Managerial Ability and Convergent Interest on Accounting Conservatism: Internal Control Quality as a Mediator

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Abstract

The development of accounting conservatism has progressed, though with various pros and cons. Therefore, this study aimed to examine the relationship between managerial ability, convergent interest, and accounting conservatism for manufacturing companies on the Indonesia Stock Exchange from 2018 to 2019. The internal quality control was used as a mediating variable of the relationship between managerial ability and convergent interest in accounting conservatism. The results showed that managerial ability and convergent interest affect internal quality control and accounting conservatism, which benefit the company and stakeholders. The Sobel test identified internal quality control as mediating variable of the relationship between managerial ability and convergent interest with accounting conservatism. This study contributed to the accounting conservatism literature and its additional determinants. This study contributes in several different ways. First, to the knowledge, this is the first study to examine a comprehensive model between managerial ability, convergent interest, internal control quality, and accounting conservatism. Second, this study contributes to the literature on accounting conservatism and produces additional determinants of accounting conservatism.

Keywords: Managerial ability, convergent interest, internal control quality, accounting conservatism

1. Introduction

Accounting conservatism involves strict measures that identify bad news as a loss than good news as a profit (Lafond and Roychowdhury 2008). Basu (1997) defined conservatism as earnings that reflect the bad news period faster than good news, which is associated with situations that can cause losses. In this situation, circumstances capable of generating profits are postponed until the situation occurs (Hajawiyah et al. 2020).

Financial statement manipulation indicates low financial reporting in the applied accounting conservatism principle, such as Toshiba Company. An independent audit team appointed by Toshiba on June 20, 2015, established that the company had overstated profits by inflating 151.8 billion yen or approximately 16 trillion rupiahs from April 2008 to March 2014 (www.Tribunnews.com). Toshiba blamed the profit inflation on inaccurate financial calculations over a long period and continuous misuse of accounting procedures, a case that affected the shareholders and investors. Inaccurate financial calculations result from ignoring the precautionary principle to identify income and expenses while preparing financial statements (Sugiarto and Fachrurrozie, 2018). For instance, the PT (Persero) Timah in Indonesia recorded errors of accounting conservatism application in 2015. The board of directors had a press release on the first quarter's financial

statements in 2015, stating that the company had achieved optimum profit. However, they had recorded 59 billion losses and a 100% debt increase compared to 2013. In general, implementing accounting conservatism in the company is difficult because it is controversial and has pros and cons.

Companies use accounting conservatism to determine accounting and estimation methods that record low book value of assets (Penman and Zhang, 2002). Ahmed and Duellman (2007) stated that conservatism could reduce management over-compensation by limiting the possibility of assets and income overstatement. Additionally, accounting conservatism is a governance mechanism that can reduce the manager's ability to manipulate and exaggerate the company's financial performance, increasing cash flow and value (Lafond & Watts, 2008). The low manager's ability in financial manipulation guarantees quality information to shareholders. The CEO's role is to prevent opportunistic management decisions for self-benefit, limit agency problems in strategic decisions, and reduce litigation costs (Ball and Shivakumar, 2005).

Haider et al. (2021), Kim et al. (2021), and Kamyabi & Nia (2021) investigated accounting conservatism for high abilities managers. In contrast, Haider (2021) studied Australian firms in 2004 – 2013 and found that managerial ability positively affects accounting conservatism. The manager's ability to implement accounting conservatism to improve and maintain their reputation can result in poor performance in the future. Kim et al. (2021) studied the US firms from 1988 to 2019 and

found that high abilities managers avoid accounting conservatism. Managerial ability resolves their performance uncertainties and operational ability to reduce accounting conservatism. Although managerial ability can be an accounting conservatism substitute, it reduces information asymmetry, specifically with high conservatism demand. Kamyabi & Nia (2021) found that the managerial ability variable cannot moderate investor sentiment and accounting conservatism. However, previous studies only examined the direct effect of managerial ability variables on accounting conservatism.

