Debt, State-owned Enterprise, and Accounting Conservatism: Indonesia Evidence

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Abstract: This research aims to empirically examine the effects of public debt ownership and state ownership on the level of corporate conservatism in Indonesia. More specifically, this study will examine whether: (1) the level of conservatism of companies that have public debt will be higher than companies that only have private debt; (2) conservatism of state-owned enterprise (SOE) will be lower than non-SOE companies, and (3) conservatism of SOEs that have public debt will be higher than SOEs that do not have public debt. The examination is done using two ways, market-price based and accrual-based. Both of these methods are used to mitigate the bias of results due to the inefficient nature of the market. The test results show that accrual-based measurements are better at explaining conservatism in an inefficient market such in Indonesia. Accrual-based test results show that: (1) conservatism of companies that have public debt (bonds) is higher than companies that only have private debt; (2) SOE conservatism is lower than non-SOE, and (3) conservatism of SOE that have public debt is lower than SOEs that do not have public debt. The low level of SOE conservatism is presumably due to the assumption that there is protection from the government, weak public demand for SOE conservatism, and the absence of regulations that encourage the practice of high conservatism in SOE.

1 INTRODUCTION

The predicted total bond issuance in Indonesia for 2017 is IDR.119.6 trillion (Gumelar, 2017). This value is smaller than the corporate credit provided by a state-owned bank in one quarter (BRI recorded that it had disbursed credit of Rp. 182.1 trillion in the first quarter of 2017 (Permana, 2017)). This shows that in Indonesia, there are still very few companies that issue bonds. According to IDX Book Fact 2016, there are 104 companies that have issued bonds, and 62 of them are public companies. Compared to the total issuers listed on the Indonesia Stock Exchange, the number of issuers issuing bonds is only 12% (62 out of 533 issuers). So, it is interesting to examine whether there are differences in characteristics between companies that issue bonds and those that do not issue bonds.

Bharath et al. (2008) have found evidence that companies that have poor accounting quality tend to prefer private debt (bank debt) over public debt (bonds). This is consistent with the statement that banks have superior information access and have the ability to reduce adverse selection costs from borrowers. In contrast to bonds, bondholders do not have access to company internal information and also do not have the ability to monitor and control the company. So that bondholders need information on timely loss recognition is higher than banks or other private lenders (Nikolaev, 2010). Referring to Basu (1997), the more time the company recognizes losses, the more conservative the company is called. Because corporate conservatism arises because of requests from *lenders,* this conservatism is called *conditional conservatism.*

In companies with state ownership, the position of the manager or leader is often related to politics or social reputation. To improve their social and political reputation, managers will focus on short-term performance (Cullinan et al., 2012). So it is suspected that managers will tend to do aggressive accounting practices, which are faster in recognizing good news than bad (not conservative) news. Plus, the research results of Faccio et al. (2006) found that companies that have political relations are more often saved when bankruptcy (bailed out) than companies that do not have political relations. Then the incentives of state-owned companies to engage in

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conservative practices will be lower. This is consistent with the results of the study of Chen et al. (2010), who found that state-owned companies in China had a lower level of conservatism than private companies.

Based on the background above, this research aims to empirically test whether there are differences in conservatism between companies that have public debt (bonds) and companies that only have private debt (do not have bonds). This research is also wanted to test the effect of the ownership of the state of the accounting conservatism to see: (1) differences in conservatism among state-owned enterprises (SOEs) and non-state enterprises, and (2) differences in the conservatism of SOEs that have bonds and those that do not.

To the author's knowledge, there has been no research comparing the conservatism of companies that have public debt with those that only have private debt. Previous studies have examined conservatism and debt (Beatty et al. (2008), but have not considered the difference in the level of conservatism of companies that have public debt and only those with private debt. In Indonesia, also no one has examined the effect of state ownership on accounting conservatism. Research on conservatism in Indonesia has examined the relationship between conservatism and conflict of *bondholders-shareholders* (Dahlia, 2004), corporate governance (Ward (2008), Weku (2013), Hendro and Ward (2015), Kartika et al. (2015)), quality of financial report (Fanani (2009), Haniati and Fitriany (2010), Mutmainnah and Wardhani (2013), and Irwanto (2015)), and *corporate social responsibility disclosure* (Anis and Utama, 2016).

Previous conservatism research in Indonesia measured conservatism only in terms of the recognition of bad news (Weku, 2013), or of the total value of conservatism. Both the total value of accounting-based conservatism, namely the value of accruals (Sari (2004), Haniati and Fitriany (2010), Mutmainnah and Wardhani (2013), Irwanto (2015), Kartika et al. (2015), Anis and Utama (2016)), as well as market-based measures, namely the comparative market value and a book value of the company (Fanani, 2009), or both (Wardhani (2008), Hendro and Wardhani (2015).

This research has three contributions. First, this study seeks to provide evidence of differences in the level of conservatism between companies that have public debt (bonds), and companies that only have private debt (banks). Second, this research is trying to provide evidence of the influence of state ownership over the different levels of conservatism companies. Third, this research will measure conservatism both from delaying the recognition of good news and from the timeliness of recognition of bad news.

The first test of this study uses a conservatism measure developed by Khan and Watts (2009). In the operationalization of variables, conservatism Khan and Watts (2009) use the value of *return*; this is done with the assumption that the capital market in Indonesia is efficient. To avoid the possibility of bias in the result caused by inefficient capital markets in Indonesia, this study also tested using an accrual-based conservatism model developed by Ball and Shivakumar (2005).

Furthermore, this study will describe the literature review and hypothesis formulation, describe the data sources and empirical models, and discuss the test results using both the market price based model and the accrual-based model. Finally, the conclusions and implications of this study will be conveyed.

2 LITERATURE STUDY AND HYPOTHESIS DEVELOPMENT

2.1 Efficient Contract Theory and Conservatism

Efficient contract theory views the company as organizing itself in the most efficient way, so as to maximize the likelihood of the company to survive (Scott, 2015). This theory studies the role of accounting information in moderating information asymmetry on contracting parties, resulting in efficient contracts and stewardship.

