

THE EFFECT OF INDEPENDENT COMMISSIONERS, MANAGERIAL OWNERSHIP, AND AUDIT COMMITTEE ON ACCOUNTING CONSERVATISM

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ABSTRACT

This study aims to examine the influence of independent commissioner, managerial ownership, and audit committee on the accounting conservatism. The accounting conservatism is measured by accrual measurement. The population of this study is manufacturing's companies listed on Indonesia Stock Exchange in 2012-2015. Based on purposive sampling method, the total obtained sample is 508 companies.

The source of data is taken from annual reports of companies listed on Indonesia Stock Exchange in 2012-2015. The data analysis method is using multiple linear regressions with SPSS 22 software application. The result of this study found that managerial ownership has significant negative effect on the accounting conservatism, while the variables of independent commissioner and audit committee have no significant effect on the accounting conservatism.

Keywords : Accounting conservatism, accrual measurement, corporate governance, independent commissioner, managerial ownership, and audit committee.

A. INTRODUCTION

Financial report of a company reflects performance of the company during a period. According to PSAK No. 1 (Revision 2009), financial report is a structured presentation of financial position and financial performance of an entity. Financial report is made based on Standard Akuntansi Keuangan – Financial Accounting Standard (SAK – FAS) in order to produce helpful information for financial report users in decision making. SAK gives freedom to choose accounting method used in financial report making. The freedom in choosing this method can be used to produce different financial reports in each company. The choice of accounting method will affect the number presented in financial report. In the means to perfect financial report of a company, the concept of conservatism was born (Sari and Adhariani, 2009).

Accounting conservatism is a precautionary principle that delays income disclosure and accelerates cost disclosure, so it will produce numbers of income and assets that tend to be low, and numbers of cost that tend to be high. Therefore, financial report will produce earnings that are too low (Wulandini and Zulaikha, 2012). Conservative accounting can protect the interest of minority shareholders by limiting management power. With the presence of accounting conservatism, it is expected to reduce management ability in manipulating financial data and reducing agency cost (Ji, *et al.*, 2016). Moreover, conservatism can play important role in reducing uncertainty and information asymmetry among stakeholders (LaFond and Watts, 2008 in Cheng and Kung, 2016)

One case of financial reporting fraud happened in Indonesia was the case of PT. Kimia Farma, Tbk, where there was recording error of net profit in the financial report in 2001. The net profit that should be Rp 99 billions, was recorded Rp 132 billions. It indicates the low conservatism level applied by the company in preparing financial report and the lack of good corporate governance implementation. Many factors determine the level of conservatism in financial reporting of a company. This study

takes some factors that affect accounting conservatism which are independent commissioners, managerial ownership, and audit committee.

The proportion of independent commissioners needs to be noticed, so there is independency in the process of monitoring toward management performance of a company. The existence of independent commissioners will create monitoring done by board of commissioners more stringent, so it will require conservative accounting to avoid opportunistic attitude of manager. Moreover, managerial ownership (shareholding by commissioners and directors) can play the role as the monitoring function on the process of corporate financial reporting. If the monitoring is done well, it will require highly qualified information in order to apply more conservative accounting. Audit committee also plays role in managing a company because it is in charge to ensure that the company has applied accounting principle that is commonly applied on its financial reporting. Based on the background, the formulated research questions are: (i) do independent commissioners affect accounting conservatism? (ii) Does managerial ownership affect accounting conservatism? (iii) Does audit committee affect accounting conservatism?

The objectives of this study are: (i) investigating that independent commissioners affect accounting conservatism; (ii) investigating that managerial ownership affects accounting conservatism; (iii) investigating audit committee affects accounting conservatism. The advantage of this study for the development of science is expected to give contribution for academics in developing research in the future, and can be a reference on accounting conservatism implementation. Meanwhile, for practitioners, this study can give information on accounting conservatism implementation that is applied by company.