This study aimed to determine the internal quality control as a mediating variable between managerial ability and accounting conservatism. Various factors contribute to the effects of manager characteristics on accounting conservatism. The role of internal quality control as a connecting variable is based on various studies such as Goh and Li (2011); Mitra et al. (2013); Ji et al. (2016); Tang & Xu (2010) and Yin (2020), that linked it to accounting conservatism. In contrast, Ji et al. (2016) explained a relationship between accounting conservatism and the need for more internal control. Another internal control assurance reduces the negative effects on accounting conservatism. Li (2015), Salehi et al. (2020), and Lee (2015) linked managerial ability to internal quality control to support that the latter is a mediating variable between managerial ability and accounting conservatism.

This study examined the effect of the manager's role on accounting conservatism following internal quality control. It contributed to the literature by a) examining a comprehensive model between managerial ability, convergent interest, internal quality control, and accounting conservatism, and b) Providing additional determinants of accounting conservatism. Furthermore, the study established implications investors and other stakeholders in assessing managerial ability and convergent interest when applying accounting conservatism to financial statements or when making efficient contractual arrangements with managers. For regulators, this research can have implications for issuers in the capital market to encourage accounting conservatism. Accordingly, the quality of internal control will increase through the disclosure of internal controls to the public.

2. Literature Review

Based on the theory of upper echelons, Hambrick and Mason (1984) stated that the background characteristics of top management affect strategies implementation and the company consequences. Therefore, the management's characteristics are reflected in the organization. The manager's characteristics, skills, and abilities are displayed while disclosing internal control to the public. Disclosing internal control and the application of accounting conservatism is part of the management's strategic choices. High-ability managers disclose items from internal control as additional information for the company's financial statements users to make an effective decision. They also apply strategic accounting conservatism to improve reputation and competence in the community.

Jensen and Meckling (1976), and Hossain et al. (1995) used agency theory to explain the manager's voluntary decision to disclose company information. Managers are aware that shareholders control their behavior through engagement and monitoring activities. Shareholders conduct engagement activities by equating their interests with the managements or convergent interests. Managers voluntarily disclose certain information to show their performance to the shareholders. Furthermore, they disclose internal control to show its quality, effectiveness, and efficiency. Therefore, they show the

shareholders how internal control is optimized. This provides additional information for shareholders and other financial statements users for effective decision-making.

Accounting conservatism is asymmetric timelines to determine good and bad news through earnings (Basu, 1997). It responds to unrealized losses quicker than unrealized profits. Therefore, it requires a higher verification level of good news than bad news. Accounting conservatism ensures that the cash flow numbers are estimated conservatively. It helps to alleviate agency problems through an ex-ante efficiency role in contracts (Muttakin et al., 2019).

Conservatism is significant in governance for reducing conflict and improving contract efficiency in companies (Holthausen, 2003; Ball and Shivakumar, 2005). According to Ball and Shivakumar (2005), accounting conservatism effectively limits managers' control rights and transfers them to the finance department. In comparison, Watts (2003) stated that conservatism could reduce the company's litigation costs.

Internal quality control is achieved when the organization effectively implements its objectives and can be assessed using internal control disclosures, which determines the reliability of a reporting system. Therefore, the stakeholders can determine the company's performance. Furthermore, effective internal control improves the quality of the financial reports and minimizes the information gap between managers and shareholders. Ji et al. (2016) reported that the accounting and non-accounting areas of internal control disclosure affect the quality of the financial statements in the Chinese capital market. The internal control disclosure reveals the importance of effective internal control to the CEOs and top officials. Dowdell et al. (2014) supported that the disclosure of internal control as a proxy by management shows its positive effects on the quality of the financial reports.

3. Hypothesis Development

Structures on internal control improve financial performance, such as effective design, implementation and maintenance, and financial structures (Kabuye et al., 2019). The management's commitment to effective design and implementation of internal control improves the control environment. The management's attitudes towards internal control, such as public disclosure and documentation policies, can also measure their commitment to internal quality control (Tsai 2010). The company should implement the management's attitude, commitments, and internal control system policies.

According to the upper echelons theory, the managers' experience, education, skills, and characteristics affect their strategic decisions to disclose internal control publicly. Furthermore, top managers are challenged by situations that must be handled internally and externally (Jensen and Zajac, 2004). The managerial characteristics are value-based and cognitive-based, which help make strategic choices to improve the company's performance, such as its internal control structure. The decision to disclose internal control is part of the management's strategies.

