

Can Audit Committee Quality in Moderating Effect of Ownership Structure on Accounting Prudence?

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Abstract. This present study aimed to analyze the influence of foreign ownership, the ownership of institutional ownership of managerial and ownership concentration on accounting prudence moderated by audit committee quality. The population of this research is LQ45 indexed companies in the Indonesia Stock Exchange (IDX), in 2016-2018 there were 59 companies. Based on the purposive sampling method, samples that met the criteria of 46 companies. The final analysis unit is 105 units. The analytical method used is multiple linear regression moderation with IBM SPSS 25. The results of this study indicate foreign ownership, institutional ownership, and concentration of ownership have a positive and significant effect on accounting prudence. Managerial ownership has a significant and negative effect on accounting prudence. Audit committee quality is able to moderate (strengthen) the effect of foreign, institutional and concentration of ownership on accounting prudence. Audit committee quality is able to moderate (weaken) the effect of managerial ownership on accounting prudence.

Keywords: Foreign Ownership, Institutional Ownership, Managerial Ownership, Ownership Concentration, Accounting Prudence, Audit Committee Quality

1 Introduction

In 2012 the International Financial Accounting Standard (IFRS) replaced the concept of accounting conservatism with accounting prudence. Maltby [1] revealed that there are three meanings associated with accounting prudence. First, accounting prudence means an honest and competent attitude in business, a prudent attitude adopted by the bourgeoisie. Second, accounting prudence has the meaning of capital conservation. Third, accounting prudence has the meaning of creative accounting related to the profits or assets of the company to protect management and controlling investors from minority investors who will demand dividends. IFRS defines accounting prudence as a concept that allows companies to recognize revenue even though the income is still in the form of potential. However, revenue recognition must meet the requirements of revenue recognition and must still consider caution in its recognition [2]. It also has an impact on changes in Financial Accounting Standards in Indonesia compiled by Indonesian Institute of Accountants [3] because Financial Accounting Standards adopted IFRS as a guideline for making standards. Financial Accounting Standards which have adopted accounting prudence, namely PSAK No. 14 concerning Inventories and PSAK No. 48 concerning Impairment of Assets.

Sundari and Aprilina [4] revealed that accounting prudence focuses on the prudence associated with uncertain valuations in the company. So, that the reporting made by the

company related to assets, debt, and others is presented in accordance with reality or engineering does not occur. The draft exposure issued Indonesian Institute of Accountants [5] also explains the application of accounting prudence means that profits and assets are not presented in an overstatement manner and liabilities or liabilities are not presented in an understatement. Prudence accounting does not allow the company presents the assets and profits understatement, and obligations or liability overstatement. So, it can be concluded that accounting prudence encourages management to present assets, profits, and liabilities in accordance with the actual conditions so that accounting prudence is considered capable of maintaining the neutrality of financial statements which were previously controversial in applying accounting conservatism.

Agency theory explains that there is a contract between the principal (shareholder/owner/shareholder) and agent (manager) in running the company where each party will maximize the benefits gained from managing the company [6]. Each party who wishes to maximize returns will result in interest differences between the principal and the agent which will lead to asymmetrical information. Differences in information asymmetry will cause agency problems between the principal and agent. Information asymmetry can occur in terms of financial statement presentation. Managers can commit fraud preparing financial statements without the company owner's permission. The presence of investors will increase management supervision and control so that investors will demand management to apply accounting prudence to decrease the agency problem.

One case that occurred due to the lack of implementing accounting prudence in the company is the misstatement of financial statements at PT Lippo Karawaci Tbk. PT Lippo Karawaci Tbk restated its financial statements for the fiscal year 2017 and 2018. Previously, PT Lippo Karawaci Tbk presented revenue in 2018 of Rp12.42 Trillion which was later revised to Rp11.06 Trillion. In addition, PT Lippo Karawaci Tbk also made changes in recording its 2017 net profit of Rp614.17 billion to a loss of Rp377.35 billion (Kontan.com, 2019). This is supported by research data showing that in 2017 and 2018 PT Lippo Karawaci Tbk did not apply accounting prudence. The accounting prudence value of PT Lippo Karawaci Tbk in 2017 is -0.0842 and in 2018 is -0.0618. Falsification of financial statements can be detrimental to corporate investors. Investors can make wrong investment decisions. In addition, investors may misjudge company earnings for the coming period.