B. THEORETICAL FRAMEWORK AND HYPOTHESIS DEVELOPMENT

1. Agency Theory

Wulandini and Zulaikha (2012) defined agency relationship as a contract where one or more persons (principals) involve other person (agent) to conduct some service or activities on behalf of their names who delegate authority of decision making. Agent is given authority by owner to conduct operational activity of company, so the agent has

more information compared to the principal. According to agency theory, the agent must act rationally for the interest of principal. In its practice, conflict occurs because there is gap of interest between shareholders as the owner of company and the management as the agent. The conflict will create agency cost that eventually will be incentive to reduce it (Oktomegah, 2012).

2. Accounting Conservatism

Accounting conservatism is a relevant characteristic in financial accounting because it has effect on accounting practice in a quite long time. Accounting conservatism is a precautionary principle in facing uncertainty attached in the company to ensure that the uncertainty and risk in business environment is adequately considered. Accounting conservatism is defined as a standard use that is more precise to disclose bad news as loss and to disclose good news as profit in facilitating efficient contract between manager and shareholders (LaFond and Roychowdhury, 2007)

Some accounting methods in Financial Accounting Standard Statement (FASS) giving opportunity to manager for conducting conservative accounting among others are: FASS Number of 14 about supply and the choice in counting supply cost, FASS Number of 16 about fixed assets and the choice in counting its depreciation cost, FASS Number of 19 about intangible assets and the choice in counting its amortization, and FASS Number of 20 about research and development cost. Accounting method choices in Financial Accounting Standard (FAS) will affect the numbers presented in corporate financial report.

3. Corporate Governance

According to Forum for Corporate Governance in Indonesia (FCGI), corporate governance is a set of rules that defines the relationship between shareholders, manager, creditor, government, employees, and other external and internal shareholders related to their rights and responsibilities, or a system where company is directed and controlled. Kaihatu (2006) stated that there are five basic principles from corporate governance, which are: (i) transparency (information disclosure); accountability; responsibility; independency; fairness (equality and reasonableness).

4. Independent Commissioner

Independent commissioner is a party that is not affiliated with controlling shareholders, board of director member, and other board of commissioners both in the form of business relationship and family relationship. One main function of independent commissioner is to run monitoring function that is independent on corporate management performance. The presence of commissioners can balance the power of management (especially CEO) in managing company through its monitoring function (Wardhani, 2008). Indonesia Stock Exchange (IDX) in the regulation of Effect Recording No 1-A Nomor Keputusan I-A Kep-00001/BEI/01-2014 about Stock Recording and Non-Stock Equity Effect, states the regulation of the number of independent commissioners at least 30% (thirty percent) from all number of commissioner members.

The presence of independent commissioner in a company is very important. Fitriani (2014) proved that independent commissioner significantly affects accounting conservatism. The result is consistent with the study of Pratanda and Kusmuriyanto (2014) showing that there is significant effect between independent commissioners on accounting conservatism.

The higher proportion of independent commissioner toward total board of commissioners, the higher level of accounting conservatism. It is because the more number of independent commissioners in company create the monitoring on corporate performance is stronger. Based on the above explanation, the writer formulates hypothesis as the following:

H1: Independent commissioner positively affects accounting conservatism.

5. Managerial Ownership

Managerial ownership is the number of shares owned by management (commissioner, director, and employee) in company from all outstanding shares. Jensen and Meckling (1976) in Wardhani (2008) formed a theory stating that shareholding by management will reduce agency problem because the more shares owned by management, the stronger their motivation to work in increasing corporate share value.

The study done by Brilianti (2013) showed that managerial ownership negatively affects the level of accounting conservatism. It is in line with the study of Veres (2013) finding that managerial ownership negatively affects accounting conservatism. The presence of commissioner tendency with high shareholder to use lower conservatism is to avoid the decrease of share rate. Moreover, accounting conservatism in corporate financial reporting is one mechanism in overcoming agency problem when there is separation between ownership and controlling. The smaller managerial ownership, the agency problem appearing will be bigger so that the demand on conservative reporting will be more increasing. Based on the above explanation, the hypothesis is formulated as following:

H2: Managerial ownership negatively affects accounting conservatism

6. Audit Committee

Audit committee in charge in helping board of commissioners to ensure that financial report is presented reasonably in accordance with accounting principle that is generally applied, implementation internal ad external audit is conducted in accordance with applicable audit standard, and audit result finding follow up done by management (Wardhani, 2008). The size of audit committee is explained in Financial Service Authority Regulation - Peraturan Otoritas Jasa Keuangan Nomor 55/POJK.04/2015 about Formation and Guidelines of Audit Committee Implementation written in Chapter 4 that audit committee consists at least three members, which are independent commissioner who is also as the chief of audit committee and the party outside of the issuer or public company.

