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DETERMINANTS OF COMPANY PROFIT QUALITY BASED ON CONSERVATIVE ACCOUNTING PRACTICE FACTORS

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Abstrak

Tujuan penelitian ini adalah untuk menguji hubungan antara praktik akuntansi konservatif dan kualitas laba pada perusahaan manufaktur yang terdaftar di Bursa Efek Indonesia (BEI) selama periode 2021–2024. Dalam model penelitian, praktik akuntansi konservatif didefinisikan sebagai variabel independen, sedangkan kualitas laba sebagai variabel dependen. Penelitian ini menggunakan sampel sebanyak 57 perusahaan manufaktur selama periode empat tahun, sehingga diperoleh 228 data observasi. Data yang digunakan merupakan data sekunder dengan teknik pengambilan sampel menggunakan metode purposive sampling. Proses analisis dilakukan menggunakan regresi linier sederhana dengan tingkat signifikansi sebesar 5%. Hasil pengujian hipotesis menunjukkan bahwa praktik akuntansi konservatif berpengaruh signifikan terhadap kualitas laba, dengan kontribusi sebesar 2,7%.

Kata kunci: Akuntansi Konservatif, Kualitas Laba, Bursa Efek Indonesia

Abstract

The purpose of this study is to examine the relationship between conservative accounting practices and earnings quality in manufacturing companies listed on the Indonesia Stock Exchange (IDX)

for the 2021–2024 period. In the research model, conservative accounting practices are defined as the independent variable and earnings quality as the dependent variable. This study used a sample of 57 manufacturing companies over a four-year period, resulting in 228 observational data. The data used were secondary data, with purposive sampling as the sampling technique. The analysis process was conducted using simple linear regression at a 5% significance level. Hypothesis testing indicated that conservative accounting practices significantly influenced earnings quality, contributing 2.7%.

Keywords: Conservative Accounting, Earnings Quality, Indonesian Stock Exchange

INTRODUCTION

High net income quality indicates a company's performance is at a good level from an earnings quality perspective (Maulia & Handojo, 2022). Financial statement users prioritize net income quality and the overall quality of financial information, both in relation to contractual agreements and investment decisions (Maulia & Handojo, 2022). Earnings quality itself is an essential topic and a focus for exploration in the accounting realm (Kepramareni et al., 2021). Among the various explanations of the concept of the degree of accuracy of net income, surplus earnings relate to the ability to accurately project future company performance (Dewi Retno Mumtaz & Suwarno Suwarno, 2024). Within the context of agency theory, which underlies corporate dynamics, conflicts of interest between owners (principals) and managers (agents) often trigger information asymmetry and agency costs (Purba Br, 2023). In order to minimize these conflicts and reduce information asymmetry, the presentation of transparent and reliable financial reports is an absolute requirement for management (Purba Br, 2023).

One of the financial reporting principles that serves to maintain the accuracy and quality of earnings information is the principle of accounting conservatism, which refers to a cautious attitude in facing uncertain economic situations (Beritalima.com, 2017). Conservatism is defined as a form of protection of accounting information against uncertain conditions in the future, where revenue or profits are only recognized when they have actually been realized, while losses are recorded immediately when there is an indication (Savitri, 2016). The importance of implementing this principle is reinforced by the phenomenon of the PT Cakra Mineral Tbk (CKRA) case which was suspected of being involved in financial statement manipulation, claims of ownership of fictitious subsidiaries in PT Murui and PT Takaras, and the use of illegal zirconium mining

products that did not have clear and clean (C&C) status (Beritalima.com, 2017). These acts of financial information manipulation clearly contradict the essence of conservative accounting, resulting in misleading financial statements, creating significant losses for investors such as Cedrus Investments Ltd., and substantially degrading the quality of the company's net income (Beritalima.com, 2017). This case confirms that conservative accounting practices are not merely a technical accounting issue, but also concern ethics, governance, and stakeholder protection, especially in the manufacturing industry which is vulnerable to market pressure and potential internal manipulation (Beritalima.com, 2017).

