital tends to be low [10]. However, the findings of previous studies have shown mixed results. Khalifa et al. research [5] in 37 developing countries proves that accounting conservatism has a negative effect on the cost of equity capital. Several studies also reported the same results [10], [24]–[26]. Meanwhile, research by Goh et al. [27] shows a positive relationship between accounting conservatism and the cost of equity capital. This condition requires a more in-depth and comprehensive study of conservatism practices in Indonesia by involving the antecedents of accounting conservatism practices and examining their impact on the cost of equity capital. The findings of this study contribute to company management to reduce the cost of equity capital by applying accounting conservatism and good governance. In addition, the results of this study provide input to the Indonesian Institute of Accountants as a regulator of accounting policies in Indonesia that conservative accounting practices are important to implement considering that the principle of conservatism is no longer raised in the conceptual framework of accounting in Indonesia.

This manuscript is arranged systematically as follows. After outlining the introduction which contains the research motivation, relevant previous research, research objectives and research contributions in the first part, this paper describes the study of the literature and the development of hypotheses in the second part. The third part describes the research method. Furthermore, the fourth section contains data analysis and discussion of the results of hypothesis testing. This paper closes by presenting conclusions, limitations, and suggestions for future research.

2 Literature Review

From an agency relationship perspective, managerial ownership can help reduce agency costs by aligning the interests of managers and shareholders [17], [28]. Managerial ownership shows the proportion of shares owned by managers to the total number of shares outstanding. When managers act as shareholders, they will carry out their duties in the company's best interests [29]. This condition can reduce agency conflicts because managers who act as shareholders not only direct the company to large profits but are more concerned with the sustainability of the company. Therefore, management will tend to be careful by applying conservative accounting [12]. The higher the number of company shares owned by managers, the more conservative the financial reporting submitted by management. Several studies conducted in Indonesia prove that the higher the number of shares owned by management, the higher the level of accounting conservatism is applied [14], [29].

Conservatism is carried out to improve the quality of reported earnings information so that the market responds positively, thus increasing the market price of shares, ultimately increasing the company's value. The following hypothesis is formulated based on the logic of thought and empirical support above.

H1: Managerial ownership has a positive effect on accounting conservatism

Institutional share ownership can be a governance mechanism to increase transparency and reduce information asymmetry. Institution owners have great opportunities, resources, ability to control and limit manager behaviour [12]. Institutional shareholders will encourage and motivate the board of commissioners and the audit committee to carry out effective oversight of management to act prudently by applying conservative accounting principles. Effective oversight will minimize opportunistic actions taken by management so that it will benefit shareholders. Companies with high institutional ownership tend to have an effective and adequate external monitoring system and have the potential to increase conservatism practices [30]. Alkurdi's et al. [9] research on manufacturing and financial companies on the Amman stock exchange proves that the higher the number of shares owned by institutional investors, the higher the level of accounting conservatism. The same results were reported by El-Haq et al. [18], who researched companies owned by the government in Indonesia.

H2: Institutional ownership has a positive effect on accounting conservatism.

Agency relationship creates a conflict of interest between managers and shareholders who have different interests. Conservatism is one way to reduce agency conflicts caused by investment decisions [22]. An investment opportunity set is an investment opportunity owned by a company in the form of a combination of assets and becomes an investment option in the future [19], [31], [32]. Based on agency theory, investment opportunity sets can minimize problems that arise in agency relationships between management and principals through investment decisions by management [32]. Companies with high investment opportunity sets have high growth opportunities, so significant funds are needed to fund this growth. This large need for funds will encourage managers to apply the principle of conservatism in order to obtain funds from investors [18]. Research conducted by Murwaningsari and Rachmawati [19] proves that companies with high investment opportunities tend to apply conservative accounting principles. The same results were shown by El-haq et al. [18] who reported that the higher the opportunity for a company to grow, the more conservative management will be because conservative companies usually have hidden reserves that can be used to fund investments to create company growth. Based on this thought, the following hypothesis is formulated.

H3: Investment opportunity set has a positive effect on accounting conservatism

Agency theory states that managers and creditors have different interests, which causes agency costs to arise. The relationship between accounting conservatism and agency costs occurs because debt is used in the company's capital structure [2]. Companies with high levels of debt have a high risk of survival. This condition encourages creditors to carry out tighter supervision of the company's operations and accounting. Creditors have an interest in the security level of debt repayment that has been given to the company. Creditors are also interested in the distribution of net assets in the financing of assets granted and lower returns to managers and shareholders. Therefore, management must act more carefully by applying conservative accounting principles [22].

