

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) CONVERGENCE EFFECT TO ACCOUNTING CONSERVATISM

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Abstract

IFRS Convergence (International Financial Reporting Standards) is to adapt domestic standards to conform to IFRS (International Financial Reporting Standards). Implementation of accounting standards closely related to the selection of accounting methods. Each accounting method has a different level of conservatism. Conservatism is an attempt to choose acceptable public accounting methods that slow down the recognition of revenues, accelerate the recognition of expenses, lower the valuation of assets, and elevate the assessment of debt. This research is important to be done in an attempt to prove empirically an increase in accounting conservatism in the period after the convergence of International Financial Reporting Standards (IFRS), when compared to the period before the convergence of International Financial Reporting Standards (IFRS). The sample used in this research is PT. Indofood Sukses Makmur, Tbk with the observation period of 2010-2014. Paired-samples T-Test analysis will be used with SPSS (Statistical Package for Social Science) program Version 20. Study results shows that with the implementation of a financial accounting standards (IFRS Convergence) indicating a significant differences to Accounting conservatism value in PT. Indofood Sukses Makmur Tbk.

Key Words : *International Financial Reporting Standards (IFRS), Accounting Conservatism*

INTRODUCTION

Economy globalization marked with the appearance of multinational companies doing cross country transaction. These international transaction must be supported by global Accounting standard which can be compared. Accounting works as information provider for decision making. Therefore, the organization of Accounting is actively promoting convergence. IFRS convergence (*International Financial Reporting Standards*) is adjusting domestic standards to conform to IFRS

(*International Financial Reporting Standards*).

International Financial Reporting Standards (IFRS) are the standards and rules of financial information reporting established and approved by the FASB (Epstein et al, 2008). International Financial Reporting Standards (IFRS) is a single standard of high quality accounting report and a principle-based accounting framework that includes strong professional judgment with clear and transparent disclosures regarding the economic substance of transactions, explanations to reach certain conclusions, and accounting for such

transactions. Thus, users of financial statements can easily compare the entity's financial information between countries in different parts of the world.

The adoption of accounting standards is closely related to the choice of accounting methods, where each country has different languages, customs and cultures and accounting standards, accounting standards allow companies to choose accounting methods from a set of methods that can be applied under the same conditions, one of the most appropriate accounting methods. Each accounting method has a different level of conservatism.

The choice of accounting methods will affect the figures presented in the financial statements, both the balance sheet and the profit and loss of the company. Wolk et al. (2008) that defines conservatism as an attempt to select acceptable public accounting methods that slow down the recognition of revenues, accelerate the recognition of expenses, undermine asset valuations, and elevate debt assessments.

This research is important to be done in an attempt to prove empirically an increase in accounting conservatism in the period after the convergence of International Financial Reporting Standards (IFRS), when compared to the period before the convergence of International Financial Reporting Standards (IFRS).

LITERATURE

Agency theory is related to the relationship of principal and agent with the separation of ownership and control of the company (Jensen and Meckling, 1976). Wolk et al. (2008) states that agency theory is a theory that predicts and explains the behavior of the parties involved in a company. Some of the

important points derived from this theory are: Legally an agent is someone who works for the benefit of others., the agency theory treats the company as a "nexus" (intersection) of agency relationships, because on one side of management strives to maximize its welfare and on the other side of management strives to maximize the value of the company, and the theory seeks to understand organizational behavior by examining how the parties in the agency relating in order to maximize their own utility.

Signaling Theory

Wolk et al. (2008) suggests that agency theory provides a framework for analyzing what drives financial reporting between managers and owners, then the signal theory explains why firms have the motivation to voluntarily report on the stock market even though there is no necessity to report. The various motivations are:

1. Companies compete to minimize capital risk.
2. In order to compete successfully on capital markets for risky capital.
3. The ability of the company to increase its capital will increase if the company has a good reputation by complying with the rules of financial reporting.
4. Good reporting will undermine the company's capital cost as there is little uncertainty over the company that reports widely and reliably, resulting in fewer investment risks and lower rate of return liabilities.
5. Keep investors interested in the company.
6. The company has a good performance, so it is encouraged

to report the results of its operations.

7. The existence of competitive pressure will also force other companies to do the reporting even though the results are not good.

