The Use of Operating Cash Flow and Managerial Ownership Against Accounting Conservatism

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ARTICLE INFO

Article history:
Received : February 10, 2025
Revised : March 15, 2025
Accepted : March 17, 2025

Keywords:
Operating Cash Flow;
Kepemilikan Manajerial;
Konservatisme Akuntansi;

ABSTRACT

This study investigates the impact of operating cash flow and managerial ownership on accounting conservatism in the financial sector companies listed on the Indonesia Stock Exchange (IDX) during the 2021-2023 period. The research employs a purposive sampling method, with a sample size of 57 companies listed on the IDX within the specified period. The data analysis process includes descriptive statistical testing, multicollinearity testing, overall model testing, regression model feasibility testing, and hypothesis testing. Panel data regression analysis is the statistical method utilized in this research. The findings reveal that operating cash flow partially influences accounting conservatism, managerial ownership also has a partial effect on accounting conservatism, and collectively, both variables significantly impact accounting conservatism. The study aims to provide practical value, enabling businesses and the public to better understand the role of operating cash flow and managerial ownership in fostering accounting conservatism, particularly in companies listed on the IDX.

1. INTRODUCTION

The principle of conservatism emphasizes prudence in profit recognition and prioritizes the recognition of losses. Its objective is to provide a more realistic financial depiction. Conservative accounting continues to play a crucial role in contemporary accounting practices as this principle influences financial valuation. According to Rumapea et al. (2019), Accounting conservatism is a principle that emphasizes prudence in financial reporting by limiting the recognition of cumulative profits, postponing revenue acknowledgment, promptly recording expenses, reducing asset valuation, and enhancing liability measurement. The principle of accounting conservatism is essential in addressing the uncertainties of economic and business activities. However, many companies still fail to apply conservative accounting in their financial reporting.

The case of Wanaartha Life (PT Asuransi Jiwa Adisarana Wanaartha) serves as concrete evidence of a severe violation of accounting principles in 2022. This insurance company was found guilty of manipulating financial statements by concealing liabilities amounting to IDR 12.1 trillion. This action was taken to present a more favorable financial condition than reality. Consequently, the company's financial statements became inaccurate, harming many parties, particularly policyholders. This case highlights the importance of strict supervision of accounting practices to prevent manipulation and protect public interests.

Based on this case, operating cash flow has also become a key indicator in determining whether a company's operational activities can generate sufficient cash flow to finance its operations, pay off debts, and distribute dividends without relying on external funding. Operating cash flow is crucial because, in the long run, a business must generate a positive net cash flow from operational activities to ensure its sustainability. Operating cash flow reflects a company's performance in generating cash that can be used to repay debts, pay dividends, and make new investments without external funding dependency. The higher the operating cash flow, the better the company's performance, which can predict higher profits in subsequent periods. Several factors can influence management's decision in applying conservative accounting, one of which is cash flow (Harini et al., 2020). The cash flow

E ISSN 2621-749X **doi.org/10.31334/bijak.v21i1.4503**

statement provides insights into historical changes in an entity's cash and cash equivalents by detailing variations over a specific period in operating, investing, and financing activities. The cash flow statement from operating activities indicates a company's performance and the quality of the profits generated.

Another influential factor is managerial ownership. Managerial ownership is one of the factors that drive management to consider applying the principle of conservatism. Decision-making within a company tends to be more conservative when the level of managerial ownership is high. Managerial ownership is defined as the percentage of shares owned by management actively involved in corporate decision-making, including commissioners, directors, and employees (Oktadella and Zulaika, 2011). Additionally, Deviyanti and Rahardjo (2012) define managerial ownership as the ratio of share ownership between internal and external parties of a company. Share ownership by management serves as a mechanism to ensure that management acts in the best interests of the company since it includes shares personally owned by managers (Herawaty, 2007).