This study still refers to research that uses accounting conservatism as the dependent variable due to limited references that make accounting prudence the dependent variable. The next consideration is because the concept is almost the same between accounting conservatism and accounting prudence. Previous research has examined the factors that might influence companies to apply the principles of accounting conservatism in preparing the statement of finance.

Previous research conducted Zureigat [7]; Fadzil and Ismail [8] and Alkordi et al. [9] stated that foreign ownership has a positive and significant effect upon the application of accounting conservatism. However, Le et al. [10] revealed a negative correlation between foreign ownership and accounting conservatism. Research conducted Salehi and Sehat [11]; Alkordi et al. [9], Lin [12], Fadzil and Ismail [8], and Ramalingegowda and Yu [13] about the effect of institutional ownership upon Accounting conservatism which produces positive results. However, research conducted Syifa et al. [14] shows that institutional ownership does not have any effect on the application of the principles of accounting conservatism. The next factor that can influence accounting conservatism is managerial ownership. Research conducted Dewi and Suryanawa [15] and Putra et al. [16] show that the effect of managerial ownership upon accounting conservatism is positive. However, research conducted Maharani

and Kristanti [17] and Brilianti [18] produced negative results. Research on the concentration of ownership of accounting conservatism still produces inconsistent results. Alkordi et al. [9] and Kartika et al. [19] state that there is no correlation between the concentration of ownership on accounting conservatism. However, Cullinan et al. [20]; Loay et al. [21], and Ratnadi and Ulupui [22] state that the ownership concentration gives a negative influence on accounting conservatism.

Based on research that has been done previously still produces inconsistent results. As a result of previous research results that still produce inconsistent results, in this study there are audit committee quality factors as moderating variables which according to agency theory can strengthen or weaken the relationship of foreign ownership, institutional ownership, managerial ownership, as well as concentration of ownership related to accounting prudence variables. In addition, according to Bapepam-LK Regulation No/IX/1/5 [23], audit committee quality has the responsibilities and duties issued Republic of Indonesia Financial Services Authority [23], including reviewing financial statements issued by companies and providing results of studies on possible risks borne by the company and the implementation of risk management by directors so that audit committee quality is able to strengthen the influence of ownership structure on accounting prudence. So that, the objectives in this study are divided into eight, which are first, foreign ownership on accounting prudence. Second, ownership of institution on accounting prudence. Third, managerial ownership on accounting prudence. Fourth, ownership concentration on accounting prudence. Fifth, audit committee quality on foreign ownership and accounting prudence. Sixth, audit committee quality on ownership of institution and accounting prudence. Seventh, audit committee quality on managerial ownership and accounting prudence. Eighth, audit committee quality on ownership concentration and accounting prudence.

To answer the eighth research question, then described development of the hypothesis. An [24] argues that foreign investors have the ability to oversee companies which can have an impact on increasing managerial performance monitoring. Beuselinck et al. [25] also stated that foreign investors have good experience in international markets compared to domestic investors. Foreign investors, especially foreign institutional investors, have technology that can help them process information more quickly, relevantly and effectively [26]. Therefore, the increasing ratio of foreign ownership in a company, the supervision of managers related to transparency and accounting decisions in a company will increase. Previous research conducted Alkordi et al. [9], An, [24], and Fadzil and Ismail [8] gave the result that foreign ownership had a positive and significant effect upon the application of accounting conservatism.

H1: Foreign ownership has a significant and positive effect upon accounting prudence.

Institutions or institutions can control management actions directly by utilizing the company's share ownership and controlling it indirectly through the sale of company shares owned by the institution [27]. Chabachib et al. [28] and Gillan and Starks [27] suggested that institutional investors get good opportunities, resources, and ability to supervise, control, and affect managers. An adequate capacity of foreign investors will give positive effect upon increasing the push for management to apply prudence. The findings Ramalingegowda and Yu [13], Syifa et al. [14], and Jiang and Kim [29] revealed that affirmative correlation is present between ownership of institution and conservatism of accounting.

H2: Institutional ownership has a significant and positive effect upon accounting prudence.

The role of management as a shareholder can give effect upon the reduction in the opportunistic attitude of management in managing the company. When the ownership of management is large, management will choose a more conservative policy. This is because management puts forward the interests of the company in the long run rather than prioritizing profitability. Research conducted by Utomo [30] and Putra et al. [16] states that an affirmative correlation between managerial ownership and accounting conservatism is present. Ghozali et al. [31] and Putra et al. [32] argues that increasing managerial ownership will increase the application of accounting conservatism because management considers the continuity of the company's business rather than personal interests of management. So, that management will choose to apply accounting conservatism compared to aggressive accounting methods.