Positive Accounting Theory

Positive accounting theory evolves as the need to explain and predict the reality of existing accounting practices in society. Positive accounting theory seeks to explain the observed accounting phenomenon based on the reasons that led to the occurrence of an event. In other words, Positive Accounting Theory (PAT) is intended to explain and predict the consequences that occur if the manager determines a particular option.

At the present time the positive theory emphasizes explanations of the reasons for current practice and predictions of the role of accounting and related information in the economic, individual, corporate, and other economic interests that play a role in capital market and economic activities. Nevertheless, the assumptions underlying the positive research project are widely criticized because supporters of positive theories use alternative rejection of other aliases of thought. That is, positive theory is not free from value judgments or prescriptive implications. This is due to the consideration of implicit values often underlie or influence the form and content of research conducted. Researchers can not avoid the element of bias in all studies conducted. Thus the element of bias, clearly indicating the manifestation of the orientation of the researcher.

Convergence of International Financial Reporting Standards (IFRS)

The function of financial statements is as a tool for decision making which gives the consequence that the financial statements should present useful financial information in decision making. The Accounting information presented in the financial statements is in the form of accounts and numbers in the form of monetary units. Information processing within the Accounting cycle must pass through a single activity called measurement.

The changing climate of the economy, the never-ending price increase, has made Accounting measurements using historical cost principles to be questionable (Sparta, 2009). Longstanding criticism of measurement of Accounting with this principle is questioned by capital market actors. The decline in the natural resource content as the human population rises as the main creature on earth that contributes to the decline in the potential of natural resources, has proven that price reductions are extremely difficult and stable prices are difficult to achieve. The use of historical cost in Accounting measurement gradually becomes irrelevant in measuring the value of economic reality because historical cost only measures the completed transactions, does not recognize the real changes that occur (Anonymous, 2009).

Accounting measurement is closely related to the applicable standard Accounting, where each country has different language, customs and culture and Accounting standards, and then comes the term of standard Accounting harmonization. Harmonization is an attempt to understand the standard differences between countries and seek reconciliation to be comparable. Harmonization of international

Accounting standards means the process of improving the conformity of Accounting practices through the preparation of boundaries of different kinds (Choi, et al, 2002). Harmonization IAS (International Accounting Standards) trying to harmonize the differences that exist in order harmonious. IAS is a standard that multinational companies can use to bridge the differences between countries, in multinational commerce. Harmonization of IAS will ultimately lead to the convergence of IFRS (International Financial Accounting Standards). IFRS Convergence is adjusting domestic standards to conform to IFRS.

Benefits to be gained by IFRS convergence, namely that compliance to IFRS provides benefits to the comparability of financial statements and increased transparency. Through Compliance, the financial statements can be compared with the financial statements of other countries, so it will be very clear which company performance is better. In addition, the convergence program is also useful to reduce the cost of capital (cost of capital), increase global investment and reduce the burden of preparing financial statements.

One of the impacts of IFRS implementation is the application of fair value, which differs from market value due to the different main components. Since 1990, measurement mechanisms in financial reporting have been more likely to use fair value than historical use (Mard et al.2007, p.3). IFRS uses the concept of fair value with the advantage that financial statements become more relevant for the basis of decision making as it reflects actual market value. Based on the above description, this paper tries to describe some matters relating

to fair value evaluation as a measurement attribute in Accounting.

Harmonization leads more to International Accounting Standards (IAS), as convergence implies to the International Financial Reporting Standards (IFRS). Qu and Zhang (2008) define convergence as a converging action and in particular moves towards unity (union) or uniformity. Thus, convergence is adjusting domestic standards to conform to IFRS.

According to Suarrahman (2006), there are several obstacles in IFRS convergence, including: (1) translation of international standards; (2) non-compliance between international and national law standards; (3) the structure and complexity of international standards; (4) the frequency of changes in international standards; (5) the limitations of IFRS-based textbooks. Rahmany et.al. (2009) also argues that the IFRS convergence program will certainly lead to various impacts on business, among others: (1) Access to international tagging will be more open as financial statements will be more easily communicated to global investors; (2) The relevance of the financial statements will increase due to more fair use; (3) On the other hand, financial performance (income statement) will be more volatile if prices fluctuate; (4) Income Smoothing becomes more difficult with the use of the balance sheet approach and fair value; (5) Principle-based standards may result in the comparability of financial statements declining slightly when the use of professional judgment is oversupplied with the interest to manage earnings management; (6) The use of off balance sheet is more limited.