Debt contracts are an essential source of funding for companies. In a debt contract, there are two aspects that must be considered. First, management has more information about the company's condition. Lenders are concerned about information asymmetry because management does not share information with them, and chooses accounting policies that can harm the interests of lenders. So, lenders need protection for the possibility of this happening.

Second, *lenders* face payoff asymmetry, where lenders will suffer losses if the company's performance is reduced. But unlike investors, profits from lenders are limited to existing contracts. Thus, lenders will better protect themselves from the possibility of companies failing to pay.

Payoff asymmetry condition is generated demands on conditional conservatism, where lenders want more information on unrealized losses, rather than information on unrealized gains because

information about unrealized losses will be more useful in predicting defaults (Watts, 2003).

Conservatism in accounting is divided into two (Scott, 2015), the conservatism that is unconditional (unconditional conservatism) and conservatism that is conditional (conditional conservatism). A condition is considered unconditional conservatism if the value of the asset at risk is recorded at a value lower than the present value, even though economic gains or losses have not yet occurred for the asset (for example, recognition of R&D costs as an expense) whereas conditional conservatism is a condition where risky assets are recorded at a lower value if a condition has occurred (for example, recording inventories according to which value is lower between acquisition costs and market values). Because conservatism referred to in this study is conservatism arising from requests for debt contracts, what is meant by conservatism in this study is conditional conservatism.

2.2 Debt and Conservatism

Companies can get funding from lenders in two ways, namely through bank loans (private debt) and bonds (public debt). Bharath et al. (2008) have examined whether the quality of corporate accounting influences the choice of companies in choosing funding sources. Bharath et al. (2008) found that companies with low accounting quality preferred funding through private debt (bank debt). This is because banks have more superior access to information owned by the company, compared to the public. Banks also have higher flexibility in managing existing contracts (both in terms of price (interest rate) and non-price (maturity and collateral). So banks have the ability to reduce adverse selection costs from borrowers.

The above advantages are not owned by bondholders. Bondholders do not have access to private information and also do not have the ability to monitor and control the company. Bondholders can only exercise control over prices (interest rates). For this weakness, bondholders need information on timely loss recognition (timely loss recognition) is higher than banks or other private lenders (Nikolaev, 2010). Timely loss recognition can provide more accurate ex-ante information to determine debt prices and more quickly identify possible violations of debt terms based on accounting ratios (Ball and Shivakumar, 2005). The more timely the company recognizes the loss, the company is said to be more conservative (Basu, 1997). Upon this discussion, the researchers suspect the level of conservatism of companies that have bonds will be higher than companies that only have private debt. We, therefore, propose a hypothesis in an alternative form as follows:

H_1: Conservatism of companies that have public debt (bonds) will be higher than the conservatism of companies that only have private debt.

2.3 State Ownership and Conservatism

In companies with state ownership, there are two issues that arise (Cullinan et al., 2012). First, the ultimate owner of the company is the people as taxpayers; this causes the ownership of the company to be very scattered so that the control ability is deficient. Second, managers or company leaders are often appointed directly by the government, not through a recruitment mechanism. Manager positions are often related to politics or social reputation. To improve his social and political reputation, managers will focus on short-term performance. So it is suspected that managers will tend to do aggressive accounting practices, which are faster in recognizing good news than bad (not conservative) news.

When studying lenders' demand for conservatism in China, Chen et al. (2010) found that state-owned companies in China had a lower level of conservatism than private companies. They argue that this happened because lenders were not too worried about the possibility of a decrease in default risk of the state-owned company. This is in accordance with the findings of Faccio et al. (2006), who found that companies that have political relations are more often saved when bankruptcy (bailed out) than companies that do not have political relations. We, therefore, propose a hypothesis in an alternative form as follows:

H_{2a}: Conservatism of state-owned companies is lower than the conservatism of private companies.

If hypothesis one and hypothesis two are proven, then we suspect that the level of conservatism of state-owned companies that issue bonds will be higher than state-owned companies that do not issue bonds. This is due to the great demand for timely loss recognition from bondholders. We, therefore, propose a hypothesis three in an alternative form as follows:

H_{2b}: The conservatism of state-owned companies that issue bonds are higher than the conservatism of state-owned companies that do not issue bonds.

3 RESEARCH METHODS

3.1 Sample

The sample used in this study were all non-financial companies on the Indonesia Stock Exchange (IDX) in 2012-2015. 2012 was chosen as the initial period of observation because Indonesia won an investment grade category from Fitch Ratings on 15 December 2011 and from Moody's Investor Services on 18 January 2012 (Rachman and Pamungkas, 2012).

Observation is limited until 2015 because for the measurement of the tested variables, t-1, and t + 1 data are needed. Therefore, to meet the required data, the companies included in the sample are companies listed on the Indonesia Stock Exchange from 2011-2016.

3.2 Market Price Testing (Khan and Watts, 2009)

3.2.1 Variable Measurement

Accounting Conservatism. The conservatism in this study is defined as how much more time the company recognizes economic losses (lousy news) compared to the recognition of economic benefits (good news). To measure conservatism, this study uses a measure developed by Khan and Watts (2009), which is the total timeliness of news recognition (called CONS) which is the sum of the timeliness of the recognition of good news (called G_Score) and an increase in the timeliness of recognition of bad news (called C_Score).

The measure developed by Khan and Watts (2009) was chosen as a measure of conservatism because it can reflect the time of change in the level of conservatism and variations in conservatism between companies. This consideration is relevant to the conditions in Indonesia, because the time period since Indonesia was ranked as worthy of investment until this research was made relatively short (six years), and the first year the company issued bonds also varied. The use of this measure is done with the assumption that the capital market in Indonesia is efficient.

Following Khan and Watts (2009), to estimate the timeliness of acknowledging good news and conservatism at the company-year level, we specify G_Score each year and C_Score each year as a linear function of the specific characteristics of the company each year:

$$\text{G\_Score} = \mu_1 + \mu_2 Size_i + \mu_3 M/B_i + \mu_4 Lev_i \quad (1)$$

$$\text{C\_Score} = \lambda_1 + \lambda_2 Size_i + \lambda_3 M/B_i + \lambda_4 Lev_i \quad (2)$$

Where *size* is the natural logarithm of the *market value of equity, M / B* is the *market-to-book ratio,* and *Lev* is *leverage* (the amount of long-term debt and short-term debt, divided by the *market value of equity).* The estimator $\mu_1$and λ_1, i = 1-4 are constant for the whole company but are different for each time because this value comes from the annual cross-sectional regression estimation.