In addition, Positive Accounting Theory (PAT) plays a significant role in explaining the motivations behind managerial decisions, including the adoption of conservative accounting practices. PAT suggests that managers choose accounting policies based on their incentives, which may be influenced by contracts, market expectations, and regulatory requirements. The application of conservatism in accounting can be understood through the lens of PAT, as it helps align the interests of management with stakeholders by reducing information asymmetry and mitigating potential agency conflicts. The theory explains that companies with high managerial ownership are more likely to adopt conservative accounting policies to protect their wealth and maintain credibility in the financial markets. Although extensive research has been conducted on accounting conservatism, gaps remain in understanding the relationship between operating cash flow and managerial ownership concerning accounting conservatism. Some prior studies have focused only on individual variables without considering how the combination of these two factors affects the level of accounting conservatism. Additionally, many studies still use data from periods before major financial scandals, such as the Wanaartha Life case, making it necessary to update research findings to reflect current conditions.

Therefore, further research is needed to understand how these factors interact in the context of companies in Indonesia. The urgency of this research is heightened by the increasing number of financial statement manipulation cases in Indonesia, demonstrating that the practice of accounting conservatism has not been optimally implemented. By understanding the role of operating cash flow and managerial ownership in accounting conservatism, this study is expected to contribute to companies, investors, regulators, and academics in developing more effective policy strategies for monitoring and applying accounting conservatism principles. Based on the background presented, including inconsistencies (research gaps) in previous studies and the phenomenon of gaps in the application of accounting conservatism in companies listed on the Indonesia Stock Exchange, this study aims to examine variables suspected of influencing accounting conservatism. Thus, the researcher has conducted a study titled: **"The Influence of Operating Cash Flow and Managerial Ownership on Accounting Conservatism."**

2. METHOD

Data Collection Methods

This research uses a quantitative approach to test causality and explain cause-and-effect relationships between variables. The data is sourced from secondary information obtained through documentation methods from the Indonesia Stock Exchange (www.idx.co.id). The study population consists of 95 financial sector companies listed on the IDX from 2021 to 2023. Using purposive sampling, the study selects companies that: (1) Are registered on the Indonesia Stock Exchange (IDX), (2) publish annual reports consistently, (3) use the rupiah currency, (4) report profits, and (5) disclose complete data on the research variables for the 2021–2023 period.

Table 1. Variable Operational

Variabel	Proxy	Rasio
Accounting Conservatism	$CONACC = \frac{(NI + DEP + CF))\ x\ (-1)}{Total\ Asset}$	Febrilianty, 2022
Cash Flow	$CFO = \frac{Kas\ dari\ Aktivitas\ Operasi}{Total\ Asset}$	Harini, Syamra and Setiawan, 2020
Managerial Ownership	$ManOw = \frac{Jumlah\ Saham\ yang\ DImiliki\ Manajemen}{Jumlah\ Saham\ Beredar}$	Febrilianty, 2022

Source: 2022 recapped-data

Data Analysis Methods

In this research, the gathered data will be examined quantitatively using statistical analysis tools in EViews 12, utilizing the following statistical methods.

3. RESULTS AND DISCUSSION

Descriptive Statistics

Table 2. Descriptive Statistical Analysis

	Y	X1	X2
Mean	-0.005013	0.012953	0.046999
Median	-0.003172	0.014817	0.000478
Maximum	0.243488	0.259741	0.623285
Minimum	-0.166268	-0.162254	0.000000
Std. Dev.	0.076871	0.075561	0.156270
Skewness	0.660108	0.563531	3.434365
Kurtosis	4.548778	4.763891	12.89259
Jarque-Bera	7.765663	8.215459	271.9550
Probability	0.020592	0.016445	0.000000
Sum	-0.225573	0.582903	2.114951
Sum Sq. Dev.	0.260004	0.251215	1.074487
Observations	45	45	45

The results of the descriptive test in Table 2 can be explained as follows:

Accounting Conservatism Variable: The minimum value of -0.166268 was recorded by PT. Bank Maspion Indonesia in 2023, while the maximum value of 0.243488 was observed at PT. Bank Pembangunan Daerah Jawa Timur in 2021.

Operating Cash Flow Variable: The lowest value of -0.162254 was found at PT. Bank Maspion Indonesia in 2023, whereas the highest value of 0.259741 was reported by PT. Bank Pembangunan Daerah Jawa Timur in 2021.

Managerial Ownership Variable: The minimum value of 0.000000 was noted at PT. Bank Maspion Indonesia in 2023, while the highest value of 0.623285 was recorded at PT. Asuransi Ramayana in both 2022 and 2023.