Accounting Conservatism

Financial Accounting Standards Board (1980) The Statement Of Financial Accounting Concept No.2 defines conservatism as a cautious reaction to uncertainty by trying to ensure that the uncertainties and risks inherent in business conditions are reasonably viable to consider. Therefore, if two estimates of the amount to be accepted or to be paid in the future are equal, the conservatism determines the use of the least optimistic estimate, if the sum of the two estimates is not the same, the conservatism does not determine to use a more pessimistic number than other possibilities.

Basu (1997) defines conservatism as a practice of reducing profits (lowering net assets) in responding to bad news, but not increasing profits (increasing net assets) in response to good news. Accounting Conservatism is an asymmetry in the verification request against profit and loss. This interpretation means that the greater the required rate of verification against profit versus loss, the higher the Accounting Conservatism level. As a result of asymmetric treatment of profit and loss verification in Accounting Conservatism is a persistent understatement of net asset value.

Watts (2003) defines conservatism as the difference in the verifiability required for the recognition of profit versus loss. Accounting Conservatism arises from incentives related to contract costs, litigation, taxes and political benefits to companies to reduce agency costs and reduce excessive payments to parties such as managers, shareholders, courts and government. In addition, conservatism also causes an understatement of earnings in the current period that

may lead to overstatement of earnings in subsequent periods, as a result of an understatement of costs over the period. The choice of Accounting method will affect the figures presented in the financial statements, both the balance sheet and the income statement of the company.

Another definition of Accounting Conservatism is based on the consequences of asymmetric treatment of profit and loss verification, proposed by Wolk et al. (B) accelerate the recognition of expenses, (c) undermine asset valuation, and (d) elevate the valuation of debt. This definition results in a net asset value that is persistently understatement.

Factors Affecting Accounting Conservatism

Lo (2005) states that there are several factors that affect the conservatism that is:

a. Leverage

The level of leverage can affect the level of Accounting Conservatism. In a company with relatively high debt, the creditor has a greater right to know and oversee the operation and Accounting of the company. Larger rights owned by creditors will reduce information asymmetry among creditors with corporate managers. Manager has difficulty to hide information from creditors. The creditor has an interest in the distribution of net assets and lower profits to managers and shareholders so that creditors tend to ask managers to administer conservative Accounting. Then the level of leverage has a positive relationship with Accounting Conservatism.

b. Size

Size of the company can affect the level of Accounting Conservatism. Large firms are usually more supervised by the government and society. If large firms have high profits relatively permanently, then the government can be encouraged to raise taxes and ask for higher public services to the company. Therefore, large firms will tend to report relatively low profits permanently by administering conservative Accounting.

Hypothesis

Based on the results of research Barth et.al (2008) companies that adopt IAS tend to be more conservative than companies that do not adopt IAS, because companies that adopt IAS tend to more often recognize losses than companies that do not adopt IAS. Based on the formulation of the theory and the results of the above research, the researchers put forward the following hypothesis.

H₁: Accounting Conservatism increases after the convergence of International Financial Reporting Standards (IFRS), when compared to before the convergence of International Financial Reporting Standards (IFRS).

1. RESEARCH METHODS

Population in this research is financial data of PT. Indofood Sukses Makmur Tbk. The research sample is financial report data from 2010 to 2014, with the year of separation in 2012 when the enactment of financial reporting based on International Financial Reporting Standards (IFRS) in Indonesia.

The data used in this study is secondary data in the form of data financial statements of the company, including balance sheet, income

statement / loss, cash flow statement PT. Indofood Sukses Makmur, Tbk.

The research variables used are Accounting Conservatism. The size of the conservatism used in this study refers to the size of the conservatism alternative developed by Lo (2005: 415-416), given that the measure has considered the premise that Accounting Conservatism is one of the causes of the discretionary accrual and a. As in Fala's (2007) study, the Accounting Conservatism alternative measurement used is the Accounting Conservatism (VIKV2_23) instrumental variable developed by Lo (2005) as the Accounting Conservatism gauge which is more appropriate to the manager's chances of choosing a conservative Accounting or liberal Accounting made possible by Standard Accounting Finance. Both manager's opportunities in choosing conservative Accounting or liberal Accounting are accommodated in the establishment of VIKV2_23 in INVRPDA and DEPA proxies.