The high-ability managers disclose internal control items as additional information for the company's financial statements users to make effective decisions. One of the managerial abilities is reflected in their efficiency. Furthermore, it determines the efficiency and effectiveness of the implemented internal control system.

The manager's operational ability on the company's internal quality control depends on financial and non-financial motivations (Li 2015). Financial motivation provides incentives to enhance the achievement of internal quality control,

whereas non-financial motivation is related to reputation. Disclosing effective internal control to the public increases firms' value and the manager's reputation.

The board of directors can assess managers' abilities based on the achieved internal quality control. Therefore, managers should complement their skills with effective internal quality control. Li (2015), and Salehi et al. (2020), showed that managerial ability positively affects internal quality control.

H1: Managerial ability positively affects internal quality control.

Manager ability applies accounting conservatism because it helps the stakeholders (Haider et al., 2021). Managers with high abilities have higher profitability (Inam Bhutta et al., 2021). Accounting conservatism prevents ex-post managerial opportunism (Gao, 2012). Manager ability combines accounting conservatism with its application to improve and maintain its reputation and prevent future poor performance (Haider et al., 2021). Losing their reputation for hiding bad news can affect their future career prospects.

Applying the conservatism principle allows managers assessment based on high-quality earnings. It also means being more careful, prioritizing bad news over good news, and reporting losses first rather than profits. It causes managers ability to be judged as unable to produce quality financial reports. Studies showed that high-ability managers increase earning quality (Baik, 2011; Demerjian et al., 2013; Francis et al., 2008) and improve the company's performance (Cheung et al., 2017; Demerjian et al., 2012; Jian and Lee, 2011).

Haider et al. (2021) stated that high-ability managers apply the conservatism principle by a) using their skills and expertise to report highly biased accounting numbers. They exaggerate the company's assets or hide losses that assess the high-quality earnings. Managers receive incentives and increased compensation for their performance. b) High-ability managers report higher levels of accounting conservatism by reporting the financial statements losses, expecting for the company's debt contract suspension.

Haider et al. (2021) found that managerial ability positively affects accounting conservatism. Therefore, higher manager capacity increases the company's chances of implementing accounting conservatism.

H2: Managerial ability positively affects accounting conservatism.

The agency theory provides the bonding approach to minimize agency problems over manager behavior. Shareholders commit to managers with similar interests. The bonding approach controls and minimizes managers' deviant behavior. Therefore, the company's goals are achieved in line with the shareholders' interests. Shareholders bind managers to their convergent interests, using longer tenure to protect their interests. The shareholders provide a longer manager's tenure as motivation to effectively run the company. Wertheim et al. (2016) found that director tenure positively affected effective corporate governance as a proxy for internal control disclosure in the United States public companies from 2004 to 2014. It supports the hypothesis that a longer director's tenure, expertise, and experience, increase effective corporate governance. Managers with long tenure must know the company's internal accounting and adequate internal control system (Muttakin et al., 2019). A company effectively maintains accounting policies and internal control procedures when non-routine transactions are recorded.

Convergent interest supports managers' duties and responsibilities, such as achieving the company's internal quality control. Managers' long tenure promotes decision-making that aligns with shareholders' interests for public disclosure of the internal control information. Schoepfer (2007) determined that the older, longer tenure managers are less

likely to commit violations because financial misstatements reflect weak internal control.

H3: Convergent interest positively affect the internal quality control

A higher level of verification to recognize profits requires higher accounting conservatism for the company. Although accounting conservatism has pros and cons, its development indicates increased practices. The company stakeholders (shareholders, government, creditors, and other parties) promote increased accounting conservatism because they require information about bad news earlier than good news (Basu, 1997). The owner uses quality financial reports to maximize the firm value by implementing conservative accounting principles.

The hypothesis predicts that long tenure managers have substantial incentives to ensure accurate financial statements. Therefore, they are aware of the negative effects of earning manipulation and the need for high-quality financial information (Muttakin et al., 2019). Milbourn (2003) explained that long tenure managers build the company's reputation in the market. They maintain their reputation and ability by avoiding opportunistic behavior such as accrual management (Ali and Zhang, 2015). Managers avoid deviant accounting practices and apply accounting conservatism. Therefore, they reduce the earnings overstatement through quicker recognition of good news than bad news (Muttakin et al., 2019).

