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**The Effect of Capital Structure and Litigation  
Risk on Accounting Prudence**

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**ABSTRACT**

This study aims to analyze the influence of capital structure and litigation risk on the implementation of prudent accounting in banking companies listed on the Indonesia Stock Exchange (IDX) for the 2022-2024 period. The principle of prudent accounting is crucial in the banking sector given the high level of risk, strict regulations, and demands for transparency and reliability of financial reports. This study uses a quantitative approach with library research and documentation techniques. The data used are secondary data in the form of annual financial reports of banking companies obtained from the official IDX website and the official websites of each company. The sample was determined using a purposive sampling method based on certain criteria: banking companies listed on the Indonesia Stock Exchange (IDX) during the study period, having been public companies for at least 15 years, and publishing complete and consecutive financial reports during the 2022-2024 period. Data analysis was performed using multiple linear regression with the aid of statistical software. The results show that capital structure influences prudent accounting, with companies with a certain scale and funding structure tending to demonstrate a lower level of prudence in financial reporting. Furthermore, litigation risk also influences prudent accounting, indicating that the higher the risk of lawsuits faced by a company, the lower the tendency of management to apply prudent accounting principles. These findings imply that financial characteristics and external pressures play a significant role in determining the level of accounting prudence in the banking sector.

*Prudent Accounting, Capital Structure, Litigation Risk, Banking, Indonesia Stock Exchange*

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**INTRODUCTION**

Every company is obliged to prepare and present financial reports in accordance with applicable Financial Accounting Standards (FAS). Financial reports are the final output of the entire accounting process, reflecting the company's financial condition and operational performance over a specific period (Sugiono & Untung, 2008). Furthermore, financial reports serve as a

form of management accountability for the management of company resources, serving as a basis for performance evaluation by both internal and external parties (Achyani et al., 2021). The information presented in financial reports serves as an important tool for stakeholders to understand the company's business activities and assess management's success in achieving company goals (Permatasari et al., 2024). Therefore, financial reports are expected to present relevant, reliable, and accurate information so that they can be used as a basis for informed decision-making (F. Rahmi, 2013).

SAK provides companies with the flexibility to choose accounting policies and principles that suit their business characteristics and conditions. One principle that can be applied in preparing financial statements is the principle of prudence, previously known as accounting conservatism. Within the conceptual framework of International Financial Reporting Standards (IFRS), the term conservatism is no longer explicitly used because IFRS-based financial statements must be relevant, reliable, understandable, comparable, and free from conservative bias (Odang & Rangkuti, 2023). Therefore, IFRS adopts the concept of prudence accounting as a form of rational and balanced prudence.

Prudence is the principle of caution in recognizing and measuring elements of financial statements, particularly those related to revenue, assets, and expenses, to anticipate future uncertainty (Aristiani et al., 2017). In the application of prudence accounting, recognition of revenue, profit, or a decrease in liabilities can be done even though they have not been fully realized, as long as they meet the recognition criteria set out in accounting standards. This principle emphasizes the use of professional judgment and a reasonable assessment of the potential economic benefits and burdens that will be received or borne by the company.

According to Mubarok et al. (2022), there are fundamental differences between the principles of prudence and conservatism in terms of revenue and expense recognition. The prudence principle allows for revenue recognition when the recognition requirements have been met even though cash has not yet been realized, whereas conservatism tends to delay revenue recognition until it is actually realized, while expenses are recognized earlier when there is an indication of the possibility of their occurrence. If a company does not adequately apply the prudence principle, the presented profit and assets have the potential to be overstated, thus not reflecting the true financial condition. The application of the prudence principle is important to anticipate the uncertainty of future economic events, as failure to do so can increase the risk of losses due to overly optimistic profit recognition in the current period (Heryadi & Agustina, 2023).

Failure to adhere to the principle of prudence in preparing financial statements can lead to material misstatements in the form of inflated profits and assets, ultimately making it difficult for companies to cope with losses in subsequent periods. Therefore, the application of prudential accounting is necessary to prevent financial statements from distorting information between periods and to provide a reliable basis for decision-making for stakeholders. However, in practice, the application of prudential accounting in Indonesia remains relatively low, as reflected in various cases of financial statement manipulation that demonstrate the weak application of the prudential principle in corporate financial reporting.

