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CONSERVATIVE ACCOUNTING MEASUREMENTS FROM THE PERSPECTIVE OF ACCOUNT IN FINANCIAL STATEMENT

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ABSTRACT

The purpose of this paper is to determine the implementation of conservative accounting from the perspective of financial statements which include tax incentives, debt contracts, and political costs as research variables in manufacturing companies. The research population is the manufacturing sector listed on the Indonesia Stock Exchange with a total of 178 companies and a purposive sample obtained by 78 companies with data collection techniques using documentation. Multivariate regression techniques is the analytical tool used, and the results obtained indicate that tax incentives have a significant positive effect on conservative accounting. By contrast, debt contracts and political costs have no significant effect on conservative accounting. This paper provides encouragement to investors when evaluating financial statement changes related to conservatism, especially those relating to tax incentive accounts, debt covenant, and political costs.

Keywords: Tax Incentive, Debt Covenant, Political Cost, Conservative Accounting

ABSTRAK

Tujuan penelitian ini adalah untuk mengetahui implementasi akuntansi konservatif dari perspektif laporan keuangan yang mencakup insentif pajak, kontrak hutang, dan biaya politik sebagai variabel penelitian pada perusahaan manufaktur. Populasi penelitian adalah sektor manufaktur yang terdaftar di Bursa Efek Indonesia sejumlah 178 perusahaan dan sample berdasarkan purposive diperoleh 78 perusahaan dengan teknik pengumpulan data menggunakan dokumentasi. Multivariat regresi adalah alat analisa yang digunakan, dan hasil yang didapat menunjukkan bahwa insentif pajak berpengaruh positif signifikan terhadap akuntansi konservatif. Sedangkan kontrak hutang dan biaya politik tidak berpengaruh signifikan terhadap akuntansi konservatif. Penelitian ini memberikan implikasi bagi para investor ketika mengevaluasi perubahan laporan keuangan yang berkaitan dengan konservatisme, khususnya yang berkaitan dengan akun insentif pajak, kontrak hutang, dan biaya politik.

Kata Kunci: Insentif Pajak, Kontrak Hutang, Biaya Politik, Akuntansi Konservatif



Introduction

The information presented in financial reports reflects the entity's performance which is needed by interested parties, both internal and external. For internal parties, financial reports function as a tool for decision making, and for external parties as material for evaluating company performance and measuring investment risks or estimating profits for the coming year. So that in presenting it, company managers must apply the precautionary principle, namely that financial reports must contain truthful values in fundamental quality, including the elements: relevance, comparability, timeliness and verifiability (Handojo, 2012).

The correctness of the value of financial statements is related to the application of conservative accounting principles, the implementation of the accrual system causes the value presented in the financial statements to not only be the real value of financial transactions (both incoming and outgoing transactions), but also includes recordings that result in the possibility of receiving and disbursing cash in next time. The uncertainty of cash that will be received or disbursed in the future is what causes the implementation of conservative accounting (Hejranijamil et al., 2020). Accounting conservatism in the financial reports presented also has an impact on the valuation of stock market value (Jiménez-Angueira et al., 2021).

The application of accounting conservatism still raises debates about the pros and cons, critics admit that conservatism creates ambiguity in financial reports, namely that financial reports do not reflect relevant or actual conditions, where the quality of reported profits can be lower than it should be. (Kimouche, 2021; Millah et al., 2020). However, the International Financial Reporting Standards (IFRS) conference stated that the relevant values that are still required in reporting, including the fair value of assets, are not conservatism but contracting efficiency and are considered legal in presenting financial information. (Sebrina & Taqwa, 2019), Similar research regarding relevant values in financial reports based on mandatory IFRS was also carried out by (Manawadu et al., 2019; Manganaris et al., 2016) which states that relevant values that reflect the implementation of conservatism are more often carried out by corporations with high operation enforcement, in line with research Zhang et al. (2019) which shows that the sensitivity of executive compensation has an effect on financial report conservatism, good corporate governance mechanisms which include an independent board of commissioners have a positive effect on conservatism, but conversely managerial ownership and audit committees have a negative effect on conservatism (Nasr & Ntim, 2018).

Several other important factors that can also give rise to the implementation of conservatism in the presentation of financial statements, include tax incentives, where tax reduction

facilities that can be utilized by companies can reduce conservatism in financial statements (Fadhillah, 2022). This conservative principle in presenting financial statements can also be used to benefit the company's tax obligations (Jiménez-Angueira et al., 2021). Tax is an obligation for corporations, which in its implementation is imposed on the value of earnings reported in the financial statements so that tax can be a consideration for being conservative, but with tax incentives or facilities from the government, conservative principles can be avoided.

