

The Influence of the Level of Competition on Accounting Conservatism through Corporate Governance



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ABSTRACT: This research aims to examine the influence of competition on accounting conservatism through corporate governance. Accounting conservatism is measured using the market to book ratio approach, corporate governance is measured by the Corporate Governance Self-Assessment and competition is measured by the Lerner Index. The population in this study was 35 banking companies listed on the Indonesian Stock Exchange. The sampling technique used was Purposive Sampling, resulting in a sample size of 6 companies which were book category 4 banks. The model used in this research was panel data regression using SPSS version 24. The results of this research show that competition influences accounting conservatism and corporate governance. Corporate governance influences accounting conservatism.

KEYWORDS: Accounting conservatism, corporate governance, competition

I. INTRODUCTION

Banks are faced with various risks, including credit risk, market risk, operational risk and reputation risk in carrying out their business activities. The banking crisis in Indonesia that occurred at the end of 1997 was not solely caused by the economic crisis, but was also caused by the lack of implementation of good corporate governance and the ethics that underlie it (Purwasih, 2020). Therefore, efforts to restore confidence in the Indonesian banking world through restructuring and recapitulation can only have a long-term and fundamental impact if accompanied by three other important actions, namely: (1) Compliance with the principle of prudence (conservatism); (2) Implementation of good corporate governance; (3) Effective supervision from the Bank Supervisory Authority (Zarkasyi, 2008).

One of the efforts made by banking companies to achieve their goals is to apply the principle of conservatism. Conservatism is a principle in financial reporting that is carefully designed to recognize and measure assets and profits through economic and business activities in a company (Mohammed et al., 2017). The principle of conservatism is a prudent principle towards an uncertain event and is used to reduce the attitude of high optimism (belief) from company managers and company owners. The principle of accounting conservatism in companies is used in unequal or different capacities. The important thing to determine the degree of conservatism in the preparation of corporate financial statements is the responsibility of all company managers and all groups within the corporation in conveying information that is open, accurate and not misleading to investors. Research by Leventis et al. (2013) states that commercial banks registered in the United States with good corporate governance will carry out financial reporting with conservatism compared to banks whose governance is less good.

The level of competition in an industry influences each company to perform, other research states that the level of competition influences companies in policies related to accounting conservatism (Dhaliwal et al., 2011). A high level of competition in a market provides transparent information to each company in that market. The company cannot hide the losses incurred and recognize losses early. The recognition of this loss is an act of accounting conservatism caused by the level of competition. Lafond and Watts(2008)conducted research which stated that the better the company implements the principle of accounting conservatism, the less opportunity there is for company managers to commit fraud and exaggerate financial reports so as to increase the value of the company.

Much research has been conducted on Accounting Conservatism, previous research was conducted by Nasr and Ntim (2018) and Prabaningrat and Widanaputra (2015), which states that Corporate Governance has an influence on accounting conservatism. Research conducted by Dhaliwal et al., (2011) shows that the level of competition has an influence on accounting conservatism. Apart from that, there is research which states that competition influences corporate governance (Karuna, 2011), (Chou et al., 2011) which states that there is an effect of competition on accounting conservatism. Does competition have a

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direct effect on accounting conservatism or through corporate governance first, then it has an effect on accounting conservatism?

II. THEORETICAL BASIS

A. Agency Theory (Agency Theory)

Agency theory assumes that all individuals act in their own interests. Agency problems arise because of a conflict of interest between shareholders and managers, because maximum goals are not met between the principal and the agent. As agents, managers are morally responsible for optimizing the profits of the owners (principals), but on the other hand, managers also have an interest in maximizing welfare. So there is a high probability that the agent does not always act in the best interests of the principal (Jensen and Meckling 1976).

B. Accounting Conservatism

Watts (2003a) defines conservatism as the principle of prudence in financial reporting, companies are not in a hurry to recognize and measure assets and profits, and immediately recognize losses and debts that are likely to occur. The application of this principle results in the choice of accounting method being aimed at methods that report lower profits or assets, and report higher debt. Accounting conservatism describes prudent actions regarding events that may or may not occur. The function of the principle of conservatism is to reduce excessive optimism from company managers and company owners (Watts, 2003). The important thing in determining conservatism policies in a company is the commitment of all components in the company. In the company, both the company management and parties within the company in providing information that is open, accurate, and does not cause errors in decision making for investors.