On the other hand, more conservative debtors will receive lower initial interest rates offered by creditors due to a breach of debt agreements and the consequent risk of default. This condition will encourage management to act conservatively to obtain low debt costs. Several studies prove that the higher the level of corporate debt, the more management will apply conservative accounting principles. For example, Alkurdi's et al. [9] research on manufacturing and financial companies in the Amman stock exchange shows that debt, as measured by leverage, positively affects accounting conservatism. The same results were shown by Salehi & Sehat [2] when accounting conservatism was measured using the Beaver & Ryan [33] model. In Indonesia, Sugiarto & Fachrurrozie [22] also proves that the higher the level of debt owned, the more conservative management will act. The following hypothesis is formulated based on the thoughts and empirical facts above.

H4: Leverage has a positive effect on accounting conservatism.

Financial statements are the primary information source for all parties interested in a company [21]. Profit is a component of financial statements that presents essential information for users and reflects management's success in managing the company so that profit becomes the basis for investors and potential investors in making investment decisions. However, companies with high-profit levels will face political costs, among others, in the form of a high tax burden that must be borne. Therefore, companies with high profitability tend to apply conservative accounting methods. This is in line with Asiriuwa's et al. [16] findings, which found a positive effect of profitability on accounting conservatism. Widaryanti (2022) reported [34][34](2022)the same results and tested the effect of profitability on accounting conservatism in manufacturing companies listed on the Indonesia Stock Exchange. Therefore, the higher the profitability of a company, management tends to choose conservative accounting policies. Based on the description above, the following research hypothesis is formulated.

H5: Profitability has a positive effect on accounting conservatism

Conservatism is generally defined as the level of caution in assessing uncertain conditions with the aim of assets or profits not being inflated and liabilities or expenses not being reported lower [6]. Accounting conservatism can be used as a tool to overcome agency problems that arise in the relationship between agents and principals. The commitment of managers to produce conservative accounting numbers allows investors to infer private information about the company's future prospects. With more information obtained, investors can correctly determine the company's value and thereby reduce their estimation risk, lowering the required rate of return. Investors in companies with a high level of conservatism will face lower risks, so the rate of return in the form of the cost of equity capital is also low [5], [35]. This is in line with Krismiaji and Astuti's research [10] which examined the effect of accounting conservatism on the cost of equity capital in manufacturing companies in Indonesia. The study results show that accounting conservatism companies apply will reduce the equity capital cost. The same findings were also reported by Goh et al. [27] and Li [24], which proved that accounting conservatism positively affects the cost of equity capital. Based on the description above, the hypothesis is formulated as follows.

H6: Accounting conservatism has a negative effect on the cost of equity capital

3 Methodology

The populations in this study are manufacturing companies listed on the Indonesia Stock Exchange (IDX) in 2018-2020. The research sample was selected using a purposive sampling method, with the following criteria: 1) the company publishes audited financial reports, and 2) it has complete data. Based on predetermined criteria, a total sample of 83 companies was obtained for each year or 249 data. After testing the normality of the residuals, there were 8 data outliers, so that the total number of final data processed in this study was 241. Research data were obtained from IDX Statistics (www.idx.com) and collected using the documentary method.

This study uses two dependent variables: accounting conservatism and the cost of equity capital. The independent variables consist of two groups: ownership structure, which includes managerial and institutional ownership, and company characteristics, which include investment opportunity sets, leverage, and profitability. Variable measurements are presented in Table 1.

Table 1. Variable Measurements

Variables	Measurements	References
CONACC	((Income before extraordinary + depreciation expense - net operating cash flow)/Total assets)) * -1	[32], [36], [37]
CEC	$r = \frac{B_t + X_{t+1} - P_t}{P_t}$ r: Cost of Equity Capital B_t: Book value per share in period t X_{t+1}: Earnings per share in period t+1 P_t: stock price in period t	[13], [37], [38]
MO	Number of shares owned by institutional investors/Number of outstanding shares	[29], [37]

IO	Number of shares owned by management/Number of outstanding shares	[39]
IOS	(BVFAt - BVFAt-1)/Total Assets. BVFAt: Book value of fixed assets in period t BVFAt-1: Book value of fixed assets in period t-1	[19]
Lev	Total debt/Total Assets	[13]
Prof	Earnings after tax/Total Assets	[37], [40]

