

IFRS Convergence, Accounting Conservatism, and Examination On Moderating Effect of Woman Presence in Audit Committee in Indonesia

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ABSTRACT

The purposes of this study are to examine (1) The effect of IFRS convergences on accounting conservatism, and (2) whether the presence of women in the audit committee weaker the effect of IFRS convergence and accounting conservatism. The samples obtain from manufacturing firms in Indonesia Stock Exchange with time period 2009 to 2011 and we obtain 113 firm-years observation. We obtain data from Indonesian Stock Exchange (IDX) website and Indonesian Capital Market Directory (ICMD). Multivariat regression conducted to analyze the model. The results show that IFRS convergences can decrease accounting conservatism. In addition, the presence of women in the audit committee weakens the effect of IFRS convergence and accounting conservatism linkage. This research has implication for regulators and standard setters to more concern about presence of women in audit committee for better accounting quality improvement.

Keywords: IFRS Convergences, Accounting Conservatism, accounting quality, audit Committee

1. Introduction

The practice of accounting conservatism in Indonesia lately become more interesting study because of the convergence of Indonesian accounting standards with IFRS. If the regulations in Indonesia have required the convergence of IFRS in preparing financial statements, the study of how IFRS can affect the level of conservatism in Indonesia become an interesting and important issue to examine. It is based on the consideration that conservatism reflects the quality of financial reporting. Examining the impact of IFRS on the conservatism can answer the question whether the convergence of IFRS give contribution in improving the quality of accounting information in Indonesia. In this paper, we examine the effect of IFRS convergence on accounting conservatism practices in Indonesia. Furthermore, this study also examine whether woman existance on audit committee moderate this effect.

Some researchers have argued that the convergence of IFRS have an influence on the practice of accounting conservatism on firms that adopt IFRS (Gassen and Sellhorn, 2006; Piot et al., 2011; Andre and Filip, 2012). Some previous researchers believe that the practice of accounting conservatism had declined after IFRS convergence (Piot et al., 2011; Andre and Filip, 2012). The use of fair value principles required in IFRS focuses on the relevance and application of accounting conservatism can reduce the focus on reliability. In the other hand, DeMaria and Dufour (2007) argue that the convergence of IFRS did not affect the practice of conservatism. Gassen and Sellhorn (2006) also argue that IFRS earnings tend to make more

conservative compared to local GAAP. It is because IFRS can limit opportunistic discretionary management by eliminating various alternative accounting rules that were previously permitted under local GAAP (Barth et al., 2008).

These Mixed result about the effect of IFRS on conservatism gives us motivation to provide more consistent result on this effect, especially in developing country like Indonesia. These also motivate us to consider another variable as moderate variable that can influence the IFRS convergence-conservatism linkage. We argue that gender differences, particularly presence of women on audit committee, can moderate the effect of IFRS convergence on conservatism. It is because women have a nature to avoid the risks and less aggressive than men. The presence of women at the top management level is believed to increase the practice of accounting conservatism in a firm (Thiruvadi and Huang, 2011; Francis et al., 2009; Peni and Vahamaa, 2010). The increasing of conservatism application according to gender theory is based on the nature of women who tend to avoid risk and less aggressive to avoid potential conflict and litigation that threatens his position in the top management (Francis et al., 2009). So when women in audit committee have to decide something, they are likely to make decisions that are conservative. Since audit committees have a vital role in assisting the board of commissioners to ensure that the financial statements are fairly presented in accordance with generally accepted accounting principles, thus this role can improve the quality of financial reporting. It means, women on audit committees should be able to increase the conservatism that could ultimately improve the quality of financial reporting. Finally we expect that presence of women on audit committee can weaker the effect of IFRS-conservatism linkage. Several studies (Thiruvadi and Huang, 2011; Francis et al., 2009; and Peni and Vahamaa 2010) showed consistent evidence that the presence of women in top management can inhibit earnings management through declining in discretionary accruals.

This study contributes to the literature in several ways. First, this research has implication for regulators and standard setters to more concern about presence of women on audit committee for better accounting quality improvement. Second, this research provide empirical evidence on the early effect of IFRS convergence on accounting conservatism and the role of women in the presence of an audit committee in weakening this effect in Indonesia.

II. Literature Review and Hypoteses Development

2.1. Related Literature

Conservatism is defined as the principle of prudence in financial reporting where the company was not in a hurry to recognize and measure income and assets as well as immediately recognize losses and debt is likely to have occurred. The application of this principle resulted in selection of accounting methods that aimed at the method reported lower earnings or assets and reported a higher debt (Watts, 2003a). Conservatism is one in accounting principle has profound implications for on assessment of the company's assets (Safiq, 2010). The examples of the practice of accounting conservatism are the selection of the LIFO method for inventory valuation compared to FIFO valuation method (if the stock price increases).

Previous studies that examined the convergence of IFRS and its impact on the application of accounting conservatism have mixed result. Some researchers concluded that the application of accounting conservatism declined significantly after the convergence of IFRS (Piot et al., 2011; Andre and Filip 2012). But