Where:

VIKV2_23: VIKV formed from regression prediction value with dependent variable LBKNBLPJ and independent variable INVRPDA, UDA, ULUDA and DEPA. VIKV this is then referred to as ACCOUNTING CONSERVATISM (KONSV).

LBKNBLPJ: Excess of taxable income over income before income tax divided by total assets year t-1. LBKNBLPJ with a positive sign is an indicator of conservative Accounting, and vice versa.

INVRPDA: The abnormal trade receivable is the residuals of a cross-sectional receivable trade regression (PDjt) on the change in net sales

(PJLN_{jt}) for company j in year t, using the total assets of t-1 as deflator (A) as follows;

$$\frac{PD_{jt}}{A_{jt-1}} = \beta_{1it} \left(\frac{1}{A_{jt-1}} \right) + \beta_{2it} \left(\frac{\Delta PJLN_{jt}}{A_{jt-1}} \right) + \varepsilon_{jt}.$$

This study uses the inverse of accounts receivable abnormal (INVRPDA) divided by total assets t-1 year as a proxy of Accounting Conservatism level. INVRPDA is calculated by multiplying the PDA by -1. INVRPDA marked positive indicates conservative Accounting, and vice versa.

UDA: The abnormal trading debt is the residuals of a cross-sectional trade debt regression (UD_{jt}) on the change of goods for sale (KBD_{jt}) for the j year t corporation, using the total assets of t-1 as deflator (A) as follows;

$$\frac{UD_{jt}}{A_{jt-1}} = \delta_{1it} \left(\frac{1}{A_{jt-1}} \right) + \delta_{2it} \left(\frac{\Delta KBD_{jt}}{A_{jt-1}} \right) + \varepsilon_{jt}.$$

This study uses an abnormal trading debt (UDA) divided by total assets of year t-1 as a proxy of Accounting Conservatism level. UDAs with positive signals indicate conservative Accounting, and vice versa.

ULUDA: Current debt other than the abnormal trading debt is the residuals of a cross-sectional regression of current debt other than trade debt [on UL-UD] _{jt} on the change of net sales (PJLN_{jt}) for firm j in year t, using total assets t-1 as deflator (A) as follows;

$$\frac{(UL-UD)_{jt}}{A_{jt-1}} = \lambda_{1it} \left(\frac{1}{A_{jt-1}} \right) + \lambda_{2it} \left(\frac{\Delta PJLN_{jt}}{A_{jt-1}} \right) + \varepsilon_{jt}$$

The components of current debt other than trade payables are value added tax debt, gift debt, commission debt, contingent debt, and other unpaid costs. These components may vary against sales and operating costs. This study uses current debt in addition to the abnormal commercial debt (ULUDA) divided by total assets of year t-1 as a proxy of Accounting Conservatism level. ULUDA is a positive sign indicating conservative Accounting, and vice versa.

DEPA: Abnormal depreciation and amortization costs are the residuals of a cross-sectional regression of depreciation and amortization cost (DEP_{jt}) on gross fixed assets (ATB_{jt}) for firm j in year t, using the total assets of t-1 as deflator (A) as follows;

$$\frac{DEP_{jt}}{A_{jt-1}} = \gamma_{1it} \left(\frac{1}{A_{jt-1}} \right) + \gamma_{2it} \left(\frac{ATB_{jt}}{A_{jt-1}} \right) + \varepsilon_{jt}.$$

This study uses abnormal depreciation and amortization costs (DEPA) divided by total assets of year t-1 as proxy of Accounting Conservatism level. DEPA is a positive sign is a conservative Accounting indicator, and vice versa.