Several previous studies have examined the relationship between the application of the prudential principle and earnings quality. An academic review by Mulyani (2024) revealed that accounting conservatism and leverage have a beneficial impact on the stability of the profit value of manufacturing entities. Consistent with this, research conducted by Tumirin (2024) demonstrated that accounting conservatism significantly improves earnings quality by reducing management's discretion to manipulate financial statements in companies listed on the Indonesia Stock Exchange (IDX). Furthermore, Jao and Ho (2019) demonstrated that the application of accounting conservatism elicits a positive response from investors regarding reported earnings because it reflects good ownership governance. Further empirical support is provided by Maulia and Handojo (2022), Sugianto and Sjarief (2018), and Putri and Hasanah (2023), who consistently state that higher levels of accounting conservatism are positively correlated with increased financial statement transparency, reduced earnings volatility, and limited scope for earnings management, ultimately increasing the reliability of a company's value in the stock market.

Although the direct relationship between accounting conservatism and earnings quality has been extensively researched, most previous studies still suffer from limitations that create a research gap and also emphasize the scientific novelty of this article. Previous studies, such as those by Mulyani (2024) and Tumirin (2024), are generally limited to a corporate internal structural approach and fail to differentiate the influence of conservatism in depth based on the specific characteristics of industrial sectors with different financial risk profiles. Furthermore, many previous research models are general in nature without controlling for macro-environmental variables or focus solely on short-term relationships. This article offers scientific novelty by conducting empirical testing that focuses specifically on basic materials manufacturing companies listed on the Indonesia Stock Exchange for the most recent period, 2021-2024. The basic materials

sector was chosen due to its significant strategic role in the domestic economic structure and its industry characteristics, which are rife with cost fluctuations and high fixed asset investment (capital intensity), thus requiring a much stricter level of accounting prudence. Through this more homogeneous and contextual scope limitation, this article is expected to present a sharper and more comprehensive analysis of how the precautionary principle responds to the specific uncertainties of the industrial sector.

Based on the background of the problem and the affirmation of scientific novelty above, the problem formulation in this study is the extent of the implications of conservative accounting practices on the quality of entity earnings. In line with this formulation, the main objective or purpose of writing this article is to uncover, understand, and collect valid empirical evidence regarding the influence of conservative accounting practices on the quality of company earnings, specifically in the basic materials sector manufacturing companies listed on the Indonesia Stock Exchange. The results of this study are expected to provide theoretical contributions in enriching the literature on financial accounting and agency theory, as well as provide practical benefits for investors, auditors, and regulators in evaluating and testing the quality of financial reporting in the Indonesian capital market.

Based on this, this study focuses on manufacturing companies listed on the Indonesia Stock Exchange for the 2021–2024 period to examine the effect of accounting conservatism on earnings quality.

RESEARCH METHOD

This study applies a quantitative approach with an associative descriptive design that aims to test, explain, and measure the degree of relationship and causal influence between independent variables on the dependent variable (Sugiyono, 2020). The object of this study focuses on conservative accounting practices as the independent variable, while the quality of corporate earnings is placed as the dependent variable (Sugiyono, 2020). To operationalize the independent variables, conservative accounting practices are measured using an accrual-based proxy, namely the earnings-based measure model. The mathematical format of the measurement separates the formula on a separate line and is presented as follows:

$$C_{it} = (IN_{it} - CFO_{it} \times (-1)) / TA_{it}$$

The description of the formula is $C_{it}$is the accrual value that shows the level of conservatism

of company i in year t. NI component$_{it}$represents Net Income before extraordinary items plus depreciation and amortization of company i in year t. CFO$_{it}$ reflects the operational cash flow of company i in year t. Meanwhile, TA$_{it}$indicates the total value of all assets owned by company i in year t.

On the other hand, the dependent variable, earnings quality, is operationalized by measuring the ratio of operating cash flow to the company's net income. Using a mathematical format with separate rows, this earnings quality assessment is written as follows:

EQ = (Operating Activity Cash Flow / Net Income) × 100%

The explanation for the formula above is that EQ (Earnings Quality) indicates a company's earnings quality score. The higher the ratio resulting from comparing operating cash flow to net income, the higher the quality of reported earnings and the better it represents the true condition of the business entity.

The population in this study includes all manufacturing companies officially listed on the Indonesia Stock Exchange (IDX) (Sugiyono, 2020). Based on the sampling criteria established using the purposive sampling method, the locus of observation was narrowed and focused specifically on issuers in the basic materials sector over a four-year observation period, namely from 2021 to 2024 (Sugiyono, 2020). The type of data used in this study is entirely quantitative secondary data in the form of figures from audited annual financial reports and stock performance summaries officially published by the IDX through the corporate electronic data system (Sugiyono, 2020). The data collection procedure was carried out through documentation techniques, namely by downloading, classifying, and recording data on profit components, total accruals, total assets, and related control variables from the financial reports of basic materials sector entities that met the sample criteria (Sugiyono, 2020).