Whereas the annual cross-sectional regression model used to estimate C_Score and G_Score is as follows:

$$\begin{aligned} X_i = {} & \beta_1 + \beta_2 D_i + R_i(\mu_1 + \mu_2 Size_i + \mu_3 M/B_i + \\ & \mu_4 Lev_i) + D_i R_i(\lambda_1 + \lambda_2 Size_i + \lambda_3 M/B_i + \\ & \lambda_4 Lev_i) + (\delta_1 Size_i + \delta_2 M/B_i + \delta_3 Lev_i + \\ & \delta_4 D_i Size_i + \delta_5 D_i M/B_i + \delta_6 D_i Lev_i) + \varepsilon_i \end{aligned} \quad (3)$$

Where i is the index for the company, *X* is the value of earnings (net income divided by the value of the market value of equity period t-1), *R* is returned (annual returns are calculated starting from the 4th month after the fiscal year ends), *D* is a dummy variable where is one of the values of *R<0* and 0 if otherwise, and ε is an error.

Company Characteristics. This study will look at the characteristics of the company based on the type of debt and type of company. Related to the type of debt, it will be tested whether the company has public debt (bonds) or not. Give a value of 1 if the company has a Bond, and 0 if not. Regarding the type of company, if the company is an SOE, then the SOE variable will be given a value of 1 and given a value of 0 if otherwise.

Control Variable. We were referring to Khan and Watts (2009) this research also controls the age of the company (Age), the company's uncertainty factor (Volatility), and the company's investment cycle (InvestCycle). The company's age (Age) believed to affect the level of conservatism companies because the younger company, it tends to have more choice of asset placement, rather than the older companies. Information asymmetry between managers and investors will increase in accordance with the company's growth, and future cash flow increases tend to be difficult to verify. This can increase agency costs, so we need a conservatism to reduce agency

problems. The older age of the company is thought to reduce the level of conservatism.

The company's uncertainty factor (Volatility) and the company's investment cycle (InvestCycle) are expected to be positively related to conservatism. This is because these two factors can cause agency costs to increase. The higher the volatility of stock returns and the longer the investment cycle, increasing the difficulty in forecasting the number of future cash flows. It also increases the likelihood of shareholders experiencing losses, and increases the likelihood of experiencing litigation, thereby increasing the demand for conservatism. Volatility is measured using standard deviations from monthly stock returns. And InvestCycle is measured by dividing the value of depreciation expense by the value of lagged assets (the smaller the value of InvestCycle indicates the longer investment cycle).

3.2.2 Research Model

To test Hypothesis 1 and Hypothesis 2a proposed, this study uses the following research model equations:

$$CONS_i = \beta_0 + \beta_1 Bond_i + \beta_2 SOE_i + \beta_3 Age_i + \beta_4 Volatility_i + \beta_5 InvestCycle_i + \varepsilon_{it} \quad (4)$$

Where:
CONS = addition of G_Score and C_Score values.
Bond = dummy variable, given a value of 1 if the company has bonds, and 0 otherwise.
SOE = dummy variable, given a value of 1 if it is an SOE company, and 0 otherwise.
Age = company age .
Volatility = standard deviation of monthly stock returns.
InvestCycle = depreciation expense value divided by the value of lagged assets.

If hypothesis 1 and hypothesis 2a are proven, this research expects β_1 positive and negative values for β_2.

Specifically, for hypothesis 2b, regression testing uses model (5) and only uses SOE companies as samples.

$$CONS_i = \beta_0 + \beta_1 Bond_i + \beta_2 Age_i + \beta_3 Volatility_i + \beta_4 InvestCycle_i + \varepsilon_{it} \quad (5)$$

The description of the variable has been explained in the explanation of the model (4). If hypothesis 2b is proven, this research expects a β_1 positive value.

3.3 Accrual based Testing (Ball and Shivakumar, 2005)

Ball and Shivakumar (2005), based on a model developed by Basu (1997), developed a model that can measure the level of conservatism of private companies. The Ball and Shivakumar (2005) model would be suitable if the research assumes that the capital market in Indonesia is not an efficient market so that not all gains and losses experienced by a company are reflected in the value of the company's stock market price. The Ball and Shivakumar (2005) models referred to are as follows:

$$ACC_{it} = \beta_0 + \beta_1 NEGCFO_{it} + \beta_2 CFO_{it} + \beta_3 NEGCFO * CFO_{it} \quad (6)$$

Where ACC_{it} is the current period's accrual value divided by the market value of the company at the beginning of the period *(* initial *market value of equity* - $MVE_{t-1)}$, CFO_{it} is cash flow from operational activities divided by MVE_{t-1}, and $NEGCFO_{it}$ is dummy variable, which is worth one if the value of *the* CFO_{it} is less than zero.

Ball and Shivakumar (2005) argue that if the influence of cash flows on persistent current news, timely recognition will be the cause of a positive relationship between accruals and current period cash flows. The difference in recognition time between losses and profits caused by conservatism applied by the company, causing a positive relationship between cash flow and accruals, will be more substantial for the recognition of losses rather than profits. In accordance with the hypothesis, Ball and Shivakumar (2005) found a negative correlation between accruals and operating cash flow, current cash flow is negative ($\beta_3 > 0$). While the coefficient β_3 indicates the timeliness of the company recognizing bad news (losses), the coefficient β_2 indicates the timeliness of the company recognizing good news (profit).