Managers with long-term experience provide knowledge of the company's goals convergent with the owner's interests. It also helps to reduce monitoring and agency costs (Brookman and Thistle, 2009). Therefore, long tenures managers have similar accounting conservatism principles with company owners. Hsu et al. (2017) suggested that the longer the manager's term, the more conservative accounting principles applied, enhancing cash flow performance.

H4: Convergent interest positively affect accounting conservatism

Several studies stated that the environmental contracts and corporate governance determine the accounting conservatism principle (Nikolaev, 2010; Lafond and Roychowdhury, 2008). The increased severity of agency problems encourages greater accounting conservatism (Lafond and Roychowdhury, 2008). The internal control system is significant in corporate governance to monitor the manager's behavior and minimize agency costs (Fama and Jensen, 1983). Creating a culture of strong internal control system provides accounting conservatism benefits in the corporate governance environment. Companies with strong internal control systems apply accounting conservatism (Goh and Li 2011). In contrast, weak internal control systems provide inaccurate information and do not promptly recognize the company's losses, resulting in low accounting conservatism.

The companies with weak internal control have high risks that can be reduced by adopting conservative financial reporting strategies. The companies risk public disclosure of their weak internal control (Mitra et al., 2013). Implementing regulations on public companies will affect their reporting strategy.

Goh and Li (2011) established that companies that disclose internal control weakness have low accounting conservatism. Mitra et al. (2013) proved that strong internal control supports accounting conservatism, while its weakness leads to lower accounting conservatism. Ji et al. (2016) explained a relationship between accounting conservatism and strong internal control. The other internal control assurance reduces the negative effect of the internal control weakness on accounting conservatism. Tang and Xu (2010) and Yin et al. (2020) stated a positive relationship between internal control quality and accounting conservatism.

H5: Internal quality control positively affects accounting conservatism.

Haider et al. (2021) stated that high-ability managers apply accounting conservatism using a higher level of conservatism report, including economic losses in the financial statements to handle corporate contracts like debt contracts efficiently. This is aimed to build and maintain their reputation. Managers must provide correct information to lending institutions and markets to avoid losing their reputations. High-ability managers issue accurate earnings forecasts and improve earnings quality (Baik et al., 2011). They apply accounting conservatism to benefit the stakeholders by reducing agency problems, improving management and conservatism monitoring, and increasing contract efficiency with shareholders.

Strong internal control support accounting conservatism (Mitra et al., 2013). High-ability managers are aware that they are responsible for achieving internal quality control. The public disclosure of internal control determines its quality. Therefore, high-ability managers support disclosure of internal control because it reliably supports accounting conservatism. Ji et al. (2016) established a relationship between accounting conservatism and the demand for strong internal control.

H6: Internal quality control mediates between managerial ability and accounting conservatism.

The hypothesis states that longer tenure managers have exclusive expertise and company environment knowledge.

Therefore, they better understand the company, create financial reporting systems, and effectively communicate financial information to shareholders (Muttakin et al., 2019). It also helps them realize their convergent interest with shareholders. Longer tenure managers understand the organization's internal accounting system operations by collecting information on the adequacy of the internal control system. For example, the company maintains accounting policies and internal control procedures when non-routine transactions are recorded. Ineffective accounting policies and internal control procedures result in management accelerating profits and deferring losses, causing a lower verification in recognizing good news in financial statements, and biasing the organization's accounting measures (Muttakin et al., 2019).

Convergent interest improves the manager's attitude to protect shareholders and maintain their reputation. Therefore, long-term managers are aware of the negative effects of earnings manipulation and the need for quality financial information (Ali and Zhang, 2015). The quality financial information provided by longer tenure managers is achieved by applying the conservatism principle to be more careful, prioritizing bad news over good news, and reporting losses first rather than profits (Ahmed and Henry, 2012).

H7: Internal quality control mediates between convergent interest and accounting conservatism.