All collected quantitative empirical data were first tested for validity and construct reliability to ensure data accuracy and consistency before further modeling (Sugiyono, 2020). Because this study used secondary data, the validity test was aimed at ensuring the correspondence between the actual conditions of the research object and the accuracy of the financial report indicators collected by the researcher (Sugiyono, 2020). Furthermore, the data analysis method used to solve the research problem formulation was simple linear regression analysis, considering that this study focused on testing the single effect of one independent variable on one dependent variable (Sugiyono, 2020). The mathematical model format for the regression is presented separately in the

following line:

$$Y = a + bX$$

The explanation of the regression formula above is that Y represents the dependent variable of the company's earnings quality, a represents the constant value, b is the value of the regression direction coefficient, while X reflects the conservative accounting practice value index from the measurement results of the independent variable (Sugiyono, 2020).

Before the linear regression model can be scientifically interpreted, a series of classical assumption tests must be met to ensure the model's feasibility, which is the Best Linear Unbiased Estimator (BLUE). The classical assumption tests applied in this study include a normality test to check whether the model's residuals are normally distributed, a heteroscedasticity test to ensure equality of variance from one observation to another, and an autocorrelation test to identify the absence of correlation between confounding errors in period t and the previous period (Sugiyono, 2020). After the classical assumption tests are met, the variable contribution is evaluated through a coefficient of determination (R^2) analysis to measure how much of the variation in changes in earnings quality can be simultaneously explained by variations in conservative accounting practices (Sugiyono, 2020). The closer the number is to one, the higher the model's predictive ability (Sugiyono, 2020).

The final stage of this methodology is to conduct hypothesis testing to draw statistically valid causal conclusions. Hypothesis testing is conducted by referring to the significance value (Sig.) generated from the processed regression model with a confidence level of 95% or a five percent alpha significance limit ($\alpha = 0.05$) (Sugiyono, 2020). The statistical decision-making criteria are set as follows: if the Sig. value <0.05, then the alternative hypothesis (H_1) is accepted, which means there is a significant influence of accounting conservatism practices on the quality of company earnings (Sugiyono, 2020). Conversely, if the Sig. value ≥ 0.05, then the null hypothesis (H_0) is accepted, indicating that there is no significant influence of accounting conservatism practices on the quality of company earnings in the basic materials sector (Sugiyono, 2020).

RESULTS AND DISCUSSION

This study examines the effect of conservative accounting practices on earnings quality in 57 basic materials manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the 2021–2024 period, with a total of 228 observations after purposive sampling. The data were

analyzed using simple linear regression with a pooled Ordinary Least Squares (OLS) approach to test the research hypotheses.

Descriptive statistical analysis was conducted to determine the characteristics of the research data, including the minimum, maximum, average and standard deviation values, which are summarized in Table 1.

Tabel 1 Descriptive Statistics Result

Variables	N	Minimum	Maximum	Mean	Std. Deviation
Conservative Accounting	228	-1,22	0,32	-0,0063	0,14457
Earnings Quality	228	-141,60	63,21	0,1327	14,00225

The Conservative Accounting Practices variable has a mean of -0.0063 with a standard deviation of 0.14457, indicating that the sample generally applies reporting principles that tend to be neutral to slightly conservative in a homogeneous manner. The Company's Earnings Quality variable has a mean of 0.1327 with a high standard deviation value (14.00225), indicating wide variability and distribution of earnings quality data among sample companies.

Before hypothesis testing, the regression model has been declared to have passed the classical assumption test as follows:

1. Normality Test: The Kolmogorov-Smirnov method produces an Asymp. Sig. (2-tailed) value of 0.200 (> 0.05), confirming that the data is normally distributed.
2. Heteroscedasticity Test: The Glejser test produces a significance value of 0.149 (> 0.05), indicating that the model is free from heteroscedasticity problems.
3. Autocorrelation Test: The Durbin-Watson (DW) value of 1.958 meets the criteria for no autocorrelation.
4. Linearity Test: The significance value of Linearity is 0.048 (< 0.05) and Deviation from Linearity is 1.000 (> 0.05) confirming the appropriate linear model.