3.3.1 Research Model

To test Hypothesis 1 and Hypothesis 2a, using accrual-based conservatism models (Ball and Shivakumar, 2005), the research models tested are as follows:

$$ACC_{it} = \beta_0 + \beta_1 NEGCFO_{it} + \beta_2 CFO_{it} + \beta_3 NEGCFO * CFO_{it} + \beta_4 BOND_{it} + \beta_5 SOE_{it} + \beta_6 SIZE_{it} + \beta_7 NEGCFO * BOND_{it} + \beta_8 CFO * BOND_{it} + \beta_9 NEGCFO * CFO * BOND_{it} + \beta_{10} NEGCFO * SOE_{it} + \beta_{11} CFO * SOE_{it} + \beta_{12} NEGCFO * CFO * SOE_{it} + \beta_{13} NEGCFO * SIZE_{it} + \beta_{14} CFO * SIZE_{it} + \beta_{15} NEGCFO * CFO * SIZE_{it} + \varepsilon_{it} \quad (7)$$

Where:
ACC = current period accrual value.
CFO = cash flow from operational activities.
NEGCFO = dummy variable, which is worth one if the value of *the CFO* is less than zero.
BOND = dummy variable, given a value of 1 if the company issued BOND, and 0 if otherwise.
SOE = dummy variable, given a value of 1 if it is an SOE company, and 0 if otherwise.
SIZE = company size.

If the hypothesis is proven, then this research expects β_9 positive and β_{12} negative values.

Specifically, for hypothesis 2b, regression testing uses model (8) and only uses SOE companies as samples.

$$ACC_{it} = \beta_0 + \beta_1 NEGCFO_{it} + \beta_2 CFO_{it} + \beta_3 NEGCFO * CFO_{it} + \beta_4 BOND_{it} + \beta_5 SIZE_{it} + \beta_6 NEGCFO * BOND_{it} + \beta_7 CFO * BOND_{it} + \beta_8 NEGCFO * CFO * BOND_{it} + \beta_9 NEGCFO * SIZE_{it} + \beta_{10} CFO * SIZE_{it} + \beta_{11} NEGCFO * CFO * SIZE_{it} + \varepsilon_{it} \quad (8)$$

The variable description has been explained in the explanation of the model (7). If the hypothesis is proven, then this research expects a β_8 positive value.

In accordance with Ball and Shivakumar (2005), this study also exerted control over company size *(SIZE)*. The larger size of the company is expected to report losses faster than smaller companies. This is because there is a higher risk of litigation, or because of different types of agency fees. *SIZE* value is obtained from the logarithm of the market value of the company's equity.

3.4 Data Processing

This study uses a *balanced panel* data structure, where the sample is selected based on the completeness of the data and also the sample selection criteria that refer to previous research. The use of a *balanced panel* data structure allows this study to use the FGLS panel data estimator. As for the structure of the model, this research can use the structure of the *collective effect/pooled* model, *fixed effects,* or *random effects.* The choice of model to use depends on the best test results.

Because this study uses the FGLS data estimator, it is no longer relevant to meet classical assumptions (Ekananda, 2016). The FGLS estimation process, although not the minimum value of the variance (not the best - *best)*, is still linear and has an unbiased parameter estimator (linear unbiased estimator).

4 RESEARCH RESULTS AND ANALYSIS

4.1 Sample Selection Results

Table 1: Sample Selection Procedure

Sample Criteria	Number of Companies	Number of observations
Registered on the Indonesian Stock Exchange in 2012 - 2015	549	2,196
Reduced by:		
▪ Data incomplete	(124)	(496)
▪ Included in the financial industry	(70)	(280)
▪ Has no private and/or public debt	(130)	(520)
▪ Has a non-December reporting period end	(5)	(20)
▪ Has a negative asset or negative book value of equity	(8)	(32)
The number of final observations	212	848

Source: processed data

The sample criteria used in this study are as follows: (1) companies listed on the Indonesia Stock Exchange in 2011-2016; (2) has complete data needed; (3) does not include the financial industry; (4) has private and/or public debt; (5) has a book year ending in December; and (6) has no negative asset value or equity book value.

The financial industry is excluded from the sample because of the nature of the composition of financial statements that is different from other industries, so it cannot be compared. A summary of sample selection can be seen in Table 1.

4.2 Descriptive Statistics and Correlation Test

The descriptive statistical analysis aims to provide a simple description of the data and the results of the research conducted. Table 2 panel A shows descriptive statistics for the variables tested using market-based testing. Table 2 panel A shows that the average level of firm conservatism is negative. This is because many sample companies experience negative *returns*. So as an initial guess, the sample company is suspected of having admitted bad news (losses) in a timely manner.

Table 2 panel A also shows that 17% of the sample companies have public debt (bonds), and 5% of the sample companies are state-owned companies. Regarding the age of the company, it can be seen that the age of the sample companies varies significantly from the youngest age of 3 years to the oldest 198 years (Kimia Farma Tbk. Company has been established since the Dutch colonial era) while the value of *volatility* shows that the average monthly *return* of the sample company is worth 0.12. The *Investment Cycle value* of the sample companies also looks very varied, ranging from 0.00 to 10.35, with an average value of 5%.

Whereas for accrual-based testing variables can be seen in Table 2 panel B. The table shows that the average value of the sample company accruals is negative 0.07.

Table 2: Descriptive Statistics for Variables Tested During the Observation Period

Panel A: Market-based testing					
Variable	The mean	Median	Maximum	Minimum	Std. Dev
CONS	-0.77	-0.20	10,43	-12.03	2.46
BOND	.17	0.00	1,00	0.00	0.38
SOE	0.05	0.00	1,00	0.00	0.23
AGE	31.54	29.00	198.00	3.00	19.96
VOLATILITY	0.12	.10	.84	0.00	0.08
INVESTCYCLE	0.05	0.03	10,35	0.00	.36
Panel B: Accrual-based testing					
Variable	The mean	Median	Maximum	Minimum	Std. Dev
ACC	-0.07	-0.02	6.14	-4.81	0.56
NEGCFO	0.22	0.00	1.00	0.00	0.41
CFO	0.13	0.06	6.87	-4.89	0.53
BOND	0.16	0.00	1.00	0.00	0.37
SOE	0.05	0.00	1.00	0.00	0.23
SIZE	28.0 9	27.99	33.37	23.66	1.97

N = 848 observations

CONS = company conservatism level, is the sum of the values of G_Score and C_Score; BOND = 1 if the company has public debt, and zero if otherwise; SOE = value 1 if the company is a state-owned company (SOE), and zero if otherwise: Age = age of the company; VOLATILITY = the level of volatility of the company, is the standard deviation of the monthly *stock return* ; INVESTCYCLE = the company's investment cycle, calculated from the value of depreciation expense divided by the value of *lagged assets.*

ACC = *current accrual* value *;* NEGCFO = value 1 if the value of *CFO is* less than zero, and zero if otherwise, CFO = cash flow from operational activities; BOND = value 1 if the value of the company issues *bonds,* zero if otherwise; SOE = 1 value if the company is a SOE company. SIZE = firm size control variable.