H3: Managerial ownership has a significant and positive effect on accounting prudence.

Kiatapiwat [33] explains that the concentration of share ownership can result in controlling shareholders obtaining private information easily so that it will have an impact on reducing agency conflict. Therefore, the quality of financial statements in a company that has a high level of concentration in ownership will be lower [34]. Majority investors do not really need financial information because majority investors have been able to access private company information so that majority investors will not encourage increased companies application of accounting conservatism [35]. Cullinan et al. [20], Loay et al. [21], and Ratnadi and Ulupui [22] support the statement above that there is a negative relationship between ownership concentration and the application of the principle of accounting conservatism.

H4: Ownership concentration has a significant and positive effect on accounting prudence.

The participation of foreign investors will increase supervision of management. This is in accordance with one of the objectives of external investors. The presence of a committee in an audit in a company will help foreign investors to oversee the behavior of management in managing the company. According to the Chairman's decision of BAPEPAM-LK Kep-643/BL/2012 regarding the Formation and Guidelines for the Work of audit committee quality, it is well-defined that audit committee quality members are not allowed to own company shares either directly or indirectly. Based on this decision, the number of audit committee quality in the company is at least three people with a composition of members of at least an independent commissioner as well as two other members from external parties of the company where the members are from outside the issuer or public company. An independent audit committee quality that has competence, experience and independence will strengthen the influence of foreign ownership to encourage management to apply prudence

[36].

H5: Audit committee quality significantly strengthens the influence of foreign ownership on accounting prudence.

Institutional investors expect high returns on invested resources, while management returns high on their performance. Institutional investors will implement corporate governance that aims to safeguard the interests of shareholders by encouraging companies to report information transparently [28][37]. In conducting surveillance, shareholders will be assisted by the board of commissioners as representatives of shareholders. The board of commissioners assisted by audit committee quality will supervise management performance. According to the Chairman's decision of BAPEPAM-LK Kep-643/BL/2012 regarding the Establishment and Guidelines for the Work of audit committee quality, it is well-defined that audit committee quality members are not allowed to own company shares either directly or indirectly and the number of audit committees quality in the company is at least three people consisting of independent commissioner and two external parties of the company where the member comes from outside the issuer or public company. Audit committees quality from outside the company will have higher independence compared to audit committees quality originating from within the company so that the independent audit committee quality will oversee management to the maximum and will strengthen the influence of institutional ownership in encouraging management to apply the principles of accounting prudence.

H6: Audit committee quality significantly strengthens the influence of institutional ownership on accounting prudence.

The role of management as a shareholder and manager of the company can have an impact on the reduced opportunistic attitude of management in managing the company. When the ownership of management is large, management will choose a more conservative policy. The presence of in the audit committee will assist management in conducting oversight in the company. This is in line with the agency theory explaining that the presence of an independent party in the company will help supervise the management. According to the decision of the Chairperson of BAPEPAM-LK Kep-643/BL/2012 regarding the Establishment and Guidelines for the Work of audit committee quality, the number of audit committee quality in the company consists of at least one independent commissioner and two other members from external parties. The members of audit committee quality who come from outside the company are considered to have high independence because audit committee quality is not involved in managing the company or acting as a shareholder. Thus, audit committee quality can influence the correlation between ownership of managerial and conservatism of accounting.

H7: Audit committee quality significantly strengthens the effect of managerial ownership on accounting prudence.

Yunos et al. [38] which states that investors from outside parties have demands to have information that is equivalent to investors from inside parties by demanding transparent reporting. This is done by outside investors to protect investments that have been invested in the company. The presence of audit committee quality will assist controlling investors in supervising management, one of which is preparing financial statements. This in line with the

agency theory which explains that audit committee quality as an external party of the company will assist the management in carrying out supervision. According to the decision of the Chairman of BAPEPAM-LK Kep-643/BL/2012 regarding the Establishment and Guidelines for the Work of audit committee quality, it is clear that audit committee quality members were composed of at least an independent commissioner and two external parties. Independent audit committee members have the ability, independence, and qualified experience so that they will work professionally in carrying out their tasks. Thus, audit committee will be able to influence the correlation between ownership concentration and accounting prudence.

H8: Audit committee quality significantly strengthens the effect of ownership concentration on accounting prudence.

