

**THE RELATIONSHIP BETWEEN ACCOUNTING CONSERVATISM LEVEL AND THE AMOUNT OF BANK LOAN IN INDONESIAN STOCK EXCHANGE (IDX) COMPANIES FOR 2012 – 2014 PERIOD**

**Rivo Giovanni Lasmindar**

Professional Accounting / Faculty of Business and Economics

[rivogiovanni@yahoo.com](mailto:rivogiovanni@yahoo.com)

**Abstract** – In today's era financial statement is prepared to benefit several parties for a certain purpose. Thus, information in financial statement is not neutral containing information asymmetries. Conservatism principle in accounting emerges to give protections for the information users. Using banks institution as the financial statement users to see the relationship between accounting conservatism and the amount of bank loan – as their form of decision – in the companies listed in IDX for 2012 to 2014. This finding shows that accounting conservatism do not significantly affecting the amount of Bank Loan. However, the liquidities ratio and the cash flow from operating activities can be an indicator to the amount of Bank Loan possess by the companies.

**Keywords:** Bank Loan, Accounting Conservatism

## **INTRODUCTION**

Basu (1997) stated that accounting conservatism is the accountant tendency to recognize loss immediately on its occurrence and recognize gain until there are sufficient evidence that economics benefits may flow to the company. Furthermore, Belkaoui (1985) argue that accounting conservatism is accountant preferences of accounting method to report lower assets and revenues and higher values of liabilities and expenses recorded. Whatever people define about accounting conservatism, the definition is toward to one understanding about conservatism that it may be protections of the stakeholders from information asymmetries (Hui et al., 2012) and prevent companies for over reporting their assets or revenue (Watts, 2003).

Financial statement needs protections to protect the interest of their information users (Watts, 2003). Generally known, financial statements always contain information asymmetries. Financial information is became a tool for certain parties to achieve their own objections. For example the WorldCom case

that happened in the early 2000. Based on Thibodeau and Frier (2014), WorldCom intentionally and aggressively markup their revenue in order to maintain the stock price, WorldCom allocating some of its operational expenses to financing activities. Indeed, by implementing accounting conservatism it leads to conservative reporting that can benefits stakeholders' through mitigating their agency problems (Watts, 2003 and Holthausen and Watts, 2001).

Despite maintain the stock price, information misleading in financial statement also occur when the companies want to get bank loans or trade credits from their trading partners. The main role of conservatism for both parties is to prevent companies from over-reporting its assets and damaging the interest of creditors (Watts,2003: Jiang and Zhang, 2007). In the creditors' perspective, the good quality of financial report helps them to avoid the emerging of non-performing loan (NPL) and bad debt expense. In the debt contracting process, lenders bear downside risk while they have no upside potential (Zhang 2007). Thus, Bank must selective in their lending decisions to value the information contain in the financial statement. Otherwise, they will bear the downside risk of the companies.

This research is explanatory research which is provided to enhance the financial statement users' horizon about the influence of accounting conservatism against the amount of bank loan obtained by companies. Also this research may benefits several parties such as for studies development, lenders in order to value the conservatism level and understand the effect of conservatism in their lending decisions, last but not least, for the companies to understand the benefits of accounting conservatism implementation in obtaining debt.

This research is divided into 5 sections. Sections one contain the background why the researcher is interested to exploring about this topics based on phenomena's happens in the society. Also this chapter contains the research objectives, benefits of this research, research scope and the research organization. Section two Contain theoretical framework that support this research analysis and initial hypothesis and conceptual framework. Section 3, contain how the researcher is design based on the data gathered according to research scope

(variable and sample usage), data gathering procedure, hypothesis testing plan, and measurement model. Section 4, contain of the explanation about how the data being processed, the results, and findings discussions and comparison about the initial hypothesis and the association with existing theory. Sections 5, contains the conclusion and also the research limitation, implication, and suggestion.