Source: processed data

Table 3: Correlation Test for Variables Tested During the Observation Period (Market-Based Testing)

	CONS	BOND	SOE	AGE	VOLATILITY	INVESTCYCLE
CONS	1.00					
BOND	-0.11	1.00				
SOE	-0.11	0.22	1.00			
AGE	-0.05	0.11	0.43	1.00		
VOLATILITY	-0.01	-0.06	-0.03	-0.05	1.00	
INVESTCYCLE	-0.08	-0.01	-0.01	-0.04	0.07	1.00

N = 848 observations
CONS = company conservatism level, is the sum of the values of G_Score and C_Score; BOND = 1 if the company has public debt, and zero if otherwise; SOE = value 1 if the company is a state-owned enterprise (SOE), and zero if otherwise; Age = company age; VOLATILITY = the level of volatility of the company, is the standard deviation of the monthly *stock return* ; INVESTCYCLE = the company's investment cycle, calculated from the value of depreciation expense divided by the value of *lagged assets.*

Source: processed data

As many as 22% of the sample had a CFO that the company is negative, 16.5% of companies sampled had a bond (*bond*), and the number of state-owned enterprises only 5.6% of the total sample. SIZE data also shows that company size is relatively homogeneous, that is, large companies.

Correlation test results between independent variables based on market price testing can be seen in Table 3. In the table, it appears that each variable tested has a correlation with other tested variables with an average value below 0.5. This indicates that the independent variables tested were free from colinearity problems. For the results of the correlation test, independent variables used in accrual-based testing can be seen in the Appendix.

4.3 Hypothesis Testing

4.3.1 Market-based Testing (Khan and Watts, 2009)

Hypothesis Testing 1 (H_1). The results of the empirical regression model to test whether the conservatism of companies that have public debt (bonds) is higher than the conservatism of companies that only have private debt can be seen in Table 4 section A. The table shows that the value of the *F-statistic* equation has a *Prob. (F-statistic)* which is significant, i.e., 0,000. This shows that the independent variables tested together significantly (α = 1%) affect the dependent variable (*CONS*). Adjusted R-squared of 14,4% means that the number of *CONS* can be explained by the independent variables tested by 14,4%, while the remaining 84.6% is explained by other variables not discussed in this study.

Table 4 section A also shows that companies that issue bonds (have public debt) have lower conservatism than companies that only have private debt. Conservatism is shown by the timely recognition of losses. This can be seen from the value of the *BOND* coefficient, which shows a negative direction with a level of confidence (α = 1%). Despite having significant value, but the test results did not show support for the proposed hypothesis 1 (H_1 rejected).

The *Volatility* and *InvestCycle* coefficients also have a negative and significant direction (as opposed to the prediction direction). This shows that the higher the uncertainty factor and the company's investment cycle was not responded to by the high conservatism practices of the company.

The results that are contrary to the hypotheses and prediction of the proposed direction may occur for several reasons. First, banks or *lenders* of private debt are more stringent in overseeing financial reporting, so companies that only have private debt will be more conservative. Second, there is no demand for conservatism from the public. Referring to the results of Bushman and Piotroski's research (2006), the demand for conservatism is influenced by hereditary and political-economic factors in a country. Bushman and Piotroski's (2006) research using data from La Porta (1999) and La Porta (2003) shows that the legal system and law enforcement in Indonesia tend to below. This has led to low public demand for conservatism in Indonesia. Low demand causes companies to tend to be not conservative.

Table 4: Empirical Model Regression Results Testing Hypothesis 1 and Hypothesis 2a (Market-Based Testing)

Variable	Prediction	CONS					
		A		B		C	
		Coefficient	Prob.	Coefficient	Prob.	Coefficient	Prob.
C	?	-0.086	(0.4830)	-0,225	(0.0807)	-0,159	(0.2088)
BOND	(+)	-0.658	(0.0002) [a]			-0,581	(0, 0008) [a]
SOE	(-)			-0,937	(0, 0138) [b]	-0,818	(0, 0365) [b]
AGE	(+)	-0.003	(0.2911)	-0,001	(0.7051)	-0,000	(0.8472)
VOLATILITY	(+)	-0,937	(0.0649) [c]	-0,749	(0.1491)	-0,871	(0, 0858) [C]
INVESTCYCLE	(+)	-0,576	(0.0000) [a]	-0,570	(0, 0000) [a]	-0,573	(0, 0000) [a]
Adj.R [2]		.144		.144		.150	
F-Stat Prob. (F-Stat)		36,639 (0.0000)		36,639 (0.0000)		38,439 (0.0000)	

N = 848 observations
CONS = company conservatism level, is the sum of the values of G_Score and C_Score; BOND = 1 if the company has public debt, and zero if otherwise; SOE = value 1 if the company is a state-owned enterprise (SOE), and zero if otherwise; Age = company age; VOLATILITY = the level of volatility of the company, is the standard deviation of the monthly stock return; INVESTCYCLE = the company's investment cycle, calculated from the value of depreciation expense divided by the value of lagged assets.
Where: [a] significant 1%; [b] significant 5%; [c] significant 10%

Source: processed data

Third, the use of return value in conservatism measurement *(CONS) is* done with the assumption that the capital market in Indonesia is efficient, where changes in the company's stock market price will reflect all losses and profits experienced by the company. However, if the capital market in Indonesia is not efficient, then this measurement will lead to bias in the test results. To overcome this problem, an alternative conservatism measurement technique will be tested using an accrual-based conservatism measure developed by Ball and Shivakumar (2005).

Hypothesis Testing 2a (H_{2a}). The results of the empirical regression model to test the differences in conservatism between SOE and non-SOE companies can be seen in Table 4 section B. The table shows that the *F-statistic* test results have a significant *Prob. (F-statistic)*, which is 0,000. This shows that the independent variables tested together significantly (α = 1%) affect the dependent variable (*CONS*). The adjusted R-squared value of 14,4% indicates that the *CONS* amount can be explained by the independent variables tested by 14.4%, while the remaining 85.6% is explained by other variables that are not addressed in this study.