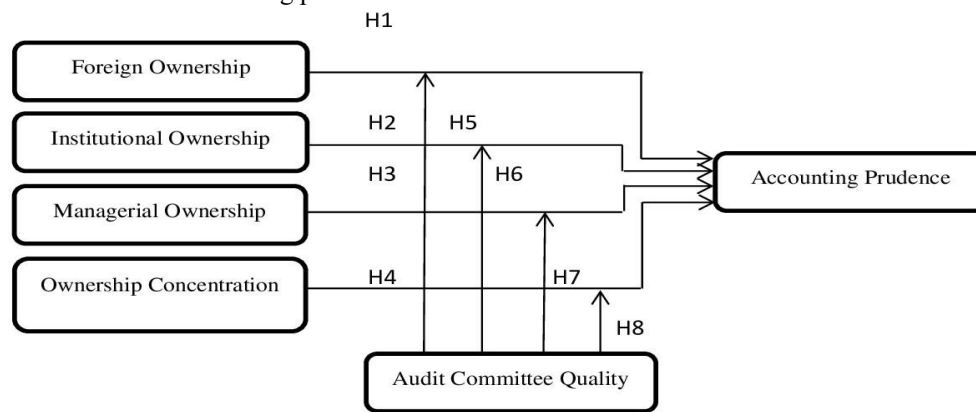


Fig. 1. Research Model

2 Method

This present study uses a quantitative approach, with a hypothesis testing research study design. The population in this study is companies indexed LQ45 on the Indonesia Stock Exchange, in 2016-2018, amounting to 59 companies. LQ45 is One of the Leading Indices on IDX. It is called superior and prestigious because the strict standards and requirements for issuers who wish to enter are limited to only 45 shares and already have the best track record in supervision over the past year. Our sample is limited in 2018 because our research was conducted in 2019. The sample was selected using the purposive sampling technique as follows:

- 1) Companies are indexed LQ45 at the Indonesia Stock Exchange during 2016-2018.
- 2) Companies that publish annual reports consistently throughout the during 2016-2018.
- 3) The company presents detailed research variable data.

The final sample of this study was 46 companies because 13 companies did not provide information related to the variables needed so that there were 138 analysis units. Outlier data amounted to 33 so that the number of final analysis units amounted to 105 analysis units. The analytical method used is moderated multiple linear regression with IBM SPSS version 25. The dependent variable in this study is accounting prudence. The independent variables in this study are foreign ownership, ownership of institution, ownership of management, and ownership of concentration and the moderating variable is audit

committee quality. The operational definitions of the variables can be seen in table 1:

Table 1. Definition of Operational Research

No	Variable	Variable Definition	Measurement
1.	Accounting Prudence	A concept that allows companies to recognize revenue even though the income is still in the form of potential.	(Net income-Operating cash flow Depreciation)/Total Assets x-1
2.	Foreign Ownership	The proportion of foreign investor shares in a company.	Shares owned by foreign investors/Number of shares outstanding x 100%
3.	Institutional Ownership	Participation in ownership of institutions or institutions such as banks, insurance companies, or other institutions in the form of ownership of shares in a company.	Number of shares owned by institutional investors/Number of shares outstanding x 100%
4.	Managerial Ownership	Ownership of shares owned by managers so that managers also play a role as shareholders.	Number of shares owned by management/Number of shares outstanding x 100%
5.	Ownership Concentration	The majority shareholding owned by the company's external parties.	$\frac{\Sigma \text{share ownership} \times 100\%}{\Sigma \text{outstanding shares}} > 5\%$
6.	Audit Committee Quality	Some consist of one or more members of the board of commissioners and can recruit from external parties who have experience, expertise, and other qualities that can help achieve the objectives of audit committee.	Number of audit committee quality in the company

The type of data is secondary data obtained by the documentation technique in the statements of finance of the Indonesia Stock Exchange LQ45 during 2016-2018. Data analysis techniques employed descriptive statistical analysis, classic assumption test, moderated regression analysis, and hypothesis testing using SPSS version 25. The moderated regression analysis model is systematically expressed in the form of equations as follows:

$$\text{PRUD} = \alpha + \beta_1 \text{ZKA} + \beta_2 \text{ZKI} + \beta_3 \text{ZKM} + \beta_4 \text{ZKK} + \beta_5 |\text{ZKA-ZKOM}| + \beta_6 |\text{ZKI-ZKOM}| + \beta_7 |\text{ZKM-ZKOM}| + \beta_8 |\text{ZKK-ZKOM}| + \varepsilon$$