RESULT AND DISCUSSION

Descriptive Statistics

From table 4.1 it can be seen that the amount of Accounting Conservatism data used in each study amounted to 4 data (4 years) with explanation 2 years prior to IFRS implementation in 2010 and 2011 and 2 years after IFRS implementation that is in 2013 and 2014. Align the value of the Accounting Conservatism variable before the application of IFRS (SBLMIFRS) is -0.6573052 with an average rate of deviation of 0.87339354. The highest

Accounting Conservatism value is - 0.6573052 with an average rate of 0.03972 as the lowest value of deviation of 0.71343069. The highest Accounting Conservatism is -1, 27489. Accounting Conservatism value is The average of the Accounting 1.16178 as the lowest value of Conservatism variable value after the Accounting Conservatism is 0.15283. application of IFRS (STLHIFRS) is

Tabel. Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
SBLMFRS	2	-1.275	-0.3972	-	0.873
				0.657	
STUHFRS	2	0.153	1.16178	-	0.713
				.6573	

Source: Authors, (2017)

Determining Value of Research Variables

$$15.222.857.000.000 \\ = 0,91788$$

Determining the Value of Accounting Conservatism

Calculation of LBKNBLPJ for all sample companies as shown in Appendix 1.

An alternative measure of accounting conservatism used is the instrumental variables of accounting conservatism (KONSV) developed by Lo (2005). An example of determining the value of accounting conservatism at PT Indofood Sukses Makmur Tbk in 2011 as follows;

- a. Determine the value of LBKNBLPJ
The excess of taxable income over income before income tax divided by total assets year t-1. LBKNBLPJ with positive sign is an indicator of conservative accounting, and vice versa.

- b. Determine the value of INVRPDA
INVRPDA is calculated by multiplying the PDA dengan -1. INVRPDA with a positive sign indicates a conservative Accounting operation, and vice versa.

$$PD = \frac{\text{Piutang Dagang}}{\text{Total Aktiva}_{t-1}} \\ = \frac{638.191.000.000}{15.222.857.000.000} \\ = 0,04192$$

$$\text{Profit Taxable} = \text{Penj} - \text{B. Usaha} - \text{B. Depr} \\ = 19.367.155.000.000 - 2.422.511.000.000 - 226.942.000.000 \\ = 16.717.702.000.000$$

$$\text{Profit Before Tax} = 2.744.910.000.000$$

$$\text{LBKNBLPJ} = \frac{\text{Taxable Profit} - \text{Taxable Income Profit}}{\text{Total Assets}_{t-1}}$$

$$= \frac{16.717.702.000.000 - 2.744.910.000.000}{15.222.857.000.000} \\ = 0,09243$$

$$\text{PJLN} = \frac{\text{Penjl thn skrg} - \text{Penj thn sbelmnya}}{\text{Total Aktiva}_{t-1}} \\ = \frac{19.367.155.000.000 - 17.960.120.000.000}{15.222.857.000.000} \\ = 0,09243$$

After having the value of PD, do PJLN, then taken residual data from the regression results as the value of PDA (Piutang Dagang Abnormal) of -0,0015.

$$\begin{aligned}\text{INVRPDA} &= \text{PDA} \times -1 \\ &= -0,0015 \times -1 \\ &= 0,0015\end{aligned}$$

INVRPDA calculations for all sample companies as shown in Appendix 1.

c. Determine the value of UDA

This study uses utang dagang abnormal (UDA) divided by total assets of year t-1 as a proxy of Accounting Conservatism level. UDA with positive signals indicate conservative accounting operation, and vice versa.

$$\begin{aligned}\text{UD} &= \frac{\text{Utang Dagang}}{\text{Total Aktiva}_{t-1}} \\ &= \frac{638.191.000.000}{15.222.857.000.000} \\ &= 0,06350\end{aligned}$$

$$\begin{aligned}\text{KBD} &= \frac{\text{B. Penj thn skrg} - \text{B Penj thn sbelumnya}}{\text{Total Aktiva}_{t-1}} \\ &= \frac{14.335.896.000.000 - 12.993.217.000.000}{15.222.857.000.000} \\ &= 0,08820\end{aligned}$$

After obtaining the UD value, regression is done with KBD which then taken residual data from result of the regression as value of UDA (Utang Dagang Abnormal) equal to 0,00292. UDA calculations for all sample companies as shown in Appendix 1.

d. Determine the value of ULUDA

This study uses utang lancar selain utang dagang abnormal (ULUDA) divided by total assets of year t-1 as the proxy of accounting conservatism level. ULUDA with a

positive sign indicates a conservative accounting operation, and vice versa.