Table 4 section B also shows that SOE companies have lower conservatism than private companies. Conservatism is shown by the timely recognition of losses. This can be seen from the value of the coefficient of *SOE,* which shows a negative direction with a level of confidence (α = 5%). The results show support for the proposed hypothesis 2a (H_{2a} received).

Table 4 section C shows the results of regression testing if the characteristics of companies that have bonds and state-owned companies are tested together. The results of joint testing show that the results of testing hypotheses one and 2a are consistent; this can be seen from the value of the *BOND* coefficient *(SOE),* which has a negative direction (positive) and remains significant with a confidence level of 1% (5%).

Hypothesis Testing 2b (H_{2b}). Hypothesis 2b wants to test whether SOE companies that have bonds will have a higher level of conservatism than SOE companies that do not have public debt (bonds) and only have private debt. The test results can be seen in Table 5.

The test results in Table 5 show that the value of the *F-statistic* equation has a *Prob. (F-statistic)* of 0.478. This shows that the model being tested is not a good model. The *adjusted R-squared* also shows the value of -0.0095, meaning that the amount of *CONS* cannot be explained by the independent variables tested. There may be other variables that affect the *CONS* value but have not been considered in this study.

Table 5: Results of Regression Empirical Model Hypothesis Testing 2b (Market-Based Testing)

Variable	Prediction	Coefficient	Prob.
C	?	-0 , 874	0 , 5379
BOND	(+)	0 , 161	0 , 8196
AGE	(+)	0 , 004	0 , 4995
VOLATILITY	(+)	-1 , 804	0 , 8435
INVESTCYCLE	(+)	-29 , 34	0 , 1076
Adj. R-squared			-0.0095
F-Stat. Prob. (F-Stat.)			0.8898 (0.478)
N = 48 observations CONS = company conservatism level, is the sum of the values of G_Score and C_Score; BOND = 1 if the company has public debt, and zero if otherwise; Age = company age; VOLATILITY = the level of volatility of the company, is the standard deviation of the monthly *stock return* ; INVESTCYCLE = the company's investment cycle, calculated from the value of depreciation expense divided by the value of *lagged assets.* Where: [a] significant 1%; [b] significant 5%; [c] significant 10%			

Source: processed data

4.3.2 Accrual based Testing (Ball and Shivakumar, 2005)

Hypothesis Testing 1 (H_1). The results of the empirical model regression equation (7) to test the effect of bond issuance on the level of corporate conservatism can be seen in Table 6 section A. In the table it appears that the amount of adjusted R-squared between models that include control variables, with those that do not include control variables shows that the *adjusted R-squared value* is higher for models that include control variables. This model also has *an adjusted R-squared* is much higher than the hypothesis test 1 that using the model equation (4).

Tests that include control variables show an adjusted R-squared value of 80.8%. This means that the amount of *ACC* can be explained by the independent variables tested by 80.8%, while the remaining 19.2% is explained by other variables not discussed in this study.

Table 6 section A also shows that companies that issue bonds (have public debt) have higher conservatism than companies that only have private debt. Conservatism is shown by the timely recognition of losses. This can be seen from the coefficient of *NEGCFO*CFO*BOND,* which shows a positive direction with a level of confidence (α = 5%), and when entering the control variable, the level of confidence increases to (α = 1%). The results show support for the proposed hypothesis (H_1). The results of this test are the opposite of the results of hypothesis 1, which were tested using equation (4). With a higher adjusted R-squared value, it is assumed that the equation model (7) is better in explaining conservatism in Indonesia.

Although not presented in a hypothesis, the test results in Table 6 section A also show that in addition to the timely recognition of losses, the conservatism of companies that have public debt is also done through delaying the recognition of good news (profits). This can be seen from the coefficient of the variable *CFO*BOND,* which has a negative direction with a significant level of confidence (α = 1%).

Hypothesis Testing 2a (H_{2a}). The results of the empirical regression model to test the differences in conservatism between SOE and non- SOE companies can be seen in Table 6 section B. The table shows that the *F-statistic* test results have a significant *Prob. (F-statistic)*, which is 0,000. This shows that the independent variables tested together significantly (α = 1%) affect the dependent variable (*ACC*). Same with the H_1 test results, the *adjusted R-squared* quantity for the model that includes the control variable shows the *adjusted R-squared value* is higher than the model that does not enter the control variable. The *adjusted R-squared* model value of equation (7) is also higher than the equation model (4).

The test that included the control variable showed an *adjusted R-squared value* of 81.1%. This means that the amount of *ACC* can be explained by the independent variables tested by 81.1%, while the remaining 18.9% is explained by other variables not discussed in this study.

Table 6, part B, also shows that SOE companies have lower conservatism than private companies. Conservatism is shown by the timely recognition of losses. This can be seen from the coefficient of *NEGCFO*CFO*SOE* that shows a negative direction with a level of confidence (α = 5%). But when entering the control variable, this value becomes insignificant. The results showed moderate support for the hypothesis (H_{2a}).

Regarding the recognition of good news (profits), Table 6, section B shows that SOE companies also recognize profits more slowly than private companies. This can be seen from the coefficient of the *CFO*BOND* variable, which has a negative direction with a significance level of confidence (α = 5%) and increases to (α = 1%) when it has entered the control variable.

Table 6 section C shows the results of regression testing if the characteristics of companies that have *bonds* and state-owned companies are tested together. The results of the joint test show that the results of hypothesis 1 testing are consistent because the value of the *NEGCFO*CFO*BOND* coefficient is positive and remains significant with a confidence level of 5% and 1% (if entering control variables). Likewise, with the results of hypothesis 2a, it still looks consistent. Namely, the conservatism value of SOE companies is moderately lower than that of private companies.