The analysis technique used in this study is ordinary least square regression with path analysis. This study uses two models, namely Model 1 and Model 2. Model 1 examines the effect of ownership structure consisting of managerial and institutional ownership and company characteristics consisting of the investment opportunity set, leverage and profitability. The mathematical equation for the two models is stated as follows.

$$CONACC = \beta_0 + \beta_1 MO + \beta_2 IO + \beta_3 IOS_{it} + \beta_4 Lev + \beta_5 Prof + \varepsilon \quad \text{(Model 1)}$$

$$CEC = \gamma_0 + \gamma_1 CONACC + \varepsilon \quad \text{(Model 2)}$$

Information:

- CONACC : Accounting conservatism
- β_0 and γ_0 : Constant
- β_1 - β_5 and γ_1 : Coefficient
- MO : Managerial ownership
- IO : Institutional ownership
- IOS : Investment opportunity set
- Lev : Leverage
- Prof : Profitability
- CEC : Cost of equity capital
- ε : Error term

4 Results and Discussion

4.1 Descriptive Statistics

Table 2 presents descriptive statistics for all the variables used in this study. Based on the information in Table 2, it can be seen that management share ownership in manufacturing companies in Indonesia is relatively low, namely around 9.3%. On the other hand, institutional share ownership shows a relatively high figure, namely 47.7%. The manufacturing companies that are the sample of this study have relatively low growth opportunities, as indicated by the average IOS score of 4.67%. The average debt level of the sample companies is 53% of the total assets owned, and the profitability shows a relatively low figure of 3.94%. The average value of accounting conservatism is 0.016, indicating that the sample companies are relatively conservative. The average cost of equity capital is also low, namely -0.136. This condition is probably caused by the company's relatively high average conservatism level. This result can be interpreted that the average sample company demanding a relatively low return on investment from investors.

Table 2. Descriptive Statistics

Variables	N	Mean	Minimum	Maximum	Std. Deviation
MO	241	.093	.000	.732	.252
IO	241	.478	.001	.933	.288
IOS	241	4.675	-14.583	256.715	19.668
Lev	241	.534	.001	5.073	.563
Prof	241	.039	-.376	.466	.082
CONACC	241	.016	-.352	.264	.072
CEC	241	-.136	-37.034	4.604	2.555

Note: MO: managerial ownership, IO: institutional ownership, IOS: investment opportunity set, Lev: leverage, Prof: profitability, CONACC: accounting conservatism, CEC: cost of equity capital.

Tests for normality and classical assumptions are carried out as a condition for using ordinary least squares regression to test Model 1. The results of the residual normality test produce a skewness value of 0.239 with a standard error of 0.157. Based on these values, the z-skewness value is 1.522. This value is between -1.96 and 1.96, so the residuals in the regression model are normally distributed. The autocorrelation test showed that the Durbin-Watson value was 1.933, between the du value of 1.725 and the 4-du value of 2.275. Therefore, in the regression model, there is no autocorrelation problem. The results of the multicollinearity test, as presented in Table 4, show that all independent variables have a tolerance value above 0.10 and the variance inflation factor (VIF) value is less than ten, so the multicollinearity problem does not occur in the regression model. Finally, the results of the heteroscedasticity test using the Glejser test are presented in Table 3. Based on the information in Table 3, it can be seen that all variables are not significant at the 5% level, so there is no heteroscedasticity problem in the regression model.

Table 3. Heteroscedasticity Test Results of Model 1

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	.002	.001		1.937	.054
	MO	8.621E-5	.002	.003	.049	.961
	IO	.001	.002	.059	.886	.376
	IOS	-3.596E-7	.000	-.001	-.016	.987
	Lev	.002	.001	.133	1.974	.050
	Prof	.007	.005	.090	1.358	.176

Note: MO: managerial ownership, IO: institutional ownership, GO: IOS: investment opportunity set, Lev: leverage, Prof: profitability.

The results of the Model 1 test are presented in Table 4. Based on the adjusted R square value, it can be seen that 22.10% of the variation in accounting conservatism can be explained by the variables of managerial ownership (MO), institutional ownership (IO), investment opportunity set (IOS), leverage (Lev), and profitability (Prof). In comparison, variables outside the model explain the remaining 77.90%. Statistical F value shows the number 14.592, significant at the 1% level. These results indicate that the variables managerial ownership, institutional ownership, investment opportunity set, leverage, and profitability affect accounting conservatism, so the model is feasible.

