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Research Article

The Role of Financial Structure and Ownership in Determining Accounting Conservatism: A Study on Leverage, Managerial Ownership, and Financial Distress Factors

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Abstract

This study aims to explore the impact of leverage, managerial ownership, and financial distress on the decision to adopt accounting conservatism in manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the period from 2013 to 2017. Leverage is assessed through the Debt-to-Equity Ratio (DER), managerial ownership is evaluated using the managerial ownership ratio (MOR), financial distress is measured by the Altman Z-score, and accounting conservatism is indicated by CONACCit. This research utilizes a quantitative approach and a purposive sampling technique, resulting in a sample of 20 companies, relying on secondary data sourced from financial reports available on the official IDX website. Data analysis is conducted using multiple linear regression. The findings reveal that leverage, managerial ownership, and financial distress significantly affect accounting conservatism. The managerial implications of these results highlight the necessity for management to maintain a prudent capital structure, promote managerial ownership to enhance accountability, and adopt accounting conservatism as a strategy for addressing financial risks and preserving stakeholder trust. From an Islamic perspective, the implementation of accounting conservatism aligns with the principle of prudence, which is essential for maintaining trust, ensuring transparency, and safeguarding the interests of all stakeholders involved.

Keywords: Leverage, Managerial Ownership, Financial Distress, Accounting Conservatism

JEL Classification: G30, G32, G33, M41,

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1. Introduction

Companies create financial reports to illustrate management's performance in managing their resources. Financial reports are the end product of a company's accounting processes and activities. These reports provide information that can be used by internal parties, such as commissioners, directors, managers, and employees, as well as external parties, including investors, creditors, and suppliers, to inform their decisions and actions. Internal decisions include, for example, the decision to reappoint or replace management. External decisions include, for example, the decision to hold or sell their investments in the company, or the decision to extend a certain amount of credit to the company (Deviyanti, 2012).

Bahaudin & Provita (2011) note that for management, Generally Accepted Accounting Principles (GAAP) provide flexibility in determining the accounting methods and estimates that can be used. This flexibility will influence managers' behavior in recording and reporting the company's financial statements. In times of uncertainty, managers should apply conservative accounting principles to ensure accurate financial reporting. Several researchers have noted an increase in the conservatism of accounting standards globally.

Ramadhoni (2014) states that when a company applies the principle of conservatism, it must acknowledge losses that are highly likely to occur, but must not anticipate profits that have not yet occurred. This will result in low profits and assets, as well as high costs and liabilities. Consequently, profits are understated. Meanwhile, according to Nugroho (2012), creditors urge companies to present conservative financial statements to neutralize those that are overly optimistic in their reporting. Therefore, the application of the principle of conservatism can protect creditors from overstated profits, and this principle can reduce conflicts between management and shareholders over the implemented dividend policy.

While some accept the concept of conservatism, others reject it, arguing that financial statements presented using the principle of conservatism will result in biased financial statements, making them unsuitable for evaluating corporate risk (Nugroho, 2012). When a company experiences increased investment, conservative financial statements will yield lower profits than those that do not apply this principle. Conservative principles will also create unrecorded reserves, allowing management to report future profits freely. Consequently, the financial statements presented are of little value because they do not accurately reflect the company's actual value or performance.

Despite the debate, conservative accounting principles continue to be in use. The reason this principle is still used is that the tendency to overstate earnings in financial reporting can be reduced by adopting a pessimistic attitude to balance managers' excessive optimism. Furthermore, overstating earnings is more dangerous than understating earnings because the risk of lawsuits is greater when presenting financial reports with significantly higher profits than actual earnings (Noviantari & Ratnadi, 2015).

A vast body of literature reveals several factors contributing to accounting conservatism. The first factor that can influence accounting conservatism is leverage. Leverage is a ratio that indicates the extent to which debt or equity is used to finance a company's assets. According to agency theory, an agency relationship exists between managers and creditors. Managers seeking credit will consider the leverage ratio (Dwijayanti, 2010).

The third factor: Financial difficulties experienced by companies can lead to layoffs of employees. The threat of layoffs is currently occurring in the textile and textile products (TPT) industry, which employs hundreds of thousands of workers. According to Franky Sibarani, Head of the Investment Coordinating Board (BKPM), 17 TPT companies have reported their difficulties. Financial difficulties are one of the sources of the problems faced by these 17 textile and textile product industries (Djumena, 2016).