Table 6: Empirical Model Regression Results Testing Hypothesis 1 and Hypothesis 2a (Accrual Based Testing)

Variable	Prediction	ACC					
		A		B		C	
C	?	0,002 (0,501)	0,195 (0,000)[a]	0,005 (0,104)	0,152 (0,004)[a]	0,001 (0 ,632)	0,194 (0,000)
NEGCFO	?	0,003 (0,655)	-0,067 (0,660)	0,004 (0,468)	-0,377 (0,003)[a]	0,005 (0 ,501)	-0,079 (0, 606)
CFO	(-)	-0,686 (0,000)[a]	-4,520 (0 ,000)[a]	-0,684 (0,000)[a]	-4,462 (0,000)[a]	-0,686 (0,000)[a]	-4 , 496 (0,000)[a]
NEGCFO*CFO	(+)	-0,400 (0,000)[a]	5,067 (0,000)[a]	-0,379 (0,000)[a]	2,637 (0,003)[a]	-0,399 (0,000)[a]	4 , 978 (0,000) [c]
BOND	?	0,039 (0,000)[a]	0,041 (0,000)[a]			0,036 (0,000)[a]	0,035 (0,000)[a]
NEGCFO*BOND	?	0,033 (0,118)	0,045 (0,123)			0,036 (0,090)[c]	0,050 (0,086) [c]
CFO*BOND	(-)	-0,130 (0,001)[a]	-0,383 (0,000)[a]			-0,115 (0,015)	-0,338 (0,000)[a]
NEGCFO*CFO*BOND	(+)	0,521 (0,040)[b]	0,979 (0,000)[a]			0,612 (0,026)[b]	1,026 (0,000)[a]
SOE	?			0,029 (0,000)[a]	0,029 (0,005)[a]	0,028 (0,044)[b]	0 ,035 (0,029)[b]
NEGCFO*SOE	?			-0,216 (0,001)[a]	-0,230 (0,000)[a]	-0,215 (0,006)[c]	-0 ,205 (0,008)[a]
CFO*SOE	(+)			-0,086 (0,067)[c]	-0,292 (0,020)[b]	-0,120 (0,240)	-0,245 (0 ,161)
NEGCFO*CFO*SOE	(-)			-0,678 (0,018)[b]	-0,540 (0,167)	-0,917 (0,038)[b]	-0 ,715 (0,172)
SIZE	?		-0,007 (0,000)		-0,005 (0,003)[a]		-0,007 (0,002) [a]
NEGCFO * SIZE	?		0,002 (0,637)		0,014 (0,002)[a]		0,003 (0,577)
CFO * SIZE	?		0,144 (0,000)		0,141 (0,000)[a]		0,143 (0,000)[a]
NEGCFO * CFO * SIZE	?		-0,206 (0,000)		-0,112 (0,001)[a]		-0,203 (0,000)[a]
Adj.R [2]		0,796	0,808	0 ,794	0,811	0,796	0,807
F-Stat Prob. (F-Stat)		474,899 (0,000)	325,997 (0,000)	467,145 (0,000)	332,226 (0 ,000)	303,051 (0,000)	236,546 (0,000)

N = 848 observations
ACC = current accrual value *;* NEGCFO = value 1 if the value of *CFO* is less than zero, and zero if otherwise, CFO = cash flow from operational activities; BOND = value 1 if the value of the company issues bonds*,* zero if otherwise; SOE = 1 value if the company is a SOE company. SIZE = firm size control variable.
Where: [a] significant 1%; [b] significant 5%; [c] significant 10%

Source: processed data

Hypothesis Testing 2b (H_{2b}). Hypothesis 2b wants to test whether SEO companies that have bonds will have a higher level of conservatism than SOE companies that do not have public debt (bonds) and only have private debt. The test results can be seen in Table 7.

The test results in Table 7 show that the value of the *F-statistic* equation has a significant *Prob. (F-statistic)*, which is 0,000. This shows that the independent variables tested together significantly (α = 1%) affect the dependent variable (*ACC*). However, the amount of *adjusted R-squared* between models that include a control variable, and those that do not include a control variable indicates that the *adjusted R-squared value* is higher for models that do not include a control variable. Tests that did not include a control variable showed an *adjusted R-squared value* of 46.4%. This means that the amount of *ACC* can be explained by the independent variables tested by 46.4%, while the remaining 53.6% is explained by other variables not discussed in this study.

Table 7 also shows that SOE companies that issue bonds have a lower level of conservatism than SOE companies that do not have public debt and only have private debt. This can be seen from the coefficient of the NEGCFO*CFO*BOND variable, which is harmful and significant, with a level of confidence (α = 1%). Therefore, hypothesis 2b is rejected.

The higher level of conservatism of state-owned companies issuing public debt compared to only having private debt, allegedly due to weak demand for conservatism in Indonesia. In accordance with the results of Bushman and Piotroski's research (2006), the demand for conservatism is influenced by hereditary and political-economic factors in a country. The research of Bushman and Piotroski (2006) states that the legal system (civil law) and the level of law enforcement in Indonesia are weak. Therefore the demand for conservatism in Indonesia is also weak.

Considering the results of the study of Chen et al. (2010) where state-owned companies will have deep conservatism due to government guarantees, and the results of Bushman and Piotroski's research (2006) which show that demand for conservatism in Indonesia is low, then the low level of conservatism offered by state-owned companies that have public debt will be included reason. The public prefers high returns from SOE companies, so SOE companies do not need to be conservative.

SOE Minister's Decree No. KEP-100/MBU/2002, regarding the assessment of the health rate of SOE, also shows that there are no indicators for evaluating the health rate of SOE for financial aspects that consider the company's ability to pay its debts. The highest weighting indicator for the financial aspect is the return to shareholders/Return on Equity (ROE), followed by the return on investment (ROI). This further weakens management's incentives to conduct conservative financial reporting practices,

Table 7: Results of Regression Empirical Model Hypothesis Testing 2b (Accrual Based Testing)

Variable	Prediction	ACC			
		Coef.	Prob.	Coef.	Prob.
C	?	0,061	0,179	-0,413	0,644
NEGCFO	?	-0,072	0,496	6,240	0,160
CFO	(-)	-1,152	0,003	2,770	0,643
NEGCFO*CFO	(+)	1,166	0,254	33,550	0,363
BOND	?	-0,040	0,499	-0,054	0,392
NEGCFO*BOND	?	-0,457	0,010	-0,332	0,087
CFO*BOND	(-)	0,538	0,252	0,757	0,195
NEGCFO*CFO*BOND	(+)	-3,304	0,006[a]	-3,642	0,009[a]
SIZE				0,016	0,590
NEGCFO*SIZE				-0,213	0,156
CFO*SIZE				-0,135	0,509
NEGCFO*CFO*SIZE				-1,080	0,390
Adj.R [2]		0,464		0,457	
F-Stat		6,832	(0,000)	4,602	(0,000)

N = 48 observations
ACC = *current accrual* value *;* NEGCFO = value 1 if the value of *CFO is* less than zero, and zero if other, CFO = cash flow from operational activities; BOND = value 1 if the value of the company issues *bonds,* zero if other; SIZE = firm size control variable.
Where: [a] significant 1%; [b] significant 5%; [c] significant 10%

Source: processed data

And can encourage aggressive financial reporting practices.