A series of banking cases in Bengkulu, such as the alleged misuse of customer funds at the Bengkulu Branch of Bank Syariah Indonesia (BSI) and the manipulation of credit facilities at Bank Raya Indonesia (BRI Agro Niaga), reflect the weak application of prudential accounting principles in banking practices. Prudential principles require banks to recognize potential losses as early as possible, maintain adequate reserves, and present financial reports conservatively to avoid concealing risks.

In these cases, indications of fund manipulation and problematic financing indicate that potential credit and operational risks were not detected or adequately disclosed in the financial statements at an early stage. Failure to implement prudential accounting resulted in delayed impairment allowances, weak internal controls, and the presentation of a bank's financial condition that appeared to be in good health. Consequently, losses were only revealed after they reached significant levels and had a broad impact on customers, the government, and public trust in the banking industry. This phenomenon confirms that inconsistent implementation of prudential accounting has the potential to increase moral hazard risks and weaken the supervisory function in maintaining financial system stability (jurnaldepok.id, 2025).

Previous research has shown differing findings regarding the effect of capital structure on accounting conservatism or prudence. Research conducted by Sidi (2022) and Handoko (2022) found that capital structure had no effect on accounting conservatism. Conversely, Arisa and Hakim (2021) found that capital structure had a significant effect on accounting conservatism. These differing results indicate a research gap that needs to be reexamined in the context of this study.

In addition to capital structure, litigation risk is also an external factor that has the potential to impact financial reporting practices. Litigation risk refers to the potential for legal action from creditors, investors, regulators, or other parties resulting from inaccurate financial reporting. High litigation risk can

incur significant costs, damage a company's reputation, and impact business continuity. Therefore, companies facing litigation risk tend to be more cautious in preparing financial statements to avoid lawsuits. However, under certain circumstances, high litigation risk can actually encourage companies to demonstrate better financial performance to maintain a positive image among investors and other stakeholders, potentially undermining the application of the prudent principle.

Research by Malenza et al. (2021) and Hardian et al. (2025) found that litigation risk significantly impacts prudence accounting. Meanwhile, Rahmi and Baroroh (2022) stated that litigation risk does not significantly impact prudence accounting. The inconsistency in these research findings indicates a research gap, necessitating further research.

Based on the background, empirical phenomena, and previous research findings that show variations in findings, this study is novel in its selection of variables, period, and research object. Unlike the research by Amalia et al. (2024) which examined the effect of information asymmetry, tax incentives, and litigation risk on prudence accounting in the 2020–2022 period in the technology sector, this study uses independent variables of capital structure, financial distress, and litigation risk, which are theoretically closely related to the application of prudence accounting. Furthermore, this study uses the 2022–2024 observation period with banking sector companies listed on the Indonesia Stock Exchange as the object.

## **RESEARCH METHODS**

The research method used in this study is a quantitative approach with the aim of examining the effect of capital structure and litigation risk on prudence accounting. The data used is secondary data obtained from the financial statements of banking sector companies listed on the Indonesia Stock Exchange (IDX) during the period 2022–2024. The study population includes all banking companies listed on the IDX, with a purposive sampling technique based on certain criteria, namely banking companies that are consistently listed, publish financial reports consecutively, and have been listed on the IDX for a specified period.

Data analysis was performed using multiple linear regression analysis with the help of IBM SPSS software version 27. Before conducting the regression test, the data was first tested through the classical assumption test which includes normality, multicollinearity, heteroscedasticity, and autocorrelation tests to ensure the feasibility of the regression model. Hypothesis testing was carried out through the coefficient of determination ( $R^2$ )

test and the t-statistic test to determine the effect of the independent variables partially on the dependent variable. The results of this analysis are expected to be able to provide objective conclusions regarding the relationship between capital structure, litigation risk, and prudence accounting in banking companies.

## RESULT AND DISCUSSION

### Descriptive Test

**Table 1.**  
**Descriptive Statistics**

Variables	N	Minimum	Maximum	Mean	Standard Deviation
Company Size	78	24,098	1251,983	490.05367	263.843499
Litigation Risk	78	0.384	2,493	0.95511	0.429181
Prudence Accounting	78	-0.188	0.229	0.00362	0.065332
ROE	78	-4,287	20,888	7.21995	6.273133
Valid N (listwise)	78				

Source: processed data, 2026

Based on Table 1, the descriptive statistics results show that all research variables have a total of 78 observations (N). The company size variable has a minimum value of 24.098 and a maximum of 1,251.983 with an average value of 490.05367 and a standard deviation of 263.843499, indicating a fairly large variation in company size. Litigation risk has a minimum value of 0.384 and a maximum of 2.493 with a mean value of 0.95511 and a standard deviation of 0.429181, indicating that the company's level of litigation risk is relatively varied but still within a moderate range. Prudence accounting has a minimum value of -0.188 and a maximum of 0.229 with an average value of 0.00362 and a standard deviation of 0.065332, indicating that the company's level of accounting prudence tends to be low and close to zero. Meanwhile, ROE has a minimum value of -4.287 and a maximum of 20.888 with an average of 7.21995 and a standard deviation of 6.273133, which illustrates a significant difference in profitability levels between companies in the research sample.