Figure 1. Empirical Model

4. Study Method

Population and Sample

This study's population included manufacturing companies listed on the Indonesia Stock Exchange (IDX) from 2018 to 2019. The sampling method used was purposive sampling, which selected samples based on specific criteria as follows:

1. The company's published financial statements as of December 31 for the 2018 to 2019 financial year.
2. The company used the rupiah currency unit considered to have the same obtained value.
3. The company was not delisted during the observation period.
4. The company has information on various measurement variables, such as the description of the internal control system in the Corporate Governance section, the number of workers, and the cost of goods sold.

Based on these criteria, 208 manufacturing companies were selected as sample of this study.

Variable Measurement

The accounting conservatism, was used as a dependent variable, divided into conditional and unconditional

conservatism (Basu 1997). Unconditional conservatism emphasizes the difficulty of valuing assets and influencing future income. In comparison, conditional conservatism emphasizes the efficiency of management incentives to report biased numbers (Beaver and Ryan, 2005). Conditional conservatism is an effective indicator of corporate governance than unconditional conservatism (Yin et al., 2020). The internal control variables are part of corporate governance. Therefore, conditional conservatism was used to measure accounting conservatism. The conditional conservatism (BTM) is calculated by Beaver and Ryan (2005). The proportion of assets' accounting value is divided by the share market value plus the liabilities book value.

The independent variables included managerial ability, convergent interest, and internal quality control. Managerial ability measurement is based on their efficiency in converting company resources into income (Demerjian et al., 2013). The DEA (Data Envelopment Analysis) was used to evaluate the relative efficiency of the UKE (Economic Activity Unit). The measurement of the manager's efficiency used the DEA method, which is a Variable Return to Scales (VRS). The same inputs and outputs were used for each UKE. Input consisted of total assets, workers, days cost of goods sale in inventory, and days sales outstanding, while the output used was sales. The results included company efficiency and manager efficiency. The following is the regression equation by García-Meca & García-Sánchez (2017) that separate company and manager

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efficiency:

$$DEA\ Score = \beta_0 + \beta_1 Size + \beta_2 Market_Share + \beta_3 Cash_Flow + \beta_4 Age + e$$

Information:

B0- β_4 : Coefficient

e: Residual value

Convergent interest is the alignment of the manager's and shareholder's interests. The measurement of the convergent interest variable used a proxy for the manager's tenure. In contrast, the measurement of internal control disclosure variables used an instrument by (Deumes and Knechel 2008) and developed by (Poel and Vanstraelen 2011) and (Weli 2018). They were adjusted to Bapepam and Financial Institution regulations number Kep-431/BL/2012. The unweight dichotomous scale was used to score each disclosure item of the company by assigning a value of 1 for a disclosed item and 0 for the undisclosed item. Furthermore, each item's scores were added to obtain the total disclosure score of each company. The internal control disclosure index was calculated using the formula below:

$$ICD = \sum_{ij} ADitem$$

$$\sum_{ij} ADitem$$

$\sum_{ij} Ditem$ = the total score for the disclosed internal control item

$\sum_{ij} ADitem$ = the total score of internal control items that should have been disclosed

The item disclosure of financial, operational control information and laws and regulations compliance are as follows:

Item A1. Internal Control Description

Item A2. Internal Control Review

Item A3. Internal Control Object

Item A4. Internal Audit function in the company's internal control system

Item A5. Activity risk management

Item A6. Audit Committee

Item A7. Company's Code of Ethics

Item A8. Whistleblower Policy

Item A9. Special risks

Item A10. Significant changes to the internal control system

Disclosure of information items on review of the internal control system effectiveness are as follows:

Item B1. Management statements on the internal control system effectiveness

Item B2. The board of commissioner's role in the internal control system

Item B3. The audit committee's role in the internal control system

Item B4. The external auditor's role in the internal control system

Item B5. Management statement on the financial statements quality assessment

Item B6. The board of commissioners discusses the internal control system at least once a year

Item B7. Management responsibility for the implementation of an internal control system

Item B8. There is a statement about the internal control system in the financial report

Item B9. Internal control criteria such as COSO

The study used control variables affecting accounting conservatism such as firm size (measured by the natural logarithm of total assets) because large companies lack conservatism (Givoly et al., 2007; Lafond and Watts, 2008). Firms' growth (MTB) affects accounting conservatism (Lafond and Roychowdhury, 2008), measured by a market-to-book ratio of equity.