Salehi & Sehat, (2019) in his research using the conservatism model of Basu (1997) and the model of Ryan (2000) stated that long-term and short-term debt structures have no effect on the implementation of conservatism in companies. In contrast to the research of Makni Fourati et al. (2020) who believes that the capital structure, namely debt contracts, influences conservatism, determining debt contracts in financial reports really requires good governance. Debt contracts do not always trigger accounting conservatism because debt contracts with good governance will provide benefits for the company. A debt contract is an agreement between the issuer and the creditor, where the creditor measures the company's ability to pay based on the asset value presented in the financial statements. Meanwhile (Anantavasilp et al., 2021) argue that capital structure gives rise to conservative behavior, where shareholders encourage conservative behavior compared to debtholders. Shareholders have an interest in the earnings value presented in the financial statements, but debtholders have a contract that remains in accordance with the issuer's agreement regarding the interest costs that must be paid.

Mohammed et al., (2017) stated the results of his research that political connection was a negative moderating variable between the board of commissioners and conservatism, the board of commissioners had a positive effect on conservatism, but managerial ownership had a negative effect. Large company sizes have greater political costs and managers will be more conservative in presenting financial information (Ahmed & Hussainey, 2017). Several research results show that political costs depend on the size of the company and are a factor in conservatism, both negative and positive (still inconsistent).

Conservative principles with relevant values that are still within the IFRS corridor are often found in reports published by issuers in the capital market. Financial reports are a tool for investors to see the company's overall proforma. One of the pro forma companies that investors prefer is the manufacturing sector because this sector promises quite promising benefits in the future and is expansive. This is supported by data from the Ministry of Industry which shows that investment in this sector has increased continuously, in 2022 cumulatively, the manufacturing sector will contribute domestic and foreign investment of 23.8 percent and 53.4 percent (kemenperin.go.id). This condition reflects that published

financial reports are a very fundamental tool for investors. And companies can consider these interests with the principle of conservatism in presenting financial reports required by stakeholders.

The various empirics described above still show inconsistencies in research results, the determination of the conservatism factor is still interesting to re-examine in current research with the variables of tax incentives, debt covenants, and political costs. Based on this explanation, the aim of this research is: to determine the determinants of conservative accounting factors from a financial reporting perspective which include: tax incentives, debt covenants and political costs, so that a hypothesis can be formulated that refers to several empirical and corporate phenomena in the property sector, namely as follows. Following :

H1: Tax incentives are thought to have an impact on the application of conservative accounting in the financial statements of manufacturing companies

H2: Debt covenants are thought to have an impact on the application of conservative accounting in manufacturing companies' financial reports

H3: Political costs are thought to have an impact on the application of conservative accounting in the financial statements of manufacturing companies

Method

This research is quantitative in nature, the data used is secondary data from manufacturing sector financial reports published on the Indonesia Stock Exchange, with a total sample of 78 companies analyzed, the sample was selected purposively according to the needs of the research variables (Ferdinand, 2014 : 179). The operational definition of the variables in this research is :

Conservative accounting

This research refers to the concept of Basu (1997) and Ryan (2000), which measures conservatism with the ratio of book value and stock market value (Salehi & Sehat, 2019), book value is the recorded equity value divided by the number of outstanding shares, market value is the share price listed on the capital market which is determined by market players:

$$CON = \frac{\text{Book Value of Shares outstanding}}{\text{Market Value of Shares outstanding}} \times (-1) \dots \dots \dots (1)$$

Tax Incentive

Tax incentives are benefits that can be utilized by entities as a form of tax aggressiveness that is still permitted, for example through tax avoidance, namely tax planning by considering cost components such as depreciation costs and other operational costs that

are still relevant to the tax system as a deduction from the tax that will be paid. (Mohan et al., 2017) :

$$\text{UnTaxBenefit} = \frac{\text{Income Tax Rate} \times (\text{Earning before Tax} - \text{Current Tax Equipment})}{\text{Total Asset}} \dots\dots\dots(2)$$