### Classical Assumption Test

The classical assumption test was conducted to ensure that the regression model used in this study meets the basic assumptions so that the estimation results obtained are valid and unbiased. The tests performed included normality tests, multicollinearity tests, heteroscedasticity tests, and

autocorrelation tests. The results of the normality test using the Kolmogorov-Smirnov method showed a significance value of 0.200, which is greater than 0.05, thus it can be concluded that the residuals are normally distributed. Furthermore, the multicollinearity test showed that all independent variables had tolerance values above 0.10 and Variance Inflation Factor (VIF) values below 10, indicating there is no high correlation between the independent variables in the regression model.

In addition, the results of the heteroscedasticity test based on the scatterplot show that the residual distribution spreads randomly above and below the zero line without forming a specific pattern, so it can be concluded that the regression model does not experience heteroscedasticity. The autocorrelation test using the Durbin-Watson method produces a value of 2.106, which is in the range of  $dU < DW < (4 - dU)$ , thus indicating the absence of autocorrelation in the regression model. By fulfilling all the classical assumption tests, the regression model used in this study is declared feasible to proceed to the stage of multiple linear regression analysis and hypothesis testing.

### Multiple Linear Analysis

**Table 2.**  
**Results of Multiple Linear Analysis**

Independent Variables	Coefficient B	Direction of Influence	Information
Company Size	-0.00001097	Negative	Increasing company size decreases prudence accounting
Litigation Risk	-0.018	Negative	Increased litigation risk reduces prudence accounting
ROE	0,000	Positive	Increasing ROE tends to increase prudence accounting

Source: data processing using SPSS27, 2025.

Based on the results of multiple linear regression analysis on banking companies presented in Table 2, the regression equation  $PA = 0.023 - 0.00001097 UP - 0.018 RL + 0.000 ROE + e$  is obtained, which indicates that Company Size and Litigation Risk have a negative influence on Prudence Accounting, while ROE has a positive influence. The Company Size coefficient of  $-0.00001097$  indicates that the larger the company size, the level of accounting prudence tends to decrease, assuming other variables are constant.

Furthermore, the Litigation Risk coefficient of  $-0.018$  indicates that an increase in litigation risk is followed by a decrease in the application of prudence accounting. Meanwhile, ROE has a positive coefficient of  $0.000$ , which indicates that increasing profitability tends to encourage the application of prudence accounting principles, although the effect is relatively very small. Overall, these results indicate that company characteristics and risk levels play an important role in determining the level of prudence accounting in banking companies.

**Coefficient of Determination Test**

**Table 3.**  
**Determination Coefficient Test**

Model	R	R Square	Adjusted R Square	Information
1	0.575	0.331	0.303	The variables of Company Size, Litigation Risk, and ROE are able to explain 30.3% of the variation in Prudence Accounting.

Source: data processing using SPSS27, 2025.

Based on Table 3, the correlation coefficient (R) value of  $0.575$  indicates a fairly strong relationship between the variables of Company Size, Litigation Risk, and ROE with Prudence Accounting. The Adjusted R Square value of  $0.303$  indicates that the three independent variables simultaneously explain  $30.3\%$  of the variation in Prudence Accounting in the banking companies studied. Meanwhile,  $69.7\%$  of the variation in Prudence Accounting is influenced by factors other than this research model.

**t-test and F-test**

**Table 4.**  
**Results of t-Test and F-Test**

Testing	Variables	Direction of Influence	t count / Sig. F	Sig.	Information
t-test	Company Size	Negative	$-2,023$	$0.047$	Has a negative and significant impact on Prudence Accounting
t-test	Litigation Risk	Negative	$-5,503$	$< 0.001$	Has a negative and significant impact on Prudence Accounting
F test	Company Size, Litigation	-	Sig. F $< 0.001$	$< 0.05$	The regression model is fit and the independent variables have a

Testing	Variables	Direction of Influence	t count / Sig. F	Sig.	Information
	Risk, ROE				significant influence simultaneously.