Multiple regression with the SPSS application analyzed the data. The research model is as follows:

$$ICQ = \beta_0 + \beta_1 MA + \beta_2 CI + e_1$$

$$BTM = \beta_0 + \beta_1 MA + \beta_2 CI + \beta_3 ICQ + e_2$$

Information:

ICQ : Internal Quality Control

MA : Managerial Ability

CI : Convergent Interest

B0- β_3 : Coefficient

BTM (Book-to Market ratio) : Conditional Conservatism

e1 e2 : Residual value

5. Result

5.1. Descriptive statistics test

The study used several variables namely managerial ability and convergent interest (as independent variables), internal quality control (as mediating variables), and accounting conservatism (as independent variables). The results of descriptive statistics are shown in Table 1 below:

Variable	N	Min	Max	Mean	Median	SD
MA	208	-.517	.543	-.1055	-.347	.4082
CI	208	5	20	11.52	11	3.658
ICQ	208	.42	.95	.7231	.7400	.11822
BTM	208	-.503	.546	.02134	-.0315	.3586
Fsize	208	14.634	19.502	17.611	17.419	2.021
MTB	208	1.176	2.932	2.231	1.826	3.754
Valid N (listwise)	208					

Table 1: Descriptive Statistics
Source: The Processed Secondary Data (2021)

Table 1 shows that the managerial ability variable has a mean of -.1055 with a standard deviation of 0.4082. It indicates that more than 40% of manufacturing companies have managerial abilities. The convergent interest has a mean of 11.52 with a standard deviation of 3.658. It confirms that more than 50% of managers have more than five years of tenure. The standard deviation of the convergent interest value is relatively high but still below the mean value. It means the data distribution is evenly distributed, thus indicating a good result. The standard deviation is a reflection of a very high deviation so that the spread of the data shows normal results

and does not cause bias. The internal control disclosure variable has a mean of 0.7231, illustrating that out of the 19 items of control disclosure, the companies disclosed only about 15 internal control items. These results indicated that the public's disclosure of internal control information had not been optimized. The mean value of the conditional conservatism (BTM) variable is 0.2134, with a standard deviation of 0.3586.

Table 2 shows the regression results of estimating equation. An effective multiple regression equation models fulfill the requirements of classical assumptions. The model must be free of multicollinearity, autocorrelation,

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heteroscedasticity, and have normal data. The previous analysis indicated that the proposed equation model fulfilled the requirements of classical assumption and was effective.

Table 2 shows the results for the first hypothesis (H1) to the fifth (H5). The first hypothesis showed the effects of managerial ability on internal quality control. The statistical test showed a significant value of 0.002 at the 5% level, proving the hypothesis. The second hypothesis claimed that managerial ability positively affects accounting conservatism, as shown by

the significant value of 0.010 at the 5% level. The third hypothesis that convergent interest positively affects the internal quality control was accepted by a significant value of 0.048 at the 5% level. The fourth hypothesis that convergent interest affects accounting conservatism showed a significant value of 0.007 at the 5% level. The fifth hypothesis that internal quality control affects accounting conservatism showed a significant value of 0.034 at the 5% level.

	Dependent Variable			
	BTM		ICQ	
Description	Coefficient	Sig	Coefficient	Sig
MA	.130	.010**	.156	.002**
CI	.224	.007**	.115	.048**
ICQ	.132	.034**		
Fsize	.340	.519	.940	.138
MTB	1.554	.092	1.077	.003**

Table 2: The Regression Results of Estimating Equation.