## **LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT**

Accounting conservatism has a closed relationship with bank loan. Banks or lenders are concern about company's conservatism for their own safety to mitigate risk from the company (Watts and Zimmerman, 1986). Since lenders, bank in this case, bear downside risk but have no upside potential (Zhang, 2007), bank needs a conservative financial report so that companies can recognize bad news sooner as their occurrence. This condition leads banks for taking appropriate actions to responds about companies' bad news. Beatty et al., (2008) shows the example of banks reaction against the conditions of their borrowers. In their research entitled *Conservatism and Debt* found that contract modification are higher when the conservatism demands from other parties are lower. It means that when lenders facing uncertainty information from the company, lenders tend to modify the debt covenant to anticipate downside risk.

There are several agreement contain in the bank loan agreement. First of all is how many loan or credit banks trusted to their lenders. Conservative financial report makes lenders having a clearer view about the companies' financial condition and predicting future ability to pay the loan through the information advantages about the changes of the companies' business (Lu and Yang, 2011). Accordingly accounting conservatism can stipulates lending decisions by protecting the interest of the lenders. Thus the accounting conservatism can encourage banks to provide more loan to the companies (Dai and Yang, 2015)..

Second, the debt contract contains interest charges. Zhang (2008) argue that bank will charge lower interest rate when companies produce conservative

financial report. Zhang develop her hypothesis based on her research that bank concern about the unexpected increase of the companies risk from any published information that bank do not expect. Thus, banks will fully information about any activities of the companies do. Thus bank can predict about the risk and can take proper lending decisions. Since Bank has lower risk than the interest rate charge is lower in order to exchange from the information benefits receive from the conservative reporting. Lara et al., (2016) also support above argument that through lower interest offered by banks, companies tend to increase their debt in order to finance their investment

Thus from several relation between accounting conservatism and bank loan above, the researcher argue that Banks are giving their attention to conservatism. Both Dai and Yang (2015) and Lara et al., (2016) argue that through the increase of accounting conservatism of the companies, is followed by the increase of the amount of companies bank loan. Thus both accounting conservatism and bank loan have positive relation or unidirectional relationship. Thus, based on those, researcher draw this following hypothesis:

**H1 Accounting conservatism has a positive relation with the amount of bank loan obtained by companies.**

## **RESEARCH METHODOLOGY**

This research used the data from listed companies in [www.idx.co.id](http://www.idx.co.id) which is Indonesian stock exchange website. The data collected from all companies listed except financial industries (sector 8) and companies that used USD as their reporting currency from 2012 to 2014. Moreover, the data must contain about the information of the variables used in this research. The total population is about 1354 firm-year data. However, there are only 640 firm-year data is fulfill the data requirement.

Bank Loan is the only dependent variable in this research that gathered from the total of short-term bank loan and long-term bank loan, divided by the total assets of the companies. Moreover, this research also has only one independent variable which is conservatism level of the companies that denoted as C-Score. In order to measure C-Score this research is referring to Khan and Watts (2003) C-Score model as follow:

\_\_\_\_\_

G-Score

C-Score

- \_\_\_\_\_ is firm  $i$ 's earnings per share divided by its stock price at the beginning of year  $t$ , by using adjusted share price.
- \_\_\_\_\_ is the stock return of firm  $i$  minus the market return in year  $t$  (from May in year  $t$  to April in year  $t + 1$ ).
- \_\_\_\_\_ is a dummy for the stock return of firm  $i$  in year  $t$ , which equals 1 when \_\_\_\_\_  $< 0$ , and 0 otherwise.
- \_\_\_\_\_ is the natural logarithm of total assets.
- \_\_\_\_\_ is the book to market ratio, which is firm  $i$ 's total market value divided by its book value for owners' equity at the end of year  $t$ .
- \_\_\_\_\_ is the ratio of total liabilities to total assets.

Also there several control variables used in this research as follow:

- Operating Cash Flow (CFO)  
The CFO can be gathered by dividing cash flow from operating activities with total assets.

- Size of the company (SIZE)  
SIZE presented from the natural logarithm of the total assets at the end of the year.
- Liquidity (LIQ)  
LIQ is current asset ratio against total assets of the company. Thus LIQ is current assets divided by total assets.
- Earnings Before Interests and Taxes (EBIT)  
EBIT shows the amount of EBIT divided by companies' total assets.
- Growth rate (GROWTH)  
Indicate the growth rate of  $i$  firm on year  $t$  which the number gather from deducting the operating income of  $i$  firm on the year  $t$  with the income of the same companies on  $t - 1$ . Then it divided with  $t - 1$  operating income.