Testing the impact of independent variables on dependent variables is carried out through simple linear regression analysis with the following mathematical formulation:

$$Y = a + bX$$

Description: Y represents Earnings Quality, a is a constant, b is the regression coefficient, and X represents Conservative Accounting Practices. The results of the regression parameter estimation are summarized in Table 2.

Tabel 2 Regression Analysis and Hypothesis Testing Result

Variables	Unstandardized Coefficients (B)	Std. Error	t	Say.	Information
(Constant)	0,032	0,917	0,035	0,972	Not Significant
Conservative Accounting	-16,005	6,354	-2,519	0,012	Significant Negative
R Square	0,027				

Based on Table 2, the empirical equation model obtained is:

$$Y = 0.032 - 16.005X$$

The constant of 0.032 is considered statistically insignificant ($p > 0.05$). Meanwhile, the regression coefficient for the Conservative Accounting Practices variable is negative at -16.005 with a t-value of -2.519 and a significance level of 0.012 (< 0.05). These results demonstrate that Conservative Accounting Practices have a negative and significant effect on corporate earnings quality.

The results of the determination coefficient test show an R Square value of 0.027. This figure indicates that the Conservative Accounting Practices variable is only able to explain 2.7% of the variation in the Company's Earnings Quality, while the remaining 97.3% of the variation is determined by other factors outside the model. The empirical findings of the study indicate that the direction of the influence between conservative accounting on earnings quality is negative and significant. This result reflects a scientific paradox in financial reporting. Theoretically, the principle of conservatism emphasizes the acceleration of recognition of potential losses/expenses and the delay in recognizing revenue until it is realized for the sake of prudence. However, intensive implementation in manufacturing companies in the basic materials sector in Indonesia has actually had a counterproductive impact on the quality of earnings information.

This negative trend occurs because delayed revenue recognition and accelerated costs create operational timing differences that trigger distortions in earnings volatility from year to year. Consequently, the predictive value and consistency of earnings information, crucial elements in assessing earnings quality, decline technically. Furthermore, this phenomenon indicates a tendency

for management to opportunistically utilize conservatism to smooth earnings or create hidden reserves (cookie-jar reserves) to manipulate financial performance if not balanced by strong corporate governance. Although technically, accounting practices reduce the quality of earnings stability, these principles still provide strategic value for external investor protection by minimizing excessive management optimism and substantially increasing the transparency of financial reporting.

This significant negative finding is consistent with and reinforces empirical studies by Magdalena and Trisnawati (2022) and Zagita and Bangun (2020), which state that accounting conservatism reduces earnings quality when applied strategically or disproportionately. Magdalena and Trisnawati's (2022) study also demonstrated that the inclusion of multiple independent variables still results in a low determination value. This confirms that the low R-square value (2.7%) in this study is driven by the inherent characteristics of the conservatism variable itself, not the limited number of variables. These results also align with Rosalim (2022), who identified that high levels of conservatism, measured through an accrual-based approach, tend to degrade the quality of earnings information by increasing the discretionary accrual component.

Given the model's limited explanatory power (R Square = 2.7%), this study contributes as a pure baseline for the influence of conservatism. Future research is recommended to develop a more comprehensive multivariate predictive model by integrating governance and operational variables, such as internal audit effectiveness, ownership structure, corporate governance mechanisms, firm size, profitability, and the influence of industry regulations.

CONCLUSION

This study provides empirical evidence that conservative accounting practices significantly influence the earnings quality of basic materials manufacturing companies listed on the Indonesia Stock Exchange for the 2021–2024 period. The analysis results indicate a negative effect, where higher conservatism tends to decrease reported earnings quality. However, the contribution of conservatism to earnings quality variation is relatively small, with a coefficient of determination of 2.7%. This finding confirms that earnings quality is a complex variable influenced by many factors beyond accounting conservatism, such as corporate governance, audit quality, ownership structure, and earnings management practices. Therefore, company management is advised to apply conservatism proportionally and contextually to ensure that financial reports reflect actual

economic conditions and are informative for stakeholders. Furthermore, investors and external parties are expected to consider underlying accounting policies rather than solely based on earnings figures to more accurately assess earnings quality. For future research, it is recommended to use a multivariate model that includes control variables such as corporate governance, company size, and industry characteristics to gain a more comprehensive understanding of the determinants of earnings quality.

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