Debt Covenant

The debt contract is the ratio of the amount of debt to the value of the assets owned by the company, assets are the value that can be used as collateral or protection from congestion or the risk of default. Debt contracts in this study refer to Anantavrasilp et al. (2021) which is formulated:

$$\text{Debt to Asset Ratio} = \frac{\text{Total Debt}}{\text{Total Asset}} \dots\dots\dots(3)$$

Political cost

Political costs arising from companies are based on the company's interests which are indirectly related to the practice of manipulating the presentation of financial reports within reasonable levels or limits aimed at various interested parties, namely stake holders, the larger the company will have greater political costs than companies that small, the size of the company can be proxied by the value of the assets owned (Mohammed et al., 2017) and formulated:

$$\text{Political Cost} = \text{Ln Total Asset} \dots\dots\dots(3)$$

Multivariate Analysis

To test the conservatism factors, multivariate analysis with multiple regression is used which can show the relationship between the dependent variable and the independent variable, and is formulated as follows:

$$\text{Conservatism} = \beta_0 + \beta_1 \text{UnTax benefit} + \beta_2 \text{Debt Covenant} + \beta_3 \text{Political Cost} + e \dots\dots\dots(4)$$

Where conservatism is the ratio of book value to stock market value, UnTax Benefit is a tax incentive or is a tax aggressiveness using a tax burden that is still relevant to the tax system. Debt Covenant is a debt contract that is proxied by the ratio of total debt to total assets, and political costs are costs based on the size of the company's level of interest related to stake holders..

Result and Discussion

Descriptive Statistics

This research uses panel data which is a combination of cross section and time series data (during the research period), namely 2020 to 2021. Next, analysis is carried out using a multivariate analysis tool with the aim of measuring the influence of tax incentives, debt

covenants and political costs as variables. independent of accounting conservatism as the dependent variable.

Before testing the model according to the proposed hypothesis, each variable is described first to find out the minimum, maximum and average values, which are presented in table 1.

Table 1 : Descriptive Statistics

Variables	Mean	Minimum	Maximum	SD
Tax Incentives	0,130	0,000	0,312	0,0270
Debt Covenant	0,4058	0,116	0,790	0,1672
Political Cost	28,75	25,32	32,83	1,598
Conservatism	0,084	-0,632	0,280	0,1201

Notes : This table presents statistical information according to sample data of 78 companies during the 2020-2021 period. The values listed in the table include the average, minimum, maximum and standard deviation values for each variable analyzed.

Data Source: Data Processed 2023

Based on the data presented in table 1, it shows that tax incentives have a minimum value of 0.000, a maximum value of 0.312 with a deviation level of 0.0270 and an average of 0.130. The average value is not too far from the maximum value, indicating that the sample of manufacturing sector companies used is taking advantage of tax incentives with a nominal value that is not much different. The average debt covenant value obtained is 0.4058 with a maximum value of 0.790 and a deviation level of 0.1672, indicating that the majority of companies have debt contracts more than the minimum value of 0.116. Furthermore, political costs show a minimum value of 25.32 with an average of 28.75, which indicates that the political costs used by the company have a range that is not too different with a deviation of 1,598. and conservative accounting shows a deviation value that is greater than the average value of 0.084, indicating that the distribution of conservatism values is spread evenly because the average value is not much different from the maximum value of 0.280.

Furthermore, before the data was analyzed using multiple regression, classical assumptions were tested first, which included a data normality test, obtained a Kolmogorov Smirnov value of 0.092 with a significance of 0.066, which was declared to meet the normality requirements because the significance level was greater than 0.05. The multicollinearity test of the independent variables shows that a value of more than 1 and less than 10 is declared free from multicollinearity. The autocorrelation test in this study used a run test and obtained a result of 0.093 with a significance of 0.098 greater than 0.05 and was declared to meet the autocorrelation free requirements. The Spearman rho test was used to detect heteroscedasticity and the results obtained for all independent variables were more than 0.05, which means they were free from autocorrelation. The classical

assumption test has been fulfilled and the multiple regression test is continued to prove the proposed hypothesis.