Selection of Panel Data Regression Model

The selection of the most appropriate regression model among the Fixed Effect Model (FEM), Random Effect Model (REM), and Common Effect Model (CEM) is conducted through two tests: the

E ISSN 2621-749X **doi.org/10.31334/bijak.v21i1.4503**

Chow Test and the Hausman Test. The analysis results indicate that the Fixed Effect Model (FEM) is the most optimal regression model for this study.

Table 3. Model Conclusion Results

No.	Model Selection Test	Probability Value	Model Result
1.	Chow Test (CEM vs FEM)	0.0000 < 0.05	FEM
2.	Hausman Test (REM vs FEM)	0.2933 > 0.05	REM
3.	Lagrange Multiplier Tests (CEM vs REM)	0,3684 < 0,05	REM
	Conclusion		**REM**

Source: Processed secondary data, 2024

Table 4. Statistics Test Result

Variabel	Ordinary Least Square		Multicollinearity	Heteroscedasticity
	Coefficient	**Prob.**	**Prob.**	**Prob.**
C	-0.014305	0.0000		
X1	1.000982	0.0000	-0.065626	0.4767
X2	-0.078163	0.0000	-0.065626	0.8501
Jarque-Bera				1.995861
Probability				0.368642
Durbin-Watson				1.238412
F-Statistic				5522.404
Prob (F-Statistic)				0.000000
Adjusted R-Squared				0.996031

Source: Processed secondary data, 2024

Classical Assumption Test

The classical assumption tests in this research consist of normality, multicollinearity, heteroscedasticity, and autocorrelation tests. The normality test results show that the Jarque-Bera value is 1.995861 with a probability of 0.368642 (>0.05), indicating that the residuals are normally distributed. The multicollinearity test results indicate that the Variance Inflation Factor (VIF) values for all independent variables are less than 10, confirming the absence of multicollinearity in this regression model. The heteroscedasticity test using the Glejser test shows that all independent variables have a significance level of >0.05, concluding that the model does not exhibit heteroscedasticity. Additionally, the autocorrelation test using the Durbin-Watson method shows a value of 1.238412, which falls within the range of -2 to +2, indicating that this regression model is free from autocorrelation issues. Therefore, the regression model used in this study meets the classical assumptions and is suitable for further analysis.

The goodness of the Fit Model Test

The ANOVA Significance Test (F Test) indicates that independent variables simultaneously influence the dependent variable if the probability value of the F-statistic is less than 0.05. The Partial Significance Test (t Test) reveals that the probability values for Operating Cash Flow and Managerial Ownership are both 0.0000, which is less than 0.05, indicating that both variables significantly affect Accounting Conservatism. Additionally, the Adjusted R^2 Determination Test result shows an Adjusted R-squared value of 0.996031, meaning that Accounting Conservatism can be explained by the independent variables by 99.6%, while the remaining 0.4% is influenced by other factors outside this regression model.

The Influence of Operating Cash Flow Usage on Accounting Conservatism

The hypothesis test results show that the regression coefficient is 1.000982 with a significance level of 0.0000, which is smaller than the significance threshold of 0.05 (0.000 < 0.05). Thus, it can be concluded that the use of Operating Cash Flow (X1) influences Accounting Conservatism. This finding is consistent with the research conducted by Suharni et al. (2019), Kahirani and Africano (2017), and Jayanti (2016), which states that Operating Cash Flow affects accounting conservatism. Within the framework of Positive Accounting Theory, this relationship can be explained through the contracting efficiency hypothesis and market discipline mechanisms. Companies with high levels of Operating Cash Flow tend to have better financial flexibility, making them more cautious in revenue recognition and quicker in expense recognition, aligning with the principles of accounting conservatism. This approach is adopted to mitigate the risk of overly optimistic financial reporting and ensure business sustainability in the long term. Conversely, companies with low Operating Cash Flow often face pressure from stakeholders, which may encourage them to adopt more aggressive accounting practices to increase reported earnings and appear more attractive to investors. In this context, Positive Accounting Theory explains that managers have incentives to choose accounting policies that maximize firm value, including the application of accounting conservatism in response to the company's financial conditions and market pressures.