**significant at the level of 5%

Source: The Processed Secondary Data (2021)

6. Discussion

Managerial ability positively affects internal control quality. This indicates that the higher the manager's ability, skill, and experience, the more the achievement influence internal quality control. High-capacity managers use internal control disclosure to optimize internal control. According to the upper echelons theory, internal control disclosure is based on the manager's strategic decisions, with higher abilities, values, and cognitive-based to handle internal and external objective situations. The high-ability managers disclose internal control items as additional information for the company's financial statements users to make effective decisions. These results are supported by Li (2015) and Salehi et al. (2020) but are different from those of Lee (2015). Li (2015) established that managerial ability positively affects internal control quality. A strong ability depends on financial and non-financial motivation. Financial motivation is through incentives, while non-financial reflect reputation. Suppose the company's internal control achieves good quality when disclosing the internal control to the public; in that case, the public increases the firm value; consequently, the manager's reputation will also increase. Other impacts received by managers include: the board of directors can assess the ability of managers based on the achieved quality of internal control. The company's management also needs to know that the managerial ability is getting better, accompanied by a better quality of internal control. Therefore, the manager is motivated to support the disclosure of internal control as a proxy for internal quality control.

Managerial ability positively affect accounting conservatism. The upper echelons theory states that experience, education level, age, and social background will shape the manager's character with high abilities. It is supported by value and cognitive-based to determine the strategy of accounting conservatism application. The higher the capacity of the manager, the higher the company's chances to implement accounting conservatism. According to Haider et al. (2021), the positive effect of managerial ability on accounting conservatism has two interpretations. First, high-ability managers use their exceptional skills and expertise to apply conservatism accounting according to their efficient contracts. Second, high-ability managers follow conservatism to maintain reputation and future careers. They receive incentives and increased compensation for their performance. Furthermore, high-ability managers apply higher levels of accounting

conservatism. They report losses in the financial statements with the expectation of the company's debt contract suspension. These results are in line with Haider et al. (2021) dan Kamyabi & Nia (2021) but different from those of Kim et al. (2021).

Convergent interest positively affects internal quality control. It indicates that the manager's long tenure as a proxy of the variable convergent interest motivates decision-making that aligns with the shareholders' interests. It supports the public disclosure of internal control information. Convergent interest supports the managerial duties and responsibilities, including achieving internal quality control. The longer the manager's tenure, it will encourage the decision-making that aligns the interests of managers and shareholders to support the internal control information disclosure to the public. The findings follow the bonding approach of agency theory to prevent problems. There is a management binding program to align their interests with the shareholders. Schoepfer (2007) determined that longer tenure managers are less likely to commit violations because financial misstatements reflect weak internal control. These results align with Wertheim et al. (2016) but are different from Lin et al. (2014).

Convergent interest positively affects accounting conservatism. Managers with long tenures apply accounting conservatism principles in line with the company owners. Managers with long tenures reputation awareness prevent deviant accounting practices and apply accounting conservatism. The longer the manager's term, the more knowledge of the company's goals align with the company owner's interests. The owners maximize the firm value through quality financial reports and applying conservative accounting principles. Hsu et al. (2017) suggested that the longer the manager's term, the more conservative accounting principles applied for effective cash flow performance.

The fifth hypothesis stated that internal quality control positively affects accounting conservatism. Goh and Li (2011) stated that internal control disclosure items affect the company's decision to apply the accounting conservatism principle. The management uses internal control to minimize agency costs (Hooghiemstra et al., 2015). Companies with internal quality controls understand the conservatism role in contracting and reducing agency conflicts (Ji et al., 2016). An effective internal control system supports timely recognition of losses. Therefore, a strong internal control system motivates the application of accounting conservatism in the company's

financial statements. An effective internal quality control system encourages a good internal control culture that increases companies understanding of accounting conservatism benefits. According to Goh and Li (2011) and Mitra et al. (2013), internal quality control facilitates accounting conservatism. In contrast, weak internal control prevents timely loss recognition. Weak internal controls result in inaccurate

information and cannot recognize losses promptly, reducing accounting conservatism (Yin et al., 2020). For example, the accounting staff incorrectly estimates future assets cash flow such as goodwill and fixed assets or incorrectly identifies future cash flow reductions that would enable earlier recognition of losses.