Information:

PRUD	=	Accounting Prudence
A	=	A constant
β	=	Regression Coefficient
ZKA	=	Standardized Value of Foreign Ownership
ZKI	=	Standardized Value of Institutional Ownership
ZKM	=	Standardized Value of Managerial Ownership
ZKK	=	Standardized Value of Ownership Concentration
ZKOM	=	Standardized value of Audit Committee Quality
e	=	Standard Error

3 Result and Discussion

The description of the data used in this study can be known through descriptive statistical analysis. Descriptive statistical tests will show the mean, maximum, minimum, and standard deviation of the data of the research. The descriptive statistics is presented in Table 2.:

Table 2. Results of Descriptive Statistics Test

Variable	N	Minimum	Maximum	Mean	Std. Deviation
Foreign Ownership	105	.0000	.9452	.330521	.2611932
Government Ownership	105	.0000	7536	.211790	2921816
Institutional Ownership	105	.0371	.8985	.397690	.3104397
Managerial Ownership	105	.000000	.016000	.00074555	.002417126
Ownership Concentration	105	2543	.8053	.557884	.1129701
Audit Committee Quality	105	3	6	3.50	.867
Accounting conservatism	105	-.1527	2861	.049409	.0755989
Valid N (listwise)	105				

(Secondary data processed)

Before conducting the moderation regression test and testing the hypothesis, first the classical assumption test is composed of tests of normality, multicollinearity, autocorrelation, and heteroscedasticity. The multicollinearity test showed that the data were free from multicollinearity symptoms because all variables showed a VIF value <10 and a tolerance value >0.10. The first normality test shows the asymp value sig. 0,000 which means that the data were not normally distributed so that the removal of the data outlier as many as 33 of data outliers. The results of the second normality test show asymp values sig. equal to 0,200(0,200>0,05) which reveals that the data is distributed normally. The autocorrelation test results showed $du < DW < 4-dU = 1.7827 < 1.834 < 2.2173$ so that in this study autocorrelation does not exist. Heteroscedasticity test results show that there is no heteroscedasticity in the research data, it can be seen in the results of the Glejser test that shows the t test and F test all variables have a significance value that is above the 5% confidence level or 0.05. Table 3. presents a summary of the results of hypothesis testing in the study. The table contains information related to the hypothesis, regression coefficient, significance value, alpha value, and to the decision whether the hypothesis is accepted.

Table 3. Summary of Hypothesis Test Results

No	Hypothesis	Regression Coefficient	Sig.	Alpha	Decision
1	H1	0.050	0,000	0.05	Accepted
2	H2	0.040	0,000	0.05	Accepted
3	H3	-0,054	0.005	0.05	Rejected (negative)
4	H4	0.020	0.010	0.05	Accepted
5	H5	-0,016	.191	0.05	Rejected (weaken)
6	H6	-0,022	0.072	0.05	Rejected (weaken)
7	H7	0.059	0.002	0.05	Accepted (Strengthen)
8	H8	-0,001	0.933	0.05	Rejected (weaken)

To answer **the first research question**, which is H1 testing results obtained regression

coefficient of 0.050 and a significance value of 0,000 (<0.050) so that H1 is accepted. This indicates that the increase in the percentage of foreign ownership will have a positive influence that can reduce the opportunistic behavior of management so that it will have an impact on increasing the application of accounting prudence. This can occur because the supervision conducted by foreign investors can be optimally guaranteed so that it can influence management in making decisions. Foreign investors will pressure management to implement accounting prudence in an effort to protect the resources that have been invested. This research is in line with agency theory and is supported by research conducted Fadzil and Ismail [39] and Alkordi et al. [9] which states that foreign ownership positively influences accounting conservatism. This indicates that an increase in the percentage of foreign ownership will encourage management to increase accounting prudence in preparing the statement of finance.

To answer **the second research question**, which is H2 test results obtained a regression coefficient of 0.040 and a significance value of 0.000 (<0.050) so that H2 is accepted. This indicates that increasing the percentage of institutional ownership will have a positive influence that can reduce the opportunistic behavior of management so that it will have an impact on increasing the application of accounting prudence, and vice versa. Institutional investors will carry out oversight of management optimally because usually the institution has a relatively large share so that the institution will pressure management to apply prudence to protect their capital and reduce the risk of bankruptcy in the company. The supervision is also supported by the high ability of investors to supervise management. The statement was supported by Gillan and Starks [27] also suggested that investors of institution get good opportunities, resources, and ability to supervise, discipline and influence managers. This research is in line with agency theory and is supported by research conducted by Alkordi et al. [9] and Lin [12] which explains that positive correlation between institutional ownership and accounting conservatism was present.