$$\begin{aligned}\text{ULUD} &= \frac{\text{Utang Lancar} - \text{Utang Dagang}}{\text{Total Aktiva}_{t-1}} \\ &= \frac{2.988.540.000.000 - 966.691.000.000}{15.222.857.000.000} \\ &= 0,13282\end{aligned}$$

$$\begin{aligned}\text{PJLN} &= \frac{\text{Penj thn skrng} - \text{Penj thn sbelumnya}}{\text{Total Aktiva}_{t-1}} \\ &= \frac{19.367.155.000.000 - 17.960.120.000.000}{15.222.857.000.000} \\ &= 0,09243\end{aligned}$$

After obtained ULUD value, regression was done with PJLN then taken residual data from the regression result as ULUDA value (Utang Lancar Selain Utang Dagang Abnormal) equal to -0,01901. The ULUDA calculations for all sample companies are shown in Appendix 1.

e. Determine the value of DEPA

This study uses biaya depresiasi and amortisasi abnormal (DEPA) divided by total assets of year t-1 as the proxy of Accounting Conservatism level. DEPA with a positive sign indicates a conservative Accounting operation, and vice versa.

$$\begin{aligned}\text{DEP} &= \frac{\text{Biaya Depresiasi}}{\text{Total Aktiva}_{t-1}} \\ &= \frac{226.942.000.000}{15.222.857.000.000} \\ &= 0,01491\end{aligned}$$

$$\begin{aligned}\text{ATB} &= \frac{\text{Aktiva Tetap Bruto}}{\text{Total Aktiva}_{t-1}} \\ &= \frac{4.993.918.000.000}{15.222.857.000.000} \\ &= 0,75309\end{aligned}$$

After obtained the value of DEP, regression with ATB is done and then taken residual data from the regression result as DEPA value (Biaya depresiasi abnormal) equal to 0,00117. DEPA calculations for all sample companies as shown in Appendix 1.

- f. Determine the value of KONSV
KONSV is variabel instrumental konservatisme (VIKV) formed from regression prediction value with LBKNBLPJ dependent variable equal to 0,91788 and independent variable of INVRPDA equal to 0.00150, UDA equal to -0,00292, ULUDA equal to -0,01901 and DEPA equal to 0,00117 after the regression is done then obtained the prediction value as the value of KONSV (Variabel Instrumental Konservatisme) of -1,27489. KONSV calculations for all sample companies as shown in Appendix 1.

Data Analysis

Detecting normality can be done by statistical tests. The statistical test used in this study was to use the Kolmogorov-Smirnov.

Based on results, the Kolmogorov-Smirnov value is 0.368 and significant at 0.999 for the data before and after the application of IFRS, this means H_0 is accepted which means the data is normally distributed. Normally distributed data is indicated by a significance value above 0.05 or 5%.

Hypothetical Testing Results

Paired-Samples T Test

From the results, obtained value equal to 0,055 significance. Because the value of significance is smaller than the level of significance used is 5%, so the results obtained that H_0 Denied and H_a Accepted which means that There is Difference between Accounting Conservatism Before and After Application of IFRS at PT.Indofood Sukses Makmur Tbk.

Research Results Discussion

The results obtained in this study using Paired-samples T-Test analysis or paired test using SPSS program (statistical package for social science) Version 20. From the results of this study, showed that with the application of the standard AI Accounting financial (IFRS Convergence) able shows a significant difference in the value of Accounting Conservatism in PT. Indofood Sukses Makmur Tbk. IFRS is useful in improving the quality of financial reporting, by allowing companies to choose the Accounting method from a set of methods that can be applied under the same conditions, so that the company can choose one of the most appropriate Accounting methods. Each Accounting method has a different level of conservatism. The choice of Accounting method will affect the figures presented in the financial statements, both the balance sheet and the income statement of the company.

CONCLUSION

Conclusion

Based on the discussion in the previous chapter, it is concluded that there is difference of value of Accounting Conservatism Before and After Application of IFRS at PT.Indofood Sukses Makmur Tbk.

Therefore this study can be continued with more and more varied sampling of

the biandg industry and the use of longer time spans of research resulting in more valid conclusions.

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