- 
- Age of the companies (AGE)  
The natural logarithm of the years since the company was established
  - Type of Ownership (TYO)  
This research differ the type of ownership into 5 categories which are companies who the majority shares owned by society will be labeled with 0, individual shareholders will be labeled with 1, companies whose majority shares owned by family or family business labeled with 2, companies whose majority shares owned by others company 3, and state owned companies labeled with 4.
  - Percentage of Independent Commissioners (COM)  
The percentage of independent commissioners gather from dividing how many independent commissioners works in the company with total numbers of commissioners in the company.
  - Percentage of Expertise Audit Committee (AUD)  
This percentage shows how many audit committees is placed based on its expertise in finance and accounting. The numbers of the percentage is equal with how many audit committee placed accordance with their

experience or educational background in finance and accounting divided with total audit committee in the company.

- Type of Industry (TI)

Type of Industry shows in which sector the company listed in IDX.

Then to answer **H1** this research uses this following model:

## **RESULTS AND DISCUSSIONS**

In order to obtain reliable data, the data validity test is conducted. In this research, the data do not passed normality test and heteroscedasticity test. However, Gujarati (2003) stated that, normality problem and heteroscedasticity problem do not significantly influence the data processing as long as the data have total population for more than 100. In the autocorrelation test or Durbin Watson test shows that the data is in the grey area which means that the data cannot be concluded whether those data contain autocorrelation problem or not. Lastly, all the variables passed the multicollinearity test.

This research use Kolmogorov-Smirnov test for normality test. For Heterescedastivity test this research use Glejser test. For Autocorrelation test this research use Durbin-Watson test, and use Variance Inflation Factors (VIF) to detect the multicollinearity.

Based on the results of linier regression model (2) test that depicted in the table 1, then the multiple regression models can be draw as follow:

Table 1  
Multiple Regression Test Table

<b>Variables</b>	<b>Coefficient</b>	<b>t</b>	<b>Sig</b>
Constanta	0,143	1,264	0,207
C-Score	-0,002	-0,082	0,935
CFO	-0,129	-2,092	0,037
SIZE	0,004	1,080	0,281
LIQ	-0,066	-2,589	0,010
EBIT	-0,074	-1,227	0,220
GROWTH	-0,06965	-0,313	0,755
AGE	0,000	-0,484	0,629
TYO	-0,001	-0,175	0,861
COM	-0,089	-1,749	0,081
AUD	0,03934	-0,002	0,999
TI	-0,004	-1,763	0,078

Source: Data Processed from regression model (2) (PASW Statistics for Windows)

From the linear regression, the H1 is rejected. The reason is, based on the regression linear model (2) in the table 1, it shows that the *sig* value of C-Score is higher than 0,05 which is 0,935. The results show that the amount of Bank Loan in Indonesian companies is not depends on the conservatism of the financial report of the companies. However, the amount of Bank Loan is more influenced by the level of the Cash Flow from Operating activities (CFO) and the companies' liquidities (LIQ). This argument is based on the results of t-Test which is shows that CFO and LIQ have significant influence to the Bank Loan (BL).

Furthermore, CFO and LIQ have negative significant correlation with BL. The negative correlation is interpreted by looking in the table 1 in the column t. It shows that CFO has -2,092 and LIQ has -2,589. Thus we can draw the conclusion that the more Bank Loan which are owned by Indonesian companies is because the company has less cash flow from operating activities (CFO). When the companies obtain less cash flow, it results to less liquidity ratio also. Liquidity

ratio indicates the ability of the companies to fulfill short-term liabilities or to fund their short-term business operation (Kasmir, 2008). Thus, companies that suffer liquidity problems will chase loan to fund their short-term payments. Indeed, less liquidity ratio push the company to possess more loans from banks.