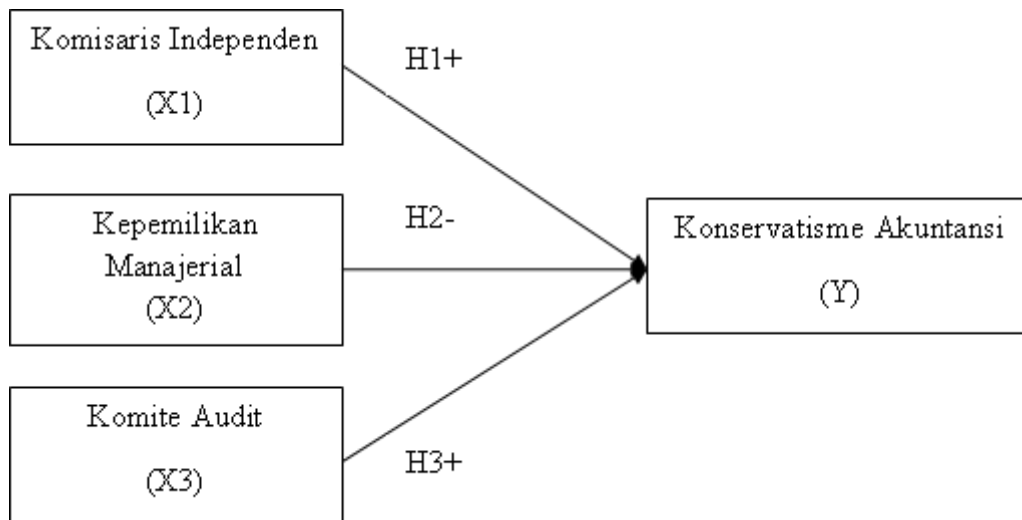
The study of Wardhani (2008) gave evidence that the presence of audit committee positively and significantly affects conservatism level by using accrual size. This result is consistent with the study done by Fitriani (2012) showing that audit committee significantly affects accounting conservatism. The presence of audit committee will ensure that company applies accounting principles that will produce accurate and qualified financial information of company through the use of high conservatism principle in the process of company's financial reporting. Based on the explanation, hypothesis formulated is as the following:

H3: Audit Committee positively affects accounting conservatism

7. Framework

The model in this study is as the following:

Figure 1
Framework



Note: Independent Commissioner (X1), Managerial Ownership (X2), Audit Committee (X3), Accounting Conservatism (Y)

C. RESEARCH METHODOLOGY

1. Type and Source of Data

Type of data used in this study is secondary data. Secondary data are the data obtained through available sources without being collected by the writer. Secondary data in this study are annual reports of companies downloaded through the website of Indonesia Stock Exchange (IDX).

2. Population and Sample

Population used in this study is manufacturing companies listed on Indonesia Stock Exchange in 2012-2015. Sampling method uses purposive sampling that is

chosen based on certain criteria. The criteria of sample in this study are as the following:

1. Manufacturing companies listed on Indonesia Stock Exchange (IDX) in 2012-2015.
2. Companies present annual reports during the observation period.
3. There is data completeness needed during the observation period.