Based on the information in Table 4, managerial ownership (MO) has a beta value of -0.026 with a significance level of 0.117, so the first hypothesis which states that managerial ownership has a positive effect on accounting conservatism is rejected. Based on agency theory, share ownership by management should be a mechanism for aligning the interests of management and shareholders [28]. However, empirical facts show that share ownership by management has no impact on accounting conservatism policies. This can happen because the average management share ownership in manufacturing companies in Indonesia is relatively low, and even some companies whose shares are not owned by management, so management is not motivated to apply the principle of accounting conservatism. Management who is not the owner of the company will tend to increase accounting profits to get bonuses, thereby ignoring the principle of accounting conservatism [12]. The findings of this study do not support agency theory which states that management ownership can be a mechanism for aligning conflicts of interest between management and principals. The results of this study contradict the findings of previous studies conducted by Putra et al. [14] and Indarti et al. [32], which prove that managerial ownership has a positive effect on accounting conservatism.

The beta coefficient on institutional ownership shows a number of 0.033 with a significant level of 0.024, so hypothesis 2 which states that institutional ownership positively affects accounting conservatism, is accepted. As expected, institutional ownership has a positive effect on accounting conservatism. The average share ownership by institutions in manufacturing companies in Indonesia is relatively high, so that institutional investors have an important role in enforcing corporate governance through supervision and monitoring of management. The findings of this study prove that institutional owners have carried out the supervisory and monitoring functions effectively, thereby limiting management from taking opportunistic actions such as earnings management and tending to apply the principle of accounting conservatism. This finding is in line with the results of the research reported by Alkurdi et al. [9], El-Haq et al. [18] and Putra et al. [14], which proves the positive effect of institutional share ownership on accounting conservatism. However, the findings of this study contradict the results of research by Hakiki & Solikhah [15], El-Habhasy [12] and Asiriuwa et al. [16] which show that institutional ownership has no effect on the practice of accounting conservatism by management.

The investment opportunity set variable has a beta coefficient of 0.000 with a significant level of 0.261, so the third hypothesis, which states that the investment opportunity set positively affects accounting conservatism, is rejected. The explanation that can be given is that investment opportunities in the future will affect the company's market performance so that management is encouraged to report its best results to shareholders without having to pay attention to the principle of conservatism in order to increase the value of the company. The average investment opportunity in sample companies is also relatively low and not optimal, which is indicated by a negative number in the descriptive statistics. This condition encourages management to apply aggressive accounting principles so that the performance looks good and the market responds positively. This study's results align with the research of Hakiki & Solikhah [15] and Indarti et al. [32] who reported that investment opportunities have no effect on accounting conservatism. On the contrary, the results of this study contradict Murwaningsari & Rachmawati [19] and El-Haq et al. [18] which prove that investment opportunities positively affect accounting conservatism.

Leverage has no effect on accounting conservatism, so the fifth hypothesis is rejected. The findings of this study do not support the agency theory, which states that when a company has a high level of leverage, creditors will tend to carry out strict monitoring so that management will choose conservative accounting policies. The companies that are the sample of this study have relatively high levels of leverage, so management tends to use aggressive accounting so that financial performance looks better. As a result, there is no need to renegotiate their debt contracts. The findings of this study are in line with the results of the research reported by Alkurdi et al. [9], Solichah & Fachrurrozie [21] and El-Habhasy [12], which show that leverage has no effect on accounting conservatism policies but does not support the research results of Sugiarto & Fachrurrozie [22] and Salehi & Sahat [2].

Table 4. Test Results of Model 1

Model	Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.	Collinearity Statistics Tolerance	Collinearity Statistics VIF
1 (Constant)	-.007	.010		-.655	.513		
MO	-.026	.017	-.092	-1.575	.117	.955	1.048
IO	.033	.015	.134	2.268	.024	.935	1.069
IOS	.000	.000	-.065	-1.126	.261	.986	1.014
Lev	-.006	.008	-.045	-.767	.444	.923	1.083
Prof	.390	.051	.447	7.662	.000	.952	1.050
Adjusted R Square							.221
F value							14.592
Sig.							.000

Note: MO: managerial ownership, IO: institutional ownership, IOS: investment opportunity set, Lev: leverage, Prof: profitability