When a company experiences financial difficulties, it is crucial to present accurate and transparent financial statements. The measurement of assets, liabilities, equity, revenue, and expenses must comply with generally accepted accounting principles (Aristiyani & Wirawati, 2013). These accounting principles include accrual accounting, materiality, conservatism, and others. Compared to other principles, conservatism is crucial and is often referred to as the dominant accounting principle when preparing financial statements.

2. Literature Review and Hypothesis

Accounting conservatism

Harahap (2011) states that when a company is faced with choosing between two or more equally acceptable accounting principles or techniques, it should prioritize the option that has the least positive impact on owners' equity. Companies should report assets and revenues at the lowest value, and liabilities and expenses at the highest value. This can be achieved by recognizing potential losses and not recognizing unrealized profits.

Leverage

Sudana (2009) states that publicly traded companies are inextricably linked to debt, which can be used to expand their businesses through extensification and intensification. Debt used to expand a company's size can be obtained from creditors such as banks or other lending institutions. Leverage is quite important in determining a company's capital structure. Leverage arises because the company is financed with funds that incur fixed costs, namely, debt with fixed costs in the form of interest.

Managerial Ownership

Kusumawardhani (2012) states that managerial ownership is the percentage of shares owned by management. Management refers to the company's administrators, including directors, managers, and employees. Management ownership is a mechanism that enables managers to carry out activities in the company's best interests, given the presence of personal management ownership in the company's shareholding. Management ownership is a mechanism that enables managers to carry out activities in the company's best interests, given the presence of personal management ownership in the company's shareholding.

Financial Difficulties

Ramadhoni (2014) defines financial distress as the emergence of early signs or symptoms of bankruptcy, indicating a decline in a company's financial condition, or even conditions that occur before bankruptcy or liquidation. These signs can include a decline in company profits, receiving a debt collection letter from the bank due to failure to pay bills (obligations) on time, the company being unable to pay its debts as they fall due, and the company being insolvent, where the book value of debt is greater than the book value of assets.

Research Conceptual Framework

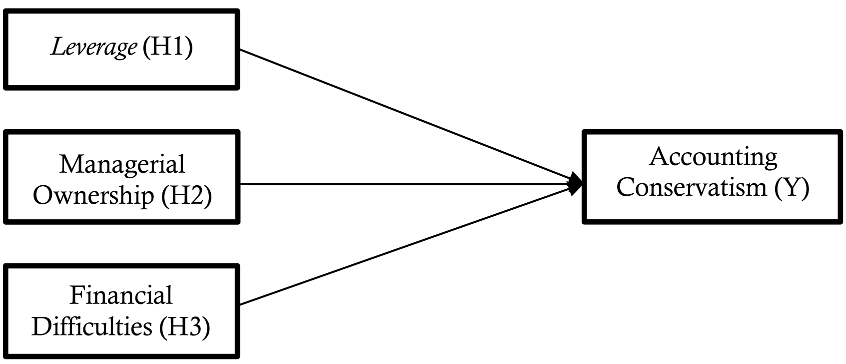

Figure 1. Research Concept Framework

The Effect of Leverage on Accounting Conservatism
High leverage indicates the extent to which a company borrows capital to finance its assets. The higher this ratio, the greater the financial risk for both creditors and shareholders. Leverage is considered profitable if a company can generate profits that exceed its fixed costs (bond interest and constant preferred stock dividends). Therefore, companies with high debt will choose to implement conservative accounting. Leverage has a significant positive effect on accounting conservatism. The results of this study align with previous findings, where Alhayati (2013), Suryanawa (2014), Yuliarti & Yanto (2017), and Rahayu et al. (2018) all demonstrated that leverage has a positive effect on accounting conservatism. According to them, high leverage will result in greater financial obligations that the company must meet. This will facilitate the increased implementation of conservative accounting, as it reduces agency conflicts that arise between shareholders and bondholders.
H1: Leverage Has a Positive Effect on Accounting Conservatism

The Influence of Managerial Ownership on Accounting Conservatism
The influence of managerial ownership affects the level of accounting conservatism. If the level of managerial ownership increases, it indicates that management will also increase its control or monitoring of financial reporting rights, thereby improving the quality of financial reporting. Consequently, management will likely suppress or increase the principle of higher accounting conservatism. Managerial share ownership (board of commissioners and directors) in this study was measured by calculating the percentage of shares owned by managers divided by the total number of shares outstanding. Hypothesis testing regarding the influence of managerial ownership variables on accounting conservatism. Research conducted by Septian and Ana (2014) shows that managerial ownership has a positive effect on accounting conservatism. According to them, managers are not only concerned with high profits reported in financial statements, but also with the desire to expand the company. Therefore, if managers maintain conservative accounting practices, they will have substantial cash reserves that the company can use to expand.
H2: Managerial Ownership affects Accounting Conservatism