Source: data processing using SPSS 27, 2026.

Based on the results of the hypothesis testing presented in Table 4, the t-test shows that Company Size and Litigation Risk partially have a negative and significant effect on Prudence Accounting, as indicated by the significance value of each variable being less than 0.05. This indicates that the larger the company size and the higher the litigation risk, the application of the principle of prudence accounting in banking companies tends to decrease. Furthermore, the results of the F-test show a significance value  $<0.001$ , which means the regression model used in this study is fit and able to explain the influence of the variables of Company Size, Litigation Risk, and ROE simultaneously on Prudence Accounting. Thus, the combination of these independent variables together has an important role in determining the level of prudence accounting in banking companies.

## Discussion

### Company Size Influences Prudence Accounting

Based on the results of the hypothesis testing, Company Size is proven to have a negative and significant effect on Prudence Accounting. This is indicated by the calculated t value of -2.023 with a significance level of 0.047 which is smaller than 0.05, so that hypothesis H1 is accepted. This finding indicates that the larger the size of a banking company, the level of implementation of prudence accounting tends to decrease.

Company size reflects the extent of its assets, operational complexity, and level of exposure to the public and capital markets. Large banking companies generally face greater performance pressure from investors and regulators to demonstrate stability and profitability. This can encourage management to present less conservative financial statements to maintain a positive performance image, resulting in a lower level of prudent accounting practice.

From the perspective of Positive Accounting Theory, specifically the political cost hypothesis, large companies tend to face higher political costs, such as increased regulatory scrutiny and public attention. To minimize these pressures, large company management may choose accounting policies that increase profits or reduce the level of prudence. This is in line with research findings showing a negative relationship between company size and prudence accounting.

The results of this study align with those of Husna Hasanah (2025), who found that company size significantly influences accounting prudence. This finding is also supported by Randi Hardian et al. (2021), who stated that company size influences accounting prudence. However, these results differ from several other studies that found no significant effect, indicating continued inconsistency in empirical findings related to the company size variable.

### **Profitability Affects Prudence Accounting**

The t-test results show that Litigation Risk has a negative and significant effect on Prudence Accounting, with a calculated t-value of -5.503 and a significance level  $<0.001$ . Thus, hypothesis H2 is accepted. This finding indicates that the higher the litigation risk faced by banking companies, the lower the level of prudence accounting implementation.

Litigation risk reflects a company's potential for facing legal action from external parties due to financial statements or managerial policies. In the banking context, high litigation risk can encourage management to present more optimistic financial performance to maintain investor and stakeholder confidence. Consequently, the application of prudent accounting principles is reduced.

Based on Positive Accounting Theory, specifically the litigation cost hypothesis, management will choose accounting policies that minimize the potential for lawsuits. However, under certain circumstances, management may actually reduce conservatism to make financial statements appear more stable and stable. This aligns with research findings showing that litigation risk negatively impacts prudence accounting.

The results of this study are consistent with the findings of Saadiah Syutiati Putri and Vinola Herawaty (2020), who stated that litigation risk has a negative and significant effect on accounting prudence. Similar findings were also presented by Randi Hardian et al. (2021), who found that litigation risk affects accounting prudence. However, these results differ from the research of Amarsya Aurelia Pamungkas and Tri Utami Lestari (2025), who found a positive effect of litigation risk on accounting conservatism, indicating differences in sector characteristics and study periods.

## **CONCLUSION**

Based on the analysis and discussion, this study concludes that company size and litigation risk negatively impact prudence accounting in banking companies listed on the Indonesia Stock Exchange. The larger the company, the lower the tendency to apply prudence principles in financial reporting, which is thought to be caused by high public pressure and performance expectations for

large-scale companies. Furthermore, the increasing litigation risk is accompanied by a decrease in the application of prudence accounting, indicating that management tends to present less conservative financial reports in an effort to maintain stability and the image of financial performance amid potential lawsuits.

Based on these conclusions, banking company management is expected to consistently apply prudential accounting principles regardless of company size or litigation risk levels to improve the quality, transparency, and credibility of financial reports. Investors and users of financial reports are advised to consider not only company size and profitability, but also the level of accounting prudence as an indicator of information quality and investment risk. Furthermore, further research is recommended to include other variables that could potentially influence prudential accounting, such as corporate governance mechanisms, information asymmetry, institutional ownership, or financial distress, as well as expand the research period and sectors to achieve more comprehensive and generalizable results.

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