As predicted, the profitability variable positively affects accounting conservatism, so the fourth hypothesis is accepted. Profitability shows the company's ability to generate profits. Therefore, companies that have a high level of profitability will tend to choose conservative accounting. This is because accounting conservatism can be used as part of earnings management by managers to manage earnings so that they look smooth and do not have too high fluctuations. In addition, the relationship between profitability and accounting conservatism is related to the political costs faced by companies. Companies with high profitability will generate high profits, so they will face high political costs such as large amounts of taxes to be paid. This causes companies with high profitability to prefer to apply conservative accounting to reduce the tax burden. The results of this study support the findings of previous research conducted by Asiriuwa et al. [16], which proved that profitability has a positive effect on accounting conservatism, but is not in line with the results of research conducted by El-haq et al.[18] and Alkurdi et al. [9] who reported that profitability does not affect accounting conservatism.

Model 2 examines the impact of accounting conservatism on the cost of equity capital.

Information in Table 5 shows that 7.4% of the variation in the cost of equity capital (CEC) can be explained by the accounting conservatism variable, while the remaining 92.6% is explained by other variables not included in the model. Statistical F value shows 13.373, significant at the 1% level. Therefore, model 2, which examines the impact of accounting conservatism on the cost of equity capital is feasible.

As presented, the accounting conservatism variable (CONACC) has a beta coefficient of -5.293 and a significance level of 0.000. Thus, the sixth hypothesis states that accounting conservatism has a negative effect on the cost of equity capital is accepted. The results of testing the sixth hypothesis indicate that accounting conservatism significantly affects the cost of equity capital. These results indicate that the more conservative management is in presenting its financial statements, the lower the rate of return demanded by investors. Requests for returns by investors are closely related to investors' perceptions of the risks that the company owns. Companies with higher levels of conservatism indicate that these companies present quality financial information to be seen as having low risk. This causes investors' demands for compensation for invested funds to decrease, which means that the cost of equity capital decreases.

The findings of this study support the agency theory which states that accounting conservatism can be used as a tool to overcome agency problems that arise in the relationship between agents and principals. The commitment of managers to produce conservative accounting numbers allows investors to determine the value of the company more precisely. This condition will reduce their estimation risk and lower the required rate of return in the form of cost of equity capital. The results of this study are consistent with the findings of Khalifa et al. [5] and Li [24], which show a negative relationship between accounting conservatism and the cost of equity capital. Krismiaji & Sururi's research [6] conducted on companies in Indonesia also showed the same results, the higher the level of accounting conservatism applied, the lower the cost of equity capital that the company must bear. However, the findings of this study contradict the results of a study by Goh et al. [27] who reported a positive relationship between accounting conservatism and the cost of equity capital.

Table 5. Test Results of Model 2

Model	Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1 (Constant)	.225	.078		2.900	.004
CONACC	-5.293	1.447	-0.284	-3.657	.000
Adjusted R Square					.074
F value					13.373
Sig.					.000

Note: CONACC: accounting conservatism

5. Conclusion

This study proved that institutional ownership and profitability have a significant positive effect on accounting conservatism. Meanwhile, managerial ownership, investment opportunity set, and leverage do not affect accounting conservatism. This study also proved that accounting conservatism has a significant adverse effect on the cost of equity capital. This study shows that managerial ownership can only sometimes minimize agency conflict. The results of this study give insight into making business decisions and provide input for the Indonesian Institute of Accountants to include the concept of conservatism in the conceptual framework of financial reporting.

Because of the relatively small adjusted R square (11.6%), future research should consider other elements of corporate governance e i., independent commissioners, audit committees, government ownership and foreign ownership. Future research can also examine corporate governance's direct and indirect effect on the cost of equity capital mediated by accounting conservatism.

Acknowledgement:

This research is supported by the Directorate of Research, Community Service and Publications, Universitas Stikubank, Semarang, Indonesia (Grant number: 062/J.09/UNISBANK/PN/XII/2021).

Competing Interests: The authors declare that they have no known competing interests.

Acknowledgement: The Director of Directorate of Research, Community Service and Publications, Universitas Stikubank, Semarang

References:

[1] S. Khajavi, M. H. G. Arani, and H. F. Nafchi, "Intellectual capital and earnings quality: a comprehensive investigation," *Int. J. Learn. Intellect. Cap.*, vol. 13, no. 4, pp. 316–337, 2016.