In addition, control variables SIZE, EBIT, GROWTH, AGE, and TYO are insignificant with BL. This result is contrast with Dai and Yang (2015). Their results shows that there is significant correlation between SIZE, EBIT, GROWTH, AGE, TYO, and credit obtain by the company. Nevertheless, SIZE and AGE are correlated with C-Score which the conservative score. This result is consistent with Khan and Watts (2009) research that indicate AGE of the company is correlated with companies' conservative level. The older companies tend to have more information available in the market that results less information asymmetries. Khan and Watts (2009) also stated that the older companies also correlated with more assets owned by the companies that depicted by the SIZE score of the companies.

Last but not least, this research also shows insignificant results with credit terms by Indonesian Bank. As 5C stated that Bank must concern about some C's. The first C which contrasts with this result is Condition of Economics. As mentioned earlier in chapter 2 this C explains about the future prospect of the lenders business sectors. Thus since the result of t-test of TI variables shows not significant relation with BL it can be interpreted that there are no relation between companies Bank Loan with industries sector of the companies.

Table 3 depicts the information about correlations between variables. From the table 3, we can see that there are no correlation between BL and C-Score. However, BL is correlate with CFO, LIQ, EBIT and TI. It means that higher amount of Bank Loan (BL) is not followed or based on the financial report contain higher accounting conservatism. Thus, correlation result is consistent with the hypothesis results that reject **H1** in this research.

	<b>BL</b>	<b>C-SCORE</b>	<b>CFO</b>	<b>SIZE</b>	<b>LIQ</b>	<b>EBIT</b>	<b>GROWTH</b>	<b>AGE</b>	<b>TYO</b>	<b>COM</b>	<b>AUD</b>	<b>TI</b>
<b>BL</b>	1	0,024	-0,125**	0,028	-0,124**	-0,140**	-0,014	-0,042	-0,047	-0,062	0,007	-0,082*
<b>C-SCORE</b>	0,024	1	0,018	0,272**	-0,089*	0,002	-0,003	0,078*	0,055	-0,019	-0,038	-0,098*
<b>CFO</b>	-0,125**	0,018	1	0,226**	-0,045	0,531**	-0,010	0,217**	0,066	0,028	-0,033	0,037
<b>SIZE</b>	0,028	0,272**	0,226**	1	-0,183**	0,195**	0,000	0,255**	-0,038	0,069	-0,074	-0,081*
<b>LIQ</b>	-0,124**	-0,089*	-0,045	-0,183**	1	0,225**	0,018	0,052	0,098*	-0,072	-0,011	0,014
<b>EBIT</b>	-0,140**	0,002	0,531**	0,195**	0,225**	1	0,008	0,210**	0,151**	0,024	-0,080*	0,062
<b>GROWTH</b>	-0,014	-0,003	-0,010	0,000	0,018	0,008	1	-0,018	0,034	-0,032	0,000	0,044
<b>AGE</b>	-0,042	0,078*	0,217**	0,255**	0,052	0,210**	-0,018	1	0,101*	0,026	-0,099*	-0,123**
<b>TYO</b>	-0,047	0,055	0,066	-0,038	0,098*	0,151**	0,034	0,101*	1	0,011	-0,053	0,100*
<b>COM</b>	-0,062	-0,019	0,028	0,069	-0,072	0,024	-0,032	0,026	0,011	1	0,043	-0,008
<b>AUD</b>	0,007	-0,038	-0,033	-0,074	-0,011	0,080*	0,000	-0,099*	-0,053	0,043	1	0,049
<b>TI</b>	-0,082*	-0,098*	0,037	-0,081	0,014	0,062	0,044	-0,123**	0,100*	-0,008	0,049	1

Spearman correlations are provided in the upper right of the table and Pearson correlations to the lower left.

\*Significant at the 10% level.

\*\*Significant at the 5% level.

\*\*\*Significant at the 1% level.