3. Operational Definition of Research Variables

Variables in this study consist of 1 dependent variable and 3 independent variables.

a. Dependent Variable

Dependent variable is the variable affected by independent variable. Dependent variable in this study is accounting conservatism measured using accrual size in accordance with the one used by Givoly and Hayn (2002) in Sari and Adhariani (2009). The formula of conservatism is:

$$\text{CONACC}_{it} = \frac{(\text{NI} + \text{Dep})_{it} - \text{CFO}_{it}}{\text{TA}_{it}}$$

Explanation:

CONACC_{it} : conservatism level of company i in year t

$\text{NI} + \text{Dep}_{it}$: net income added by depreciation and amortization of company i in year t

CFO_{it} : cash flow from operational activity of company i in year t

TA_{it} : total assests of company i in year t

Givoly and Hayn (2002) stated that company that applies conservatism is shown when net income produced is positive and lower than operation cash flow that is consistent for some years. It means that the company suspends unrealized income more and charges cost more quickly. In this study, the value used as the proxy of conservatism level is net income value added by depreciation reduced by operational cash flow divided by total assets. The result of CONACC calculation above is

multiplied by -1, so the higher accounting conservatism is shown by the higher score of CONACC.

b. Independent Variable

Independent variable is a type of variable that explains or affects other variables. Independent variables in this study are:

- Independent Commissioner

The measurement of this independent variable is obtained by adding up independent commissioner then divided by total number of commissioners (Pratanda and Kusmuriyanto, 2014). The information about the number of independent commissioners is obtained from annual report of company and from the announcement issued by IDX.

KOM_INDP = the number of independent commissioners / total board of commissioners

- Managerial Ownership

Managerial ownership is proxied by the number of shares owned by management (commissioner, director, and employee) divided by the number of outstanding shares (Veres, 2013).

KEP_MNJ = the number of shares owned by management / the number of outstanding shares

- Audit Committee

Variable of audit committee in this study is measured by calculating the number of members in audit committee (Fitriani, 2014).

4. Data Analysis Method

Hypothesis testing uses multiple regression analysis. Data are processed using SPSS 22 software application. Multiple regression model in this study is as the following:

$$\text{CONACC} = \beta_0 + \beta_1\text{KOM_INDP} + \beta_2\text{KEP_MNJ} + \beta_3\text{UKA} + \varepsilon$$

Explanation:

CONACC	: Accounting conservatism level
KOM_INDP	: Proportion of independent commissioner
KEP_MNJ	: Percentage of shareholding by management
UKA	: The number audit committee
β_0	: Constant

D. ANALYSIS AND DISCUSSION

1. Description of Research Object

Population in this study is manufacturing companies listed on Indonesia Stock Exchange (IDX) during the period of 2012 to 2015. The total manufacturing companies listed on IDX during the observation period is 540 companies. Based on purposive sampling method, the obtained research sample is 508 companies.

2. Descriptive Statistics

Table 1
Descriptive Statistics

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
CONACC	508	-.521161	1.269171	-.01306550	.112809205
KOM_INDP	508	.2000	.8000	.393953	.0916203
KEP_MNJ	508	.000000	.739138	.03099301	.100663698
UKA	508	2	5	3.06	.375
Valid N (listwise)	508				

Source: Processed secondary data (2017)

Variable of accounting conservatism (CONACC) has the lowest value of -0,5211 owned by PT Sekawan Intipratama Tbk in 2013. Meanwhile, the highest value of 1.2691 is owned by PT Karwell Indonesia Tbk in 2015.

Variable of independent commissioner (KOM_INDP) has the lowest value of 0.2 and the highest value of 0.8 with standard deviation of 0.09. Variable of managerial ownership (KEP_MNJ) has the lowest value of 0.0000 and the highest value of 0.7391 with standard deviation of 0.1006. Variable of audit committee has the lowest value of 2 and the highest value of 5 with standard deviation 0.375.

3. Classic Assumption Test

In data processing, the data that are not distributed normally are found, so the tester conducts transformation on variable of independent commissioner (KOM_INDP) and variable of audit committee (UKA) in to natural logarithm form (Ln). Next, the writer detected the presence of outlier data in this study. After outlier is done from 508 research samples, there are 44 data that are stated as outlier data, so they must be eliminated from the research sample. The total research sample became 464 samples.