C. Competition

Competition is the efforts of both parties or companies, each of which is active in "obtaining orders" by offering the most favorable prices or terms. Competition can consist of price cuts, promotions, variety and quality, packaging, design, and market segmentation (Maribun, 2003). And according to Kocabay (2009) competition is a process between companies (banks) in winning business which aims to increase market share and earn greater profits. The tighter the level of competition, the more the market will reduce companies' ability to gain or make profits, thus encouraging a company to take large risks (careless attitude) in an effort to increase profits. The banking industry with its high level of competition causes banks not to carry out conservative policies because banks want to make a profit and retain customers. Companies will tend to adopt policies that increase risk, banks choose riskier customers by entering customer groups that have been avoided, and banks include risky credit portfolios from certain industries (Wibowo and Siantoro, 2018).

D. Corporate Governance

Corporate *governance* Basically it concerns the issue of controlling the behavior of top company executives to protect the interests of company owners (shareholders). Corporate governance problems occur because of the separation between ownership and control in the company. This problem can be traced from the development of agency theory which explains that the parties involved in the company (managers, company owners and creditors) will behave in accordance with their respective interests or have different interests. With good governance, it is expected that company management will be more conservative and can affect profit management activities.

E. Hypothesis

1) The influence of competition on accounting conservatism.

The conventional view of competition is the competition fragility view which states that an increasingly high level of competition in a market will reduce a company's ability to gain or make a profit, thereby encouraging a company to take large risks (careless attitude) in an effort to increase its profits. or company profits. Company managers must report losses quickly through conservative financial reporting. Companies tend to be more conservatism through choosing conservative accounting principles and policies to recognize these losses immediately. Based on the research of Dhaliwal et al.,(2011)that there is an influence of the level of competition on accounting conservatism. From the description above, a hypothesis can be made as follows:

H1: Competition influences accounting conservatism.

2) The influence of competition on corporate governance.

Corporate governance can be influenced by the level of competition, a higher degree of market competition will increase corporate management behavior. In an industry where companies are in a competitive environment, corporate governance tends to influence the level of competition or adjusts to the competition that occurs in the industry.(Chou et al., 2011). Research

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conducted by Karuna (2011) states that there is an influence of competition on corporate governance. From the description above, a hypothesis can be made as follows:

H2: Competition influences corporate governance

3) The influence of corporate governance on accounting conservatism.

Agency theory occurs when a company owner employs other people (agents) to manage and make decisions related to company activities. The relationship between company managers and owners can lead to a condition of information imbalance because company managers have more information about company activities compared to company owners. One of the ways used to limit the opportunistic behavior of company managers is by implementing corporate governance. Corporate governance implemented by the company, where the board of commissioners is tasked with supervising the performance of directors so that the policies of the company's directors will create a level of conservatism that will be implemented by the company in terms of method selection (Wardhani, 2008), so that the implementation of corporate governance will affect the level of corporate accounting conservatism (Nasr & Ntim, 2018), (Ahmed & Duellman, 2007), (García Lara et al., 2009) and (Prabaningrat & Widanaputra, 2015). From the description above, a hypothesis can be made as follows:

H3: Corporate governance influences accounting conservatism.

4) The influence of competition on accounting conservatism through corporate governance

Based on the research of Dhaliwal et al., (2011) There is an influence of the level of competition on accounting conservatism. In intense competition, the market provides complete information about real market conditions so that company managers cannot hide the losses that occur. Company managers must report losses early, which is conservatism reporting. Corporate governance can be influenced by the level of competition, a higher degree of market competition will increase the behavior of corporate management. Implementation of corporate governance carried out by the company, where corporate governance is tasked with overseeing the performance of company managers so that the policies of the company's directors will determine the level of conservatism that the company will implement. Is the influence of competition on accounting conservatism directly or is the influence of competition affecting accounting conservatism through corporate governance. From the description above, a hypothesis can be made as follows:

H4: Competition influences accounting conservatism through corporate governance

III. METHOD

A. Population and Sample

This research uses a population of all banking corporations on the Indonesian Stock Exchange (BEI), totaling 45 corporations taken from 2013 to 2017. This research, to obtain samples, uses a purposive sampling method, namely a method based on predetermined parameters and suitability of characteristics in determining samples. Based on the selection of samples according to the criteria, it was determined that there were 6 companies. Sample selection is based on benchmarks, namely:

1. Banking sector corporations listed on the BEI (Indonesian Stock Exchange) from 2013 to 2017 and banking corporations that publish audited annual financial statements ending on December 31 within the research period.
2. Banking is included in book 4 criteria, because it can describe the state of banking in Indonesia based on the size of assets of 6 companies.
3. Corporations have data regarding self-assessment, level of competition, and data that is related to the research variables to be studied.

B. Variable Operational Definitions

Operational variables are used to clarify the operationalization of several concepts and terms reviewed in this research plan, definitions are used so as not to create misunderstandings:

1) Competition (X1)

Competition is a picture of a company winning the competition by increasing market share and profits. To measure competition based on market structure using the Lerner Index, according to Demirguc-Kunt and Peria (2010), The Lerner Index value describes the degree of competition divided into three large groups, the first is a perfectly competitive market which is described as the Lerner Index value going towards zero. Second, the monopoly market is described by a Lerner index of one or close to one. The three monopolistic competition markets are described by the Lerner Index being between zero and one or the market conditions are around the two market forms above, namely perfect competition markets and monopoly markets. Lerner index with the following formulation:

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$$\text{Lerner Index (X1)} = \frac{\text{TR}-\text{TC}}{\text{TR}}$$

Where:

TR (Total Revenue) = Total interest and non-operating income.

TR (Total Cost) = Total interest and non-operational costs

2) Corporate Governance (Y1)

Corporate governance proxied by Self Assessment Corporate Governance, is the basis for banks to measure the performance of bank governance regulated by Bank Indonesia through Bank Indonesia Regulation No.8/4/PBI/2006 dated 30 January 2006 and Number 8/14/PBI/2006 dated 5 October 2006 concerning Amendments to Bank Indonesia Regulation Number 8/4/PBI/2006 regulating the Implementation of GCG for Commercial Banks, which is one of the efforts to strengthen the national banking industry in accordance with the Indonesian Banking Architecture. Ratings from 1 to 5, where 1 is very good and 5 is not good.

3) Accounting Conservatism (Y2)

Accounting conservatism is if the market value of a company is greater than its book value. In this research, conservatism is proxied using calculations by Givoly and Hayn (2000), namely explaining the size of the market relative to the company's book value, which is called the market to book ratio. The assessment of the market to book ratio if it is worth more than one (1) illustrates the determination of conservative accounting principles because the corporation obtains a company value lower than its market value. If the comparison of the market to book ratio equation is less than one (1), it shows that the determination of accounting principles is not conservative because the corporation obtains a higher corporate value than its market value. (Beaver & Ryan, 2000).

$$\text{Market to book ratio (Y1)} = \frac{\text{Market price per share}}{\text{Book value per share}}$$

$$\text{Book value per share} = \frac{\text{Total equity}}{\text{Number of share outstanding}}$$

IV. RESEARCH RESULT

This section will describe a detailed explanation of data analysis and discussion of research findings. The data study was carried out by carrying out several stages, namely descriptive analysis, purposive sampling, assumption testing and using the SPSS 24 program for path analysis. Discussion of research findings is presenting, interpreting and discussing research results in accordance with the problem formulation and research objectives.

A. Descriptive Analysis

Descriptive statistical studies are used to convey an overview or representation of research variables. Descriptive statistical analysis in this research is about calculating the amount of corporate governance, competition, accounting conservatism and profit management in the Indonesian banking industry listed on the Indonesian Stock Exchange in 2013-2017.

Table 1. Descriptive Statistics Test Results

	N	Minimum	Maximum	Means	std. Deviation
Competition	25	1	1	.67	,077
Corporate Governance	25	1	2	1.53	.479
Accounting Conservatism	25	0	4	1.93	1,170
Valid N (listwise)	25				

Based on table 1, descriptive statistical calculations can be seen that the banking industry on the BEI in 2013-2017 had an average self-assessment calculation of 1.53, which means the level of corporate governance is very good because the sample is a bank with book criteria 4. And competition at level 1 means in a monopoly market. And the average level of accounting conservatism in the banking industry is 1.93. banks tend to be conservative.