## **CONCLUSION AND RECOMENDATION**

This research provides evidence that accounting conservatism do not significantly affect the amount of Bank Loan in Indonesian companies. However, Based on the F-Test or simultaneous test, the *sig* value shows 0,001 which indicate that the main independent variables (C-Score) and all the control variables in this research is simultaneously effecting the amount of bank loan. Also the  $R^2$  analysis tell that the bank loan is only effected 4,7% by the regression model (2). Thus, there are still many factors that affect the amount of bank loan outside the variable that used in this regression model. Furthermore, this research also prove that the amount of bank loan is more affected by the necessity of cash flow from the companies that can be seen in the negative correlation from between BL and the CFO and LIQ ratio.

Also in preparing this research, researcher also faces several limitations. First is Limitation of available data. As stated in the Chapter 4 there are 132 firm-year financial report do not stated or explain about their audit committee educational background or previous working experience. Moreover, some companies do not have share price information available in the yahoo finance website. There are about 33, 34, and 30 companies from 2012, 2013, and 2014, respectively. Second is the accuracy of Bank Loan. Some companies do not specifically separate their or list about their debt. Third is the normality problems and heteroscedasticity problems.

Based on all the stages explained, researcher note some suggestions for a better future research result quality. First, researcher suggests that further research can gather another source except yahoo finance to collect companies' share price data. Second, used another regression model to measure the relation between accounting conservatism and the amount of bank loan.. Lastly, Use another measurement to measure the conservatism of companies' financial report besides Khan and Watts (2009) measurement. For example by using another simpler model that Basu (1997) develop that maybe resulting different results.

## **REFERENCES**

- Amstrong, Christopher S., Wayne R. Guay, Joseph P. Weber, 2010. *The Role of Information and Financial Reporting in Corporate Governance and Debt Contracting*. Journal of Accounting and Economics 10, 179 – 234
- Artikis, Oanagiotis G., Georgios A. Papanastasopoulos. 2016. *Implication of the Cash Component of Earnings for Earnings Persistence and Returns*. The British Accounting Review. 48, 117 – 133.
- Ball, Ray. 2001. *Infrastructure Requirements for an Economically Efficient System of Public Financial Reporting and Disclosure*. Brookings-Wharton Papers on Financial Services page 127 – 169.
- Ball, Ray, Shivakumar, L., 2005. *Earnings Quality in UK Private firms: Comparative Loss Recognition Timeliness*. J. Accounting Economics. 39, 83 – 128.
- Basu, Sudipta., 1997. *The Conservatism Principle and The Asymmetric Timeliness*. J. Accounting. Economics. 24, 3-37.
- Beatty, Anne., Joseph Weber, Jeff Jiewei Yu. 2008. *Conservatism and Debt*. J. Accounting and Economics. 45, 154 – 178.
- Belkaoui A. 1985. *Accounting theory. 2nd edition*. Harcourt Brace Jovanovich, Orlando, Florida.
- Dai, Bingbin and Fan Yang. 2015. *Monetary Policy, Accounting Conservatism, and Trade Credit*. China Journal of Accounting Research. 8, 295-313.
- Bursa Efek Indonesia. [www.idx.co.id](http://www.idx.co.id)
- Efferin, S., Stevanus H.D., and Yuliawati Tan. 2004. *Metodologi Penelitian Akuntansi: Mengungkap Fenomena Dengan Pendekatan Kuantitatif*. Yogyakarta, Indonesia: Graha Ilmu.