The Impact of Financial Distress on Accounting Conservatism
Financial distress is a condition in which a company experiences negative net income for two or more consecutive years. Predicting companies experiencing financial distress (which then goes bankrupt) is an important analysis for interested parties such as creditors, investors, regulatory authorities, auditors, and management. For creditors, this analysis is a primary consideration in deciding whether to call in their receivables, increase receivables to overcome these difficulties, or take other policies. The results of this study are supported by research conducted by Pramudita (2012), which found that financial difficulties have a positive effect on accounting conservatism. This finding is inconsistent with research conducted by Alhayati (2013), which found that financial difficulties do not have a significant effect on accounting conservatism.
H3: Financial difficulties have an impact on accounting conservatism.

3. Data and Method

Types of Research Data
Based on the title and problem formulation, this research is quantitative in nature. Data sources include primary and secondary data. The primary data source was obtained from the official website of the Indonesia Stock Exchange (www.idx.co.id) in the form of company financial reports. The documentation method was used in this study, collecting data from the financial reports of manufacturing companies listed on the IDX.

Population and Sample
The population in this study is manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the period 2013-2017. Several samples will be taken from this population. The researcher used purposive sampling. The criteria used for selecting the sample were manufacturing companies listed on the IDX and those that consistently published complete, audited financial reports consecutively from 2013 to 2017.

4. Results

Normality Test Results

Table 1. Normality Test Results: Kolmogorov-Smirnov Test

One-Sample Kolmogorov-Smirnov Test

		Unstandardized Residual
N		100
Normal Parameters a,b	Mean	,0000000
	Standard Deviation	,07197482
Most Extreme Differences	Absolute	,046
	Positive	,034
	Negative	-,046
Test Statistics		,046
Asymp. Sig. (2-tailed)		,200c,d

Source: Processed Data (2019)

The Table above shows a Kolmogorov-Smirnov significance value of 0.200, greater than 0.05. This indicates that the residual data is usually distributed, thus fulfilling the classical regression assumptions.

Multicollinearity Test Results

Table 2. Multicollinearity Test Results

Coefficientsa

Model		Collinearity Statistics	
		Tolerance	VIF
1	(Constant)		
	H1	,994	1,006
	H2	,999	1,001
	H3	,994	1,006

Source: Processed Data (2019)

Based on the Table above, it can be concluded that the independent variables above do not experience multicollinearity because the tolerance value is greater than 0.10.

Autocorrelation Test Results

Table 3. Autocorrelation Test Results

Runs Test

	Unstandardized Residual
Test Value	-,00150
Cases < Test Value	50
Cases >= Test Value	50
Total Cases	100
Number of Runs	44
Z	-1,407

Source: Processed Data (2019)

Based on the Table above, the results of the autocorrelation test show that Asymp. Sig. (2-tailed) 0.159, which indicates more than 0.05, which means H0 is accepted, so it is concluded that the residuals are random or there is no autocorrelation between the residual values.

Heteroscedasticity Test Results

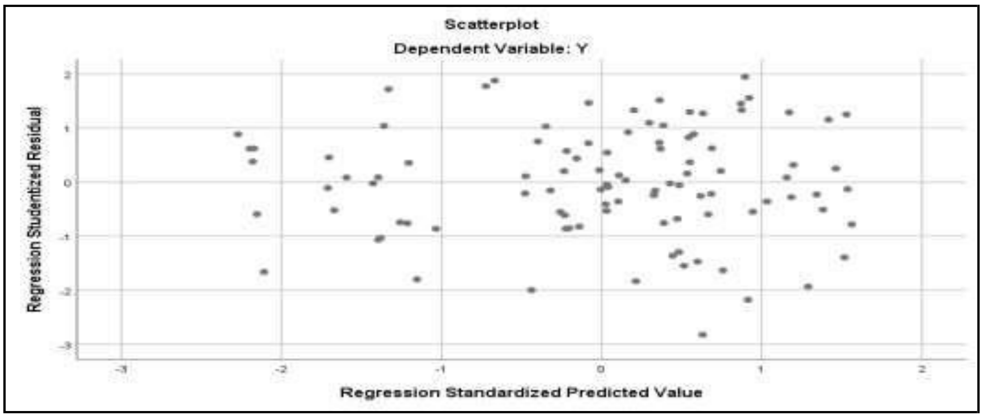

Figure 2. Heteroscedasticity Test Results: Scatterplot Graph

The figure above shows that the sample data (dots) are spread above and below the zero point (0) on the Y-axis, indicating that there is no heteroscedasticity in this study. Based on this, the regression model is suitable for further hypothesis testing.