Test the hypothesis of determining the conservatism factor in the manufacturing sector using multiple regression at a significance level of 0.05 with the results stated in table 2 below:

Table 2 : Multiple regression

Model		Coefficient ^a				
		Unstandardized Coefficients		Standardized Coefficients	t	Sig
		B	Std. Error	Beta		
1	(Constant)	-,619	,225		-,971	,334
	Tax Incentives	-1,212	,472	-,273	-2,566	,012
	Debt Covenant	-,033	,073	-,047	-,448	,355
	Political Cost	,010	,008	,129	1,223	,225

a. Dependent Variable: Konservatisme Akuntansi

Data Source: Data Processed 2023

The output of the test results in table 2 above produces a regression analysis formula for the three variables as determinant factors as follows:

$$\text{Conservatism} = -0,619 - 1,212 \text{ Untax benefit} - 0,033 \text{ Debt Covenant} + ,010 \text{ Political Cost} + e$$

The effect of tax incentives on accounting conservatism

Based on this formula, it can be stated that the regression coefficient value is -1.212 with a calculated t value of -2.566 which is greater than -1.975 at a significance of 0.012 which is smaller than 0.05 and it can be concluded that tax incentives have a significant negative effect on conservatism, which means that hypothesis 1 is accepted. The higher the utilization of tax incentives in the form of tax reductions, the lower the principle of conservatism applied. This is in line with research (Fadhillah, 2022) and as long as it is in accordance with the relevant values in IFRS, conservatism is still permitted (Sebrina & Taqwa, 2019). The Indonesian government's policy of reducing corporate tax rates as stated in Perpu Number 1 of 2020 concerning PPh Article 25 of 2020, in article 5 paragraph 1, in the Perpu states that the adjustment of income tax rates for domestic corporate taxpayers and permanent business forms from The previous rate of 25% has become 22% which applies to the 2020 and 2021 tax years. With the tax incentive policy in Indonesia itself, it encourages industry not to apply conservative principles in presenting financial reports because this policy provides direct corporate benefits, this is also in line with with previous research examining tax planning factors against the principle of conservatism, tax planning can reduce the conservatism attitude of managers' behavior in presenting financial reports (Jiménez-Angueira et al., 2021).

The influence of debt covenants on accounting conservatism

Testing the second hypothesis shows that the independent variable debt covenant has a regression coefficient of -0.033 with a calculated t value of -0.448 which is smaller than the t table -1.975 and a significance of 0.665 which is greater than 0.05 so it is stated that Hypothesis 2 is rejected. So, it can be concluded that debt covenants have no effect on accounting conservatism. The results of this research are different from previous findings which argued that debt structures encourage conservatism behavior (Salehi & Sehat, 2019), The debt structure can result in an increase in costs that must be borne by the corporation, this will pose a big risk for the company in a declining business proforma. These large cost burdens and fixed costs give rise to the cost behavior (Cost stickiness) of managers, and this cost behavior triggers the principle of conservatism (Makni Fourati et al., 2020). Penman & Zhang (2020) gave a different opinion regarding debt covenants, where the results of his research stated that the debt structure was not the main factor determining conservatism, but the cost of capital was actually an important factor in the principle of conservatism.

The influence of political costs on accounting conservatism

The results of the statistical tests in table 2 show that the political cost variable has a regression coefficient value of 0.10 with a t-value of 1.223 which is smaller than the t table of 1.975 and a significance value of 0.655 which is greater than 0.05, thus the third hypothesis (H3) is not accepted. This shows that political costs in manufacturing companies in Indonesia in 2020-2021 have no effect on accounting conservatism. Political costs, which are proxied by company size using total assets, show that the size of the assets owned by the company does not encourage the principle of conservatism. Conservative behavior is more inclined to the uncertain external environment than to the value of the wealth owned, this uncertain condition allows managers to behave conservatively (Hejranijamil et al., 2020), Similar things were also found in the results of research from (Majeed et al., 2017) which states that conservatism tends more towards the intensity of competition as stated in IFRS. Mohammed et al. (2017) who in his research believes that political costs arise because of the political connection of directors in decision making, and in this case directors will be able to behave conservatively, this is also supported by research (Zhang et al., 2019) who in his research stated that executive compensation is positively correlated with conservatism and company performance.

Conclusion

The research results state that tax incentives can reduce conservative behavior in presenting financial reports, while debt covenants and political costs do not encourage conservative behavior. In accordance with several previous empirics, the conservative behavior of managers is not only triggered by internal factors but also the company's external environment, for example government policies and business competition which have an impact on the strategies set. The research results have implications for the development of knowledge in the field of financial accounting, especially regarding the influence of tax incentives, debt covenants and political costs on accounting conservatism. Meanwhile, the practical implications for companies are that tax incentive policies can provide benefits for companies, especially related to planning taxes that will be paid in the next period and related to the financial pro forma that must be presented by the company to meet the needs of stake holders.

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