Sobel Test		
Model	Direct & Total Effect	Indirect Effect
MA→BTM	.4132**	.3751
MA→ICQ	.3780**	.421
ICQ→BTM by controlling MA Variable	1254**	.4278
MA→BTM by controlling ICQ Variable	.2314**	.2519
MA→BTM through ICQ		.0969**
Bootstrap result for the indirect effect: 2.4125**		
Variance Accounted (VAF) for by indirect effect: .4651		

Table 3. Sobel Test Result for Managerial Ability, Internal Quality Control, and Accounting Conservatism

Notes: ** $p < 0.05$ Variance Accounted (VAF): $> 80\%$ full mediation, $20\% \leq \text{VAF} \leq 80\%$ Partial Mediation, $\text{VAF} < 20\%$ No mediation.

Source: The Processed Secondary Data (2021)

Table 3 shows the Sobel test that indicates the direct and total effect of managerial ability (MA) on accounting conservatism (BTM) is 0.4132 and on internal control quality (ICQ) is 0.3780. The direct and total effect of internal control quality (ICQ) on accounting conservatism (BTM) through managerial ability (MA) as the mediating variable is 0.1254, wthe managerial ability (MA) variables on accounting

conservatism (BTM) using internal control quality (ICQ) as the mediator is 0.2314. In the direct effect, managerial ability (MA) on accounting conservatism (BTM) through internal control quality (ICQ) is recorded as 2.4125. The VAF value of 0.4651 designates internal control quality (ICQ) as a partial mediator between managerial ability (MA) and accounting conservatism (BTM). However, all the values are at a significant level of 5%.

Sobel Test		
Model	Direct & Total Effect	Indirect Effect
CI→BTM	.8137**	.5671
CI→ICQ	.0821**	.1923
ICQ→BTM by controlling CI Variable	.4810**	.8147
CI→BTM by controlling ICQ Variable	.1824**	.2298
CI→BTM through ICQ		.0395**
Bootstrap result for indirect effect: 2.7890		
Variance Accounted (VAF) for by indirect effect: .3828		

Table 4: Sobel Test Results for Convergent Interest, Internal Control Quality and Accounting Conservatism

Notes: ** $p < 0.05$ Variance Accounted (VAF): $> 80\%$ full mediation, $20\% \leq \text{VAF} \leq 80\%$ Partial Mediation, $\text{VAF} < 20\%$ No mediation.

Source: The Processed Secondary Data (2021)

Table 4 shows the Sobel test and indicates that the direct and total effect of convergent interest (CI) on accounting conservatism (BTM) is 0.8137 and on internal control quality (ICQ) is 0.0821. The direct and total effect of internal control quality (ICQ) on accounting conservatism (BTM) through convergent interest (CI) as the controlling variable is 0.4810. The convergent interest (CI) variable on accounting conservatism (BTM) using internal control quality (ICQ) as the mediator is 0.1824. In the direct effect, convergent interest (CI) on accounting conservatism (BTM) through internal control quality (ICQ) is 2.7890. The VAF value of 0.3828 indicates that internal control quality (ICQ) was a partial mediator between convergent interest (CI) and accounting conservatism (BTM). However, all the values were at a significant level of 5%.

7. Conclusion

This study examined the relationship between managerial ability, convergent interest, internal quality control, and accounting conservatism. The results showed that internal quality control mediates between managerial ability and convergent interest with accounting conservatism. High-ability

managers enhance internal quality control through public disclosure of internal control to facilitate accounting conservatism. The manager's and shareholder's convergent interests support internal quality control for timely loss recognition. Therefore, a strong internal control system motivates the application of accounting conservatism in financial statements. An effective internal quality control system will create good internal control culture to increase companies understanding of accounting conservatism benefits.

This was the first study to examine a comprehensive model between managerial ability, convergent interest, internal quality control, and accounting conservatism. It added to the accounting conservatism literature and determinants. Furthermore, it established implications for regulators, shareholders, and stakeholders to assess managerial ability through financial statements. In addition, our research has implications for investors and other stakeholders in assessing managerial ability and convergent interest when applying accounting conservatism to financial statements or when making efficient contractual arrangements with managers. For regulators, this research can have implications for issuers in the capital market to encourage accounting conservatism. Accordingly, the quality of internal control will increase through

the disclosure of internal controls to the public.

The study limitations include the sampling period being only two years and collecting samples from manufacturing companies. Therefore, future studies can include samples for a longer period in all types of companies.

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