Hypothesis Testing

Table 4. t-Test Results

Coefficientsa

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	22,524	,032		714,312	,000
	H1	,036	,004	,202	10,236	,000
	H2	,143	,003	,957	48,657	,000
	H3	,040	,024	,032	16,637	,000

Source: Processed Data (2019)

Based on the Table above, all independent variables are proven to have a significant effect on accounting conservatism. The leverage variable has a t-value of 10.236 > 1.984 with a significance of 0.000 < 0.05, so that H1 is accepted. The managerial ownership variable also has a significant effect with a t-value of 48.657 > 1.984 and a significance of 0.000 < 0.05, so that H2 is accepted. Similarly, the financial distress variable shows a t-value of 16.637 > 1.984 with a significance of 0.000 < 0.05, so that H3 is accepted. This suggests that leverage, managerial ownership, and financial distress all have a substantial impact on accounting conservatism.

Coefficient Test Results: Determination (R2)

Table 4. Results of the Determination Coefficient (R2) Test

Model Summary

Model	R	R Square	Adjusted R Square	Standard Error of the Estimate
1	,981a	,963	,962	,07309

Source: Processed Data (2019)

Based on the Table above, the coefficient of determination (R^2) test yields an adjusted R-squared value of 0.963, which is close to 1. This indicates that 96.3% of the independent variables — namely, leverage, managerial ownership, and financial distress — provide almost all the information needed to predict the variation in the dependent variable, namely accounting conservatism. Meanwhile, 3.7% of the variation in the dependent variable is explained by other variables not included in this study.

5. Discussion

The Effect of Leverage on Conservatism.

Based on Table 3, it can be interpreted that leverage has a positive and significant effect on accounting conservatism. The first hypothesis is accepted, which states that leverage has an impact on accounting conservatism. This result indicates that the higher the debt value, the greater the accounting conservatism, as the company is unable to guarantee its debts with its own capital, and thus becomes increasingly hesitant in determining profits. The results of this study are consistent with those of Alhayati (2013), Dewi & Suryanawa (2014), and Rahayu et al. (2018), which have shown that leverage has a positive effect on accounting conservatism. However, these results are inconsistent with Pramudita (2012), who found that leverage did not affect accounting conservatism.

The Influence of Managerial Ownership on Conservatism

Based on Table 3, managerial ownership has a positive and significant effect on accounting conservatism. The second hypothesis is accepted, which states that managerial ownership influences the level of accounting conservatism. The results indicate that an increase in managerial ownership is associated with greater accounting conservatism within the company. This means that managers are not only concerned with profits to expand the company, but also with ensuring that the company's operations are sustainable. Therefore, managers implement conservative accounting. With managerial ownership, the company will have a substantial reserve of funds to use for expansion. This research aligns with Dewi (2014), who found that managerial ownership has a positive effect on accounting conservatism, whereas Apriani (2015) stated that managerial ownership has no effect.

The effect of financial distress on accounting conservatism

Based on Table 3, it can be interpreted that financial difficulties have a positive and significant effect on accounting conservatism. The third hypothesis is accepted, which states that managerial ownership has an impact on accounting conservatism. This result suggests that adverse financial conditions can prompt managers to reduce the level of accounting conservatism, although shareholders and creditors typically require conservative accounting practices. This research aligns with the findings of Pramudita (2012), who reported that financial difficulties have a positive effect on accounting conservatism. This research result is inconsistent with that of Alhayati (2013), which found that financial difficulties do not have a significant effect on accounting conservatism.

6. Conclusion

Based on the results of research and discussion regarding the influence of leverage, managerial ownership and financial difficulties on the decision to apply accounting conservatism in manufacturing companies listed on the IDX, the following conclusions were obtained: The leverage variable has a significant positive effect on the decision to apply accounting conservatism, Managerial Ownership has a significant positive effect on the decision to apply accounting conservatism, Financial Difficulties have a significant positive effect on the application of accounting conservatism.

Managerial Implications

This research suggests that manufacturing companies listed on the IDX should adopt accounting conservatism by considering leverage, managerial ownership, and financial distress. High leverage demands caution in reporting, while managerial ownership encourages managers to be more responsible in maintaining report quality. Financial distress, on the other hand, requires a conservative approach to maintain stakeholder trust.

Recommendation

Manufacturing companies listed on the IDX are advised to manage leverage optimally, increase managerial ownership to strengthen accountability, and consistently implement accounting conservatism as a strategy to mitigate the risk of financial distress and maintain stakeholder trust.

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