To answer **the third research question**, which is H3 test result obtained value regression coefficient of -0.054 and the significant value of 0.005 ($<0,050$) so H3 is rejected. The test states that ownership of management has a negative and considerable influence on accounting prudence. This might occur because the percentage of shared ownership by management is smaller than the ownership of shares by external parties. In preparing conservative statements of finance will be carried out by management if the level of management ownership is higher than that of other parties. Management prefers accounting methods that support management achieving prosperity. The research results do not support agency theory, but they are consistent with research conducted by Brilianti [18] and Saeed et al. [40] stating that managerial ownership negatively influences the application of the principles of accounting conservatism. This reveals that the higher ownership of management will give an impact on the increasingly opportunistic attitude of management so that it reduces the level of accounting prudence in that company.

To answer **the fourth research question**, which is H4 test result obtained regression coefficient of 0.020 and a significance value of 0.010 (<0.050) so H4 is accepted. This indicates that increasing the percentage of ownership concentration will have a positive influence on the application of accounting prudence, and vice versa. Increased ownership by controlling investors will increase oversight of management due to the higher resources invested by controlling investors. The controlling investor will encourage management to apply accounting prudence because the application of accounting prudence can put pressure on management to manipulate profits that harm companies and investors. The research results support the agency theory and are in complimentary with research conducted by Kartika et al.

[19] which suggests that being concentrated will tend to require companies to report more conservative statements of finance.

To answer **the fifth, sixth and eighth research question**, which is H5, H6, and H8 test result significance value respectively of 0.191, 0.072, 0.933 (>0.05) so that the hypothesis is rejected. This possibility could occur because in choosing the composition of the committee of audit, the company did not consider the capability aspect [18]. It is possible that the company did not consider the ability of its members because the company only fulfilled the mandatory requirements to register on the IDX or the company did not focus its oversight on accounting. This has an impact on sub-optimal supervision in the statements of examination of finance. So, that the financial statements are not conservative. Furthermore, the cause of audit committee quality can moderate (weakening) the relationship of foreign ownership, institutional ownership and ownership concentration to accounting prudence. This contradicts agency theory but supports legitimacy theory. Companies tend to be optimistic in presenting assets and profits to attract investors and get legitimization of the stakeholder.

To answer **the seventh research question**, which is H7 test results obtained a regression coefficient of 0.018 and a significance value of 0.002 (<0.050) so that H7 is accepted. This can be interpreted if the presence of an audit committee quality can strengthen the relationship of managerial ownership to accounting prudence. This is possible because the shareholders demanded the board of commissioners to improve the quality of supervision, the competence of audit committee quality, or increase the number of audit committee quality in the company when there was an increase in the percentage of managerial ownership. This is done by investors as an effort to suppress the opportunistic behavior of management when share ownership by management increases. Excessive opportunistic management behavior will likely bring an impact on falsification of financial statements or increase the risk of bankruptcy. The research results confirm the agency theory and support the research by Putra et al. [16] stating the number of committees of audit has positive impact on the application of accounting conservatism.

4 Conclusions and Limitations Conclusion

There are three meanings associated with accounting prudence. First, accounting prudence means an honest and competent attitude in business, a prudent attitude adopted by the bourgeoisie. Second, accounting prudence has the meaning of capital conservation. Third, accounting prudence has the meaning of creative accounting related to the profits or assets of the company to protect management and controlling investors from minority investors who will demand dividends. Based on the analysis of the report, foreign ownership, institutional ownership, and concentration of ownership give a considerable and positive effect on accounting prudence. Significant influence managerial ownership and negative against accounting prudence. Audit committee quality is able to moderate (strengthen) the effect of foreign ownership, institutional ownership, and concentration of ownership on accounting prudence. The committee of audit is able to moderate (weaken) the effect of managerial ownership on accounting prudence.

5 Limitation

For researchers, variable audit committee were solely based on the data cross section. So, further research is recommended for the data base of audit committee quality with the data panel. So that, the future researchers are expected to use other moderating variables that can strengthen or weaken share ownership by foreign parties, institutions, and controlling investors.

The company should apply accounting prudence, pay attention to the structure of share ownership and audit committee quality and improve supervision and competence of audit committee.

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