Normality test with non-parametric statistics test of Kolmogorov-Smirnow (Uji K-S) shows the value of Asymp.Sig. (2-tailed) of 0.054 meaning that the data are normally distributed. Multicollinearity test shows that all independent variables have tolerance value that is bigger than 0.1 and VIF value that is smaller than 10 meaning that there is no multicollinearity. Heteroscedasticity test with scatterplot graph shows that heteroscedasticity does not occur. Autocorrelation test with Durbin Watson test shows DW value of 1.994 and upper limit value (du) of 1.857, so autocorrelation does not occur in linear regression model.

4. Hypothesis Test

a. Determination Coefficient

Table 2
The Result of Determination Coefficient Test

Model Summary^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.156 ^a	.024	.018	.077421994

Source: Processed secondary data (2017)

The value of adjusted R Square is 0.018 meaning that 1.8% of accounting conservatism is affected by variables of independent commissioner, managerial

ownership, and audit committee, while the rest of 98.2% is affected by other variables that are not investigated in this study.

b. Feasibility Test of Regression Model (F Statistics Test)

Table 3
The Result of F Statistics Test

ANOVA^a

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	.069	3	.023	3.833	.010 ^b
Residual	2.757	460	.006		
Total	2.826	463			

Source: Processed secondary data (2017)

On Table 3, it is seen that the value of sig. (0.010) < from α (alfa) = 0.05 meaning that H_a is accepted, so it can be concluded that regression model used is “fit” and feasible to be continued to hypothesis test.

c. T statistics test

Table 3
The Result of t Statistics Test

Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	.119	.059		2.034	.043
LnKOM_INDP	.031	.019	.075	1.619	.106
KEP_MNJ	-.151	.070	-.101	-2.164	.031
LnUKA	-.094	.049	-.088	-1.902	.058

Source: Processed secondary data (2017)

The testing result shows that variable of independent commissioner does not significantly affect accounting conservatism. The result that is not significant shows that independent commissioner has not been optimal in conducting monitoring toward management, so it allows resulted financial report to be not conservative. Moreover, in the research sample, there are 17 companies that have not fulfilled the regulation of IDX

stating that the number of independent commissioners at least 30% (thirty percent) from all number of commissioner members. The result of this study is consistent with the study of Wulandini and Zulaikha (2012) demonstrating that the proportion of independent commissioners does not significantly relates to accounting conservatism.

Variable of managerial ownership negatively and significantly affects accounting conservatism. Accounting conservatism in corporate financial reporting is one mechanism in overcoming agency problem when there is a separation between ownership and controlling. Therefore, the bigger managerial ownership, the smaller agency problem that will appear, so the request on conservative reporting will be lower or becoming not conservative. The result of this study is consistent with the study of Brilianti (2013) showing that managerial ownership negatively affects accounting conservatism.

Variable of audit committee does not significantly affect accounting conservatism. The result that is not significant is because the competency of audit committee member is from different background that is from other fields then accounting such as law, engineering, finance, and management, so the monitoring on company's accounting is less optimal, and produced financial report tends to be not conservative. It is proven on the companies as the research sample that there are only 42% of audit committee members who are from accounting. The result of this study is in line with the study from Brilianti (2013) showing that audit committee does not affect accounting conservatism.

E. CONCLUSION AND SUGGESTION

1. Conclusion

This study aims to examine the effect of independent commissioner, managerial ownership, and audit committee on accounting conservatism. This study uses sample on manufacturing companies listed on Indonesia Stock Exchange (IDX) during the period of 2012-2015. Accounting conservatism is measured using accrual measurement used by Givoly and Hayn (2002) in Sari and Adhariani (2009). Based on the statistic testing result using multiple regression analysis, it can be concluded that only variable of managerial ownership that negatively significantly affects accounting conservatism,

while variables of independent commissioner and audit committee do not significantly affect accounting conservatism.

2. Suggestion

Based on the study result, there are some suggestions that can be considered for the next study, which are:

1. Using wider sample, not only limited to one type of company, so that the result of study can be generalized.
2. Adding other variables that can affect accounting conservatism that cannot be explained in this study such as capital intensity, leverage, and firm size.
3. Using other measurement to measure the level of accounting conservatism such as the measurement of market value with book to market ratio proxy that reflects corporate equity book value toward relative market value (Kuspratiwi and Widagdo, 2014).

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