B. Path Analysis Results

This research uses path analysis to analyze data and is assisted using the SPSS version 24 computer program. Path analysis was chosen because this analysis is used to analyze relationship patterns between variables. In this research model there is an intervening variable, namely the effectiveness of accounting conservatism which strengthens or weakens the relationship between corporate governance and competition and earnings management.

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C. Classical Assumption Testing

Based on test equipment using SPSS version 24 computer program to test normality, multicollinearity test and heteroscedasticity test produces the data used in this research is normally distributed data, there is no multicollinearity between variables and in the regression model there is no heteroscedasticity.

D. The First Path Model of Influence on Accounting Conservatism

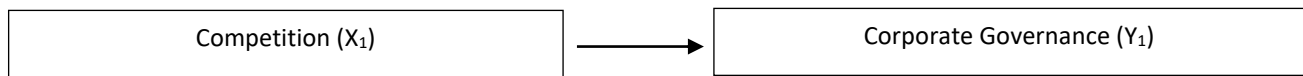


Figure 1. First Path Analysis Regression Equation

The regression model implemented in this research is a first path model to examine the partial and simultaneous impact of (exogenous) variables, competition (X1), on corporate governance (Y1). The studies that will be achieved in this research through the first line model are as follows:

Table 2. First Path Model Hypothesis Testing

Model		Unstandardized Coefficients		Standardized	t	Sig.
		B	std. Error	Coefficients		
1	(Constant)	3,747	,751		4,987	,000
	Competition	-3,297	1.108	-.527	-2,975	,007

a. Dependent Variable: Corporate Governance

First Path Analysis Regression Equation:

$$Y_1 = -0.527X_1 + e$$

Competition has a negative effect on corporate governance, so that if competition increases with corporate banking in Indonesia, corporate governance will decrease. From table 5, it can be seen that competition has a negative impact on corporate governance as indicated by the p calculation of 0.007 which is in accordance with the provisions of <0.05. So with the explanation above, the hypothesis that partnerships influence corporate governance is proven.

Second Path Model of the Influence of Competition on Accounting Conservatism through Corporate Governance

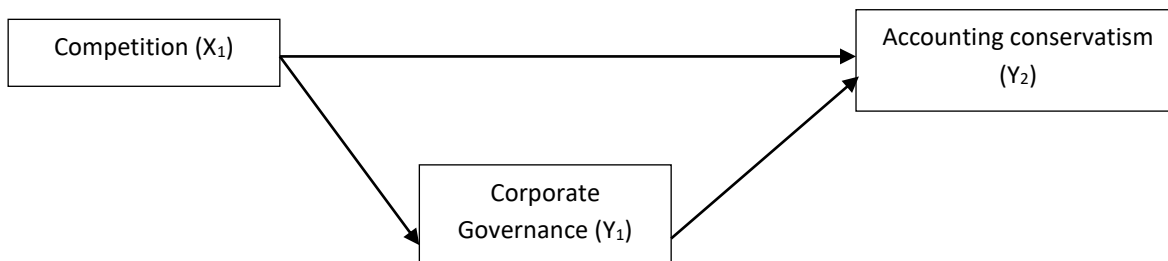


Figure 2. Influence on Accounting Conservatism through Corporate Governance

The regression model implemented in this research is the second path model to describe the partial and simultaneous (exogenous) influence of competition (X1) on accounting conservatism (Y2) through corporate governance (Y2). Assessment is achieved in this research by means of the second path model described in the second path analysis as follows:

Table 3. Second Path Model Hypothesis Testing

Model		Unstandardized Coefficients		Standardized	t	Sig.
		B	std. Error	Coefficients		
1	(Constant)	-2,146	1,855		-1,156	,260
	Competition	8,193	2,232	,537	3,671	,001
	Corporate Governance	-.949	,357	-.389	-2,660	.014

a. Dependent Variable: Accounting Conservatism

Directly

$$Y_2 = 0.537Y_1 + e$$

Indirectly

$$Y_2 = 0.205X_1 - 0.389Y_1 + e$$

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Directly

Competition has a positive effect on accounting conservatism, so that the stronger the competition, the lower the level of accounting conservatism. From table 2, it can be seen that competition has a positive impact on earnings management as indicated by a p calculation of 0.001, which fulfills the requirement that is <0.05 . So with the description above that the competition hypothesis has an effect on accounting conservatism is proven.