[2] M. Salehi and M. Sehat, "Debt maturity structure, institutional ownership and accounting conservatism," *Asian J. Account. Res.*, vol. 4, no. 1, pp. 35–51, Aug. 2019.

[3] C. J. Lin, T. Wang, and C. J. Pan, "Financial reporting quality and investment decisions for family firms," *Asia Pacific J. Manag.*, vol. 33, no. 2, pp. 499–532, 2016.

[4] S. Basu, "Discussion of International Differences in the Timeliness , Conservatism , and Classification of Earnings," *J. Account. Res.*, vol. 37, pp. 89–99, 1999.

[5] M. Khalifa, H. Zouaoui, H. Ben Othman, and K. Hussainey, "Exploring the nonlinear effect of conditional conservatism on the cost of equity capital: Evidence from emerging markets," *J. Int. Accounting, Audit. Tax.*, vol. 36, p. 100272, 2019.

[6] K. Krismiaji and S. Sururi, "Conservatism, Earnings Quality, and Stock Prices - Indonesian Evidence," *J. Account. Invest.*, vol. 22, no. 1, pp. 37–50, Jan. 2021.

[7] M. Soliman and A. A. Ragab, "Audit Committee Effectiveness, Audit Quality and Earnings Management: An Empirical Study of the Listed Companies in Egypt," *Res. J. Financ. Account.*, vol. 5, no. 2, pp. 155–166, 2014.

[8] H. Affes and H. Sardouk, "Accounting Conservatism and Corporate Performance: The Moderati ng Effect of the Board of Directors," *J. Bus. Financ. Aff.*, vol. 5, no. 2, 2016.

[9] A. Alkurdi, M. Al-Nimer, and M. Dabaghia, "Accounting conservatism and ownership structure effect: A look at industrial and financial jordanian listed companies," *J. Environ. Account. Manag.*, vol. 7, no. 2, pp. 608–619, 2017.

[10] K. Krismiaji and R. P. Astuti, "Accounting Conservatism and Cost of Equity Capital – Evidence from Indonesia," *CECCAR Bus. Rev.*, vol. 2, no. 2, pp. 64–72, Feb. 2021.

[11] P. K. Pham, J.-A. Suchard, and J. Zein, "Corporate Governance and the Cost of Capital: Evidence from Australian Companies," *J. Appl. Corp. Financ.*, vol. 24, no. 3, pp. 84–93, Sep. 2012.

[12] H. A. K. El-habashy, "The effect of corporate governance attributes on accounting conservatism in Egypt," *Acad. Account. Financ. Stud. J.*, vol. 23, no. 3, pp. 1–18, 2019.

[13] M. G. K. Indarti and J. Widiatmoko, "The Effects of Earnings Management and Audit Quality on Cost of Equity Capital: Empirical Evidence from Indonesia," *J. Asian Financ. Econ. Bus.*, vol. 8, no. 4, pp. 769–776, 2021.

[14] I. G. B. N. P. Putra, P. A. M. P. Sari, and G. D. Larasdiputra, "Pengaruh Kepemilikan Institusional Dan Kepemilikan Manajerial Pada Konservatisme Akuntansi," *Wacana Ekon. (Jurnal Ekon. Bisnis dan Akuntansi)*, vol. Vol.18, no. No.1, pp. 41–51, 2019.

[15] L. N. Hakiki and B. Solikhah, "Pengaruh Corporate Governance, Investment Opportunity Set, Ukuran Perusahaan, Dan Penerapan Psak 55 Terhadap Konservatisme Akuntansi," *Gorontalo Account. J.*, vol. 2, no. 2, p. 85, Oct. 2019.

[16] O. Asiriuwa *et al.*, "Ownerships Structures and Accounting Conservatism among Nigeria Listed Firms," *IOP Conf. Ser. Earth Environ. Sci.*, vol. 331, no. 1, pp. 1–15, 2019.

[17] S. Liu, "The impact of ownership structure on conditional and unconditional conservatism in

China: Some new evidence," *J. Int. Accounting, Audit. Tax.*, vol. 34, pp. 49–68, 2019.

[18] Z. N. S. El-haq, Z. Zulpahmi, and S. Sumardi, "Pengaruh Kepemilikan Manajerial, Kepemilikan Institusional, Growth Opportunities, Dan Profitabilitas Terhadap Konservatisme Akuntansi," *J. ASET (Akuntansi Riset)*, vol. 11, no. 2, pp. 315–328, 2019.