- Festiani Satya. 2015. BI: Jumlah Kredit Macet Naik. [Artikel].  
<http://www.republika.co.id/berita/ekonomi/keuangan/15/07/31/nscf2r367-bi-jumlah-kredit-macet-naik> (Accessed on February 25<sup>th</sup> 2016).
- Financial Accounting Standard Board. 1980. *Statement of Financial Accounting Concept No.2*. <http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175820900526&blobheader=application%2Fpdf> (Accessed on February 18<sup>th</sup> 2016).
- Frederic S. Mishkin. 2016. *The Economics of Money, Banking, and Financial Markets*, 11<sup>th</sup> ed. PEARSON: United States.
- Lara, Garcia J.M., Garcia Osma B.,Penalva F. 2011. *Conditional Conservatism and Cost of Capital*. Rev. Accounting. Study. 16 (2), 247-271.
- Lu, Z.F., Yang, D. M. 2011. *Commercial Credit: Alternative Financing or Buyers' Markets?* Management World 4, 6 -14 (in chinese).
- Lozano, Balen, M., Beatriz Martinez, Julio Pindado. 2015. *Corporate Governance, Ownership and Firm Value: Drivers of Ownership As a Good Corporate Governance Mechanism*. International Business Review
- Gujarati, Damodar N. 2003. *Basic Econometrics*. McGraw Hill
- Hui. K.W., Klasa S.,Yeung P.E. 2012. *Corporate Suppliers and Customers and Accounting Conservatism*. J. Accounting. Economics. 53. 115-135.
- Jay C. Thibodeau, and Freier Deborah. 2014. *Auditing and Accounting Cases: Investigating Issues of Fraud and Professional Ethics*. 4<sup>th</sup> ed. McGraw-Hill Education: New York, United States.
- Kasmir. 2008. *Bank dan Lembaga Keuangan lainnya*. Jakarta: PT. Rajagrafindo Persada
- Khan, Mozaffar, Watts Ross L. 2009. *Estimation and Empirical Properties of a Firm-Year Measure of Accounting Conservatism*. J. Accounting Economics. 48, 132-150.
- Kieso Donald E., Weygandt Jerry J., and Warfield Terry D. 2014. *Intermediate Accounting: IFRS Edition*. 2<sup>nd</sup> ed. WILEY: China

- Lembaga Pengembangan Perbankan Indonesia. 2011. *Tren Pendapatan Non-Bunga Perbankan Meningkat*. <http://www.lppi.or.id/index.php/module/Blog/sub/9/id/tren-pendapatan-non-bunga-perbankan-meningkat> (Accessed on April 14th 2016)
- Otoritas Jasa Keuangan. 2015. *Indonesian Banking Statistics*. Vol 13 no 9
- Pranata Evelyn. 2014. [Thesis] *Pengaruh Adopsi IFRS Terhadap Kualitas Akuntansi Dilihat dari Manajemen Laba dan Konservatisme Pada Badan Usaha yang Terdaftar di BEI Pada Periode 2009, 2010, 2012, dan 2013*. Universitas Surabaya, Surabaya
- Prasetyo Budi. 2015. *Perbankan Maupun Debitur Diminta Mewaspadaai Kredit Macet*. [Artikel]. [http:// www.tribunnews.com/regional/2015/08/19/perbankan-maupun-debitur-diminta-memwaspadaai-kredit-macet](http://www.tribunnews.com/regional/2015/08/19/perbankan-maupun-debitur-diminta-memwaspadaai-kredit-macet) (Accessed on February 25<sup>th</sup> 2016)
- Rahmat Zein. 2012. *Skandal Akuntansi Keuangan Worldcom*. [Artikel]. [http://www.academia.edu/10096576/SKANDAL\\_AKUNTANSI\\_KEUANGAN\\_WORLDCOM](http://www.academia.edu/10096576/SKANDAL_AKUNTANSI_KEUANGAN_WORLDCOM) (Accessed on January 20<sup>th</sup> 2016)
- Raenders, A. , and Gaeremynck, A. 2012. *Corporate Governance, Principal-Principal Agency Conflicts, and Firm Value in European Listed Companies*. *Corporate Governance: An International Review* 20, 125 – 143.
- Republik Indonesia. 1998. *Undang-Undang No. 10 Tahun 1998 Tentang Perbankan*.
- Watts R.L. 2003. *Conservatism in Accounting. Part I: Explanations and Implications*. *Accounting. Horizon* 17, 207-221.
- Scott, William R. 2015. *Financial Accounting Theory*. 7<sup>th</sup> ed. PEARSON: Toronto, Canada.

Xu, Xiadong, Xia Wang, Nina Han, 2012. *Accounting Conservatism, Ultimate Ownership and Investment Efficiency*. *China Finance Review International* 2, 1

Zhang, Jieying., 2008. *The Contracting Benefits of Accounting Conservatism to Lenders and Borrowers*. *J. Accounting Economics* 45,27-54