Corporate governance has a negative effect on accounting conservatism so that the stronger the corporate governance, the higher the accounting conservatism. Table 2, it can be seen that competition has a negative impact on accounting conservatism with a p calculation of 0.014, which fulfills the requirement that is <0.05 . So with the description above that the Corporate governance hypothesis has an effect on accounting conservatism is proven.

Directly, indirectly

Competition has an indirect effect on accounting conservatism through corporate governance. Table 2 can be seen the indirect effect of competition on accounting conservatism through corporate governance (corporate governance) of 0.205 (0.527×0.389). The direct effect of competition on accounting conservatism is 0.537 and the total effect is 0.742 ($0.205 + 0.537$). The results prove that the direct effect $<$ total effect ($0.537 < 0.742$), so that competition has an effect on accounting conservatism through corporate governance (strengthened by the calculation of the Sobel test). Thus the competition hypothesis has an indirect effect on accounting conservatism through corporate governance.

V. DISCUSSION

A. The influence of competition on corporate governance

Competition has a negative effect on corporate governance, meaning that if the level of competition is in a monopoly market (low level of competition), then companies implementing corporate governance will increase. The research results are supported by research by Chou et al., (2011) which illustrates that the lower the competition, the better the level of corporate governance. The level of competition for banks in Indonesia is controlled by a few banks with a large market share. Large banks already dominate the market or the level of competition at the level of large banks is low because people tend to choose large banks over small banks because their level of governance or supervision is better than small banks so they win the competition.

B. The influence of corporate governance on accounting conservatism.

Corporate governance has a negative effect on accounting conservatism, meaning that corporate governance is tighter, the influence of the level of accounting conservatism policy in a company or corporation is increased. The results of this study are in accordance with the research by Nasr and Ntim, (2018), Ahmed and Dueliman, (2007), Lara et al., (2007) and Prabaningrat et al., (2015) stating that there is a positive relationship between corporate governance and accounting conservatism. The implementation of corporate governance carried out by the company, where the competition is getting higher will still be the attitude of the company's level of prudence because the industrial environment studied is a bank that is categorized as book 4 where the big bank is, where the bank is always seen by many parties. So that banks at book 4 level have good governance and always act cautiously.

C. The influence of competition on accounting conservatism.

Competition has a positive effect on accounting conservatism, meaning that the more the market is in perfect competition, the less the application of accounting conservatism measures. The results of this research are supported by research by Dhaliwal et al., (2008) which states that the level of competition influences companies in implementing accounting conservatism policies. The conventional view relating to competition is the competition fragility view, the higher level of competition that occurs in a market will reduce the ability for companies to gain or make profits, thus encouraging a company to take large risks (careless attitude) in an effort to increase profit or company profits (Wibowo and Siantoro, 2018).

D. Competition influences accounting conservatism through corporate governance

Competition influences accounting conservatism through corporate governance. Competition in a banking industry, especially banks in book 4 (big categorized banks) is a monopoly market competition where the level of market competition is relatively low. Large banks are usually very good at implementing corporate governance because they are given more attention or supervision by the government or third parties than small banks (Setiawati and Na'im, 2001). Where the implementation of good governance can be seen with the better implementation of accounting conservatism by way of being prudent in managing the company.

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VI. CONCLUSION

Competition in the banking industry, especially in banks with book category 4, is at the level of monopoly competition. With a relatively low level of competition, it does not affect corporate governance to implement aggressive strategies (not being careful in looking for customers), so the prudent attitude in banks, especially book 4, is good, in other words, the application of accounting conservatism is good by way of a prudent attitude. Be careful in managing the company. The contribution of this research is that this research contradicts the conventional view related to competition, namely as a competition fragility view, the higher level of competition that occurs in a market will reduce the company's ability to gain or make profits, thereby encouraging a company to take large risks (attitude). not being careful) in an effort to increase profits or company profits (Wibowo and Siantoro, 2018).

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