[19] E. Murwaningsari and S. Rachmawati, "The Influence of Capital Intensity and Investment Opportunity Set toward Conservatism with Managerial Ownership as Moderating Variable," *J. Adv. Manag. Sci.*, vol. 5, no. 6, pp. 445–451, 2017.

[20] A. S. Ahmed and S. Duellman, "Accounting conservatism and board of director characteristics: An empirical analysis," *J. Account. Econ.*, vol. 43, no. 2–3, pp. 411–437, 2007.

[21] N. Solichah and Fachrurrozie, "Effect of Managerial Ownership, Leverage, Firm Size and Profitability on Accounting Conservatism," *Account. Anal. J.*, vol. 8, no. 3, pp. 151–157, 2019.

[22] V. H. S. Sugiarto and F. Fachrurrozie, "The Determinant of Accounting Conservatism on Manufacturing Companies in Indonesia," *Account. Anal. J.*, vol. 7, no. 1, pp. 1–9, 2018.

[23] M. A. Abdurrahman and W. J. Ermawati, "Pengaruh Leverage, Financial Distress dan Profitabilitas terhadap Konservatisme Akuntansi pada Perusahaan Pertambangan di Indonesia Tahun 2013-2017," *J. Manaj. dan Organ.*, vol. 9, no. 3, pp. 164–173, 2019.

[24] X. Li, "Accounting Conservatism and the Cost of Capital: An International Analysis," *J. Bus. Financ. Account.*, vol. 42, no. 5–6, pp. 555–582, Jun. 2015.

[25] K. Krismiaji and A. Raharja, "Corporate governance, accounting information quality, and cost of equity capital an Indonesia' evidence," *J. Akunt. Audit. Indones.*, vol. 22, no. 1, pp. 1–11, 2018.

[26] O. Andellsi and M. Afriyenty, "Pengaruh Konservatisme Akuntansi Terhadap Biaya Ekuitas Dan Peran Komite Audit Sebagai Moderasi," *J. Eksplor. Akunt.*, vol. 2, no. 2, pp. 2659–2672, 2020.

[27] B. W. Goh, C. Y. Lim, G. J. Lobo, and Y. H. Tong, "Conditional Conservatism and Debt versus Equity Financing," *Contemp. Account. Res.*, vol. 34, no. 1, pp. 216–251, Mar. 2017.

[28] M. C. Jensen and W. H. Meckling, "Theory of The Firm: Managerial Behavior, Agency Cost and Ownership Structure," *J. financ. econ.*, vol. 3, no. 4, pp. 305–360, 1976.

[29] M. G. K. Indarti, J. Widiatmoko, and I. D. Pamungkas, "Corporate Governance Structures and Probability of Financial Distress: Evidence From Indonesia Manufacturing Companies," *Int. J. Financ. Res.*, vol. 12, no. 1, pp. 174–183, Dec. 2021.

[30] N. W. Rustiarini, A. W. S. Gama, and D. N. S. Werastuti, "Board of Director Characteristics, Institutional Ownership, and Accounting Conservatism," *Indones. J. Account. Res.*, vol. 24, no. 02, pp. 289–320, May 2021.

[31] S. C. Myers, "Determinants of corporate borrowing," *J. financ. econ.*, vol. 5, no. 2, pp. 147–175, Nov. 1977.

[32] M. G. K. Indarti, J. Widiatmoko, A. Badjuri, and T. Ambarwati, "Determinan Konservatisme Akuntansi: Studi Empiris pada Perusahaan Manufaktur di Bursa Efek Indonesia," *J. Akunt. Indones.*, vol. 10, no. 2, pp. 161–174, Apr. 2021.

[33] W. H. Beaver and S. G. Ryan, "Biases and Lags in Book Value and Their Effects on the Ability of the Book-to-Market Ratio to Predict Book Return on Equity," *J. Account. Res.*, vol. 38, no. 1, p. 127, 2000.

[34] W. Widaryanti, "The Effect Of Managerial Ownership, Institutional Ownership, Growth Opportunity And Profitability On Accounting Conservatism," *Governors*, vol. 1, no. 1, pp. 1–7, 2022.

[35] R. Lambert, C. Leuz, and R. E. Verrecchia, "Accounting information, disclosure, and the cost of capital," *J. Account. Res.*, vol. 45, no. 2, pp. 385–420, 2007.