5 CONCLUSIONS

This research aims to empirically test whether there are differences in conservatism between companies that have public debt (bonds) and companies that only have private debt (do not have bonds). This study also wants to examine the effect of state ownership on accounting conservatism by looking at: (1) differences in conservatism between state-owned (SOE) and non-SOE companies, and (2) differences in SOE conservatism with bonds and non-bonds.

This research has three contributions. First, this study seeks to provide evidence of differences in the level of conservatism between companies that have public debt (bonds), and companies that only have private debt (banks). Second, this study seeks to provide evidence of the influence of state ownership on differences in the level of corporate conservatism. Third, this research will measure conservatism both from delaying the recognition of good news and from the timeliness of recognition of bad news.

In testing, this study uses two ways, namely market-based testing (Khan and Watts, 2009) and accrual-based testing (Ball and Shivakumar, 2005). Two methods are used because of concerns the capital market in Indonesia is not efficient.

The results of the two types of tests above give inconclusive results. The results of accrual-based testing (Ball and Shivakumar, 2005) show that the *adjusted R-squared value* is much higher than the results of market-based testing. This shows that the variables tested in the accrual-based model can explain conservatism in Indonesia better than the use of market-based models. Henceforth the conclusions of this study will be submitted based on the results of accrual-based testing.

The test results show that hypothesis 1 is accepted (conservatism of companies that have public debt is higher than companies that only have private debt). Hypothesis 2a is accepted moderately (because when entering the control variable, the coefficient value tested becomes insignificant). And hypothesis 2b is rejected (conservatism of SOEs that issue public debt, lower than SOE companies that do not have public debt).

The moderate acceptance of hypothesis 2a and the rejection of hypothesis 2b allegedly because the public strongly believes that the government will guarantee or provide support to SOEs so that SOE companies do not really need conservatism.

The implication of the research shows that the existence of bonds shows that the company will be more conservative, but if the issuing of bonds is an SOE company, the issue of conservatism is not so important. This is due to the possibility of guaranteed survival from the government and also regulations that do not encourage the implementation of conservatism.

The limitation of this research is that there has not been a stability test or model selection. Future studies should conduct this test in order to get the best testing model. This study also has not analyzed the behavior of conservatism based on G_Score and C_Score components. Future studies should do this in order to get a more comprehensive understanding.

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APPENDIX

Correlation Matrix (Accrual Based Testing)

Variabel	ACC	BOND	BUMN	CFO	CFO_BOND	CFO_BUMN	CFO_SIZE	NEGCFO
ACC	1							
BOND	0.035668	1						
BUMN	0.013668	0.22096	1					
CFO	-0.50257	-0.04786	-0.02899	1				
CFO_BOND	-0.03322	0.346924	0.094053	0.116481	1			
CFO_BUMN	-0.01965	0.151113	0.499855	0.030816	0.23859	1		
CFO_SIZE	-0.47199	-0.0449	-0.0267	0.998149	0.127947	0.036865	1	
NEGCFO	0.2327	-0.03733	-0.03182	-0.331212	-0.220514	-0.150508	-0.33444	1
NEGCFO_BOND	0.053633	0.399948	0.015638	-0.094662	-0.36042	-0.11127	-0.10053	0.334373
NEGCFO_BUMN	0.013825	0.022318	0.39841	-0.046417	-0.078769	-0.378146	-0.04928	0.183479
NEGCFO_CFO	-0.45122	0.02963	0.024445	0.508359	0.156749	0.052761	0.496958	-0.34639
NEGCFO_CFO_BOND	-0.00079	-0.2105	-0.02053	0.116904	0.633088	0.110852	0.125592	-0.17598
NEGCFO_CFO_BUMN	-0.02957	-0.05474	-0.30643	0.047335	0.140823	0.483471	0.050696	-0.14112
NEGCFO_CFO_SIZE	-0.45015	0.025252	0.02287	0.509257	0.172036	0.05693	0.498419	-0.35301
NEGCFO_SIZE	0.22643	-0.02371	-0.02546	-0.323866	-0.227818	-0.155311	-0.32782	0.997434
SIZE	0.08105	0.369698	0.255496	-0.041674	0.134961	0.157053	-0.02667	-0.20387

Variabel	NEGCFO_BOND	NEGCFO_BUMN	NEGCFO_CFO	NEGCFO_CFO_BOND	NEGCFO_CFO_BUMN	NEGCFO_CFO_SIZE	NEGCFO_SIZE	SIZE
ACC								
BOND								
BUMN								
CFO								
CFO_BOND								
CFO_BUMN								
CFO_SIZE								
NEGCFO								
NEGCFO_BOND	1							
NEGCFO_BUMN	0.124164	1						
NEGCFO_CFO	-0.07986	-0.03147	1					
NEGCFO_CFO_BOND	-0.52631	-0.09476	0.192003	1				
NEGCFO_CFO_BUMN	-0.17641	-0.76914	0.050211	0.203718	1			
NEGCFO_CFO_SIZE	-0.09204	-0.03695	0.999398	0.215713	0.057872	1		
NEGCFO_SIZE	0.362647	0.198001	-0.33098	-0.188364	-0.151761	-0.338834	1	
SIZE	0.099469	0.048874	0.154187	-0.037959	-0.034548	0.148345	-0.17385	1

Source: processed data