The Influence of Managerial Ownership on Accounting Conservatism

The hypothesis test results indicate that the managerial ownership variable has a regression coefficient of -0.078163 with a significance level of 0.000, which is smaller than the significance threshold of 0.05 (0.000 < 0.05). This confirms that managerial ownership (X2) influences accounting conservatism. From the perspective of Positive Accounting Theory, this relationship aligns with the bonus plan hypothesis and the management ownership hypothesis. When managerial ownership is low, financial reports tend to be less conservative because managers prioritize personal incentives, such as bonus maximization, rather than shareholder interests. In contrast, higher managerial ownership aligns management's interests with those of shareholders, encouraging more conservative accounting practices to reduce agency conflicts and enhance the reliability of financial reporting.

This finding is supported by Yazidah (2011), who identified a positive relationship between managerial ownership and accounting conservatism, as well as Putra et al. (2019), who concluded that managerial ownership positively affects accounting conservatism. In essence, when managers have a greater equity stake in the company, they are more likely to adopt conservative accounting policies to ensure financial transparency and protect long-term firm value.

The Influence of Operating Cash Flow and Managerial Ownership on Accounting Conservatism

The results of this study confirm that Ha3 is accepted, demonstrating that both operating cash flow and managerial ownership significantly influence accounting conservatism. This indicates that multiple independent variables have a significant impact on accounting conservatism. The panel data regression results show that the F-statistic value is 5522.404, with a Prob (F-stat) of 0.0000, which is smaller than 0.05 (0.0000 < 0.05). Therefore, the independent variables collectively have a simultaneous influence on the dependent variable.

From the perspective of Positive Accounting Theory, these findings align with the efficiency contract hypothesis and management ownership hypothesis. The efficiency contract hypothesis suggests that companies with higher operating cash flow tend to adopt conservative accounting practices to maintain financial stability and meet stakeholder expectations. Firms with strong cash flow generation are less likely to engage in aggressive earnings management, as they do not rely heavily on external financing. In contrast, companies with lower operating cash flow may feel pressured to present more favorable financial reports to attract investors and secure funding.

The management ownership hypothesis explains that higher managerial ownership aligns the interests of managers with those of shareholders, encouraging more conservative financial reporting to minimize agency conflicts. Managers with a low ownership stake may prioritize short-term earnings manipulation to maximize personal benefits, while those with a higher ownership stake are incentivized to ensure financial transparency and long-term firm value preservation. These findings reinforce the importance of considering both financial performance indicators and corporate governance structures in shaping accounting conservatism. By integrating operating cash flow and managerial ownership, companies can enhance financial reporting credibility and reduce information asymmetry, ultimately supporting more sustainable business practices.

4. CONCLUSION

Based on the research findings, it can be concluded that operating cash flow and managerial ownership have a significant impact on accounting conservatism. Companies with high operating cash flow tend to adopt a higher level of accounting conservatism due to greater financial flexibility, leading to more cautious revenue recognition and quicker expense recognition. Conversely, low managerial ownership may encourage managers to prioritize short-term profits, potentially reducing the application of accounting conservatism. These findings support Positive Accounting Theory, particularly in terms of contract efficiency and market discipline mechanisms, which explain how accounting policies are chosen based on financial conditions and managerial incentives.

However, this research has certain limitations. Firstly, the sample is restricted to companies registered on the Indonesia Stock Exchange (IDX), which may limit the generalizability of the findings to other industries or countries. Second, this study only focuses on operating cash flow and managerial ownership, while other factors such as institutional ownership structure, leverage, and corporate governance may also influence accounting conservatism. Additionally, the relatively short study period may not fully capture the long-term dynamics of accounting conservatism implementation in companies.

For future studies, it is suggested to broaden the sample by incorporating diverse industries and companies from multiple countries to improve the external validity of the results.Furthermore, incorporating additional factors, such as corporate governance mechanisms, industry competition levels, and business risks, could provide a more comprehensive understanding of accounting conservatism. A qualitative approach may also be considered to explore managerial motivations behind specific accounting policy choices. Lastly, employing more advanced econometric models, such as the Generalized Method of Moments (GMM) or Structural Equation Modeling (SEM), could help address potential biases in panel data regression analysis. By doing so, future studies are expected to offer deeper insights into the factors influencing accounting conservatism and its implications for financial reporting quality.

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