[36] D. Givoly and C. Hayn, "The Changing Time-Series Properties of Earnings, Cash Flows and Accruals," *J. Account. Econ.*, vol.

29, pp. 287–320, 2000.

[37] J. Widiatmoko, M. G. K. Indarti, and C. A. Agustin, “Corporate Governance, Growth Opportunities dan Konservatisme Akuntansi: Bukti Empirik pada Perusahaan Manufaktur di Bursa Efek Indonesia,” *J. Akunt. Bisnis*, vol. 18, no. 2, pp. 236–249, 2020.

[38] J. A. Ohlson, “Earnings, Book Values, and Dividends in Equity Valuation,” *Contemp. Account. Res.*, vol. 11, no. 2, pp. 661–687, 1995.

[39] M. G. K. Indarti, T. Taswan, B. D. Bagana, and A. Janah, “Corporate Governance Mechanism on Intellectual Capital Disclosure and Firm Value,” in *Proceedings of the 3rd International Conference on Banking, Accounting, Management and Economics (ICOBAME 2020)*, 2020, vol. 169, no. Icobame 2020, pp. 400–404.

[40] J. Widiatmoko and M. G. K. Indarti, “Karateristik Perusahaan, Tipe Auditor dan Konsentrasi Kepemilikan Saham terhadap Pengungkapan Modal Intelektual,” *J. Bisnis dan Ekon.*, vol. 25, no. 1, pp. 35–46, 2018.

Contribution of Individual Authors to the Creation of a Scientific Article (Ghostwriting Policy)

Jacobus Widiatmoko produces Ideas and Novelty as well as making research concepts

Maria Goreti Kentris Indarti has implemented theory and discussion as well as the optimization.

Cahyani Nuswandari was tabulating and processing data and management references.

5107-2235_Revised_Final140523.docx

ORIGINALITY REPORT

20%	20%	19%	8%
SIMILARITY INDEX	INTERNET SOURCES	PUBLICATIONS	STUDENT PAPERS

PRIMARY SOURCES

1	koreascience.or.kr Internet Source	3%
2	journal.umy.ac.id Internet Source	2%
3	www.hkjoss.com Internet Source	2%
4	coek.info Internet Source	2%
5	Maria Goreti Kentris Indarti, Jacobus Widiatmoko, Imang Dapit Pamungkas. "Corporate Governance Structures and Probability of Financial Distress: Evidence From Indonesia Manufacturing Companies", International Journal of Financial Research, 2020 Publication	1%
6	journal.unnes.ac.id Internet Source	1%
7	repository.uhamka.ac.id Internet Source	1%

8	lib.unnes.ac.id Internet Source	1%
9	Novi Ayu Arthasari, Agustina Ratna Dwiati. "Effect of Managerial Ownership, Audit Committee, Profitability and Leverage on Accounting Conservatism", JAE (JURNAL AKUNTANSI DAN EKONOMI), 2022 Publication	1%
10	Listyorini Wahyu Widati, Bambang Sudiyatno, Titiek Suwarti, Kis Indriyaningrum. "An Empirical Study of the Impact of Accounting Conservatism and Ownership Structure on Firm Performance in Indonesia", Business Perspectives and Research, 2023 Publication	1%
11	Sun Liu. "The impact of ownership structure on conditional and unconditional conservatism in China: Some new evidence", Journal of International Accounting, Auditing and Taxation, 2019 Publication	1%
12	repository.ubharajaya.ac.id Internet Source	1%
13	www.econstor.eu Internet Source	1%
14	Maha Khalifa, Hakim Ben Othman. "The effect of conservatism on cost of capital: MENA	1%

evidence", Applied Economics, 2014
Publication

15 jurnal.itscience.org
Internet Source
1%

16 repository.unibos.ac.id
Internet Source
1%

17 Ain Hajawiyah, Agus Wahyudin, Kiswanto, Sakinah, Indra Pahala. "The effect of good corporate governance mechanisms on accounting conservatism with leverage as a moderating variable", Cogent Business & Management, 2020
Publication
1%

18 jurnal.ugm.ac.id
Internet Source
1%

19 Mukhammad Idrus, Siti Fatimah, Afiah Mukhtar, Karta Negara Salam. "Examining the Factors Affecting Accounting Prudence", ATESTASI : Jurnal Ilmiah Akuntansi, 2022
Publication
1%

Exclude quotes	On	Exclude matches	< 1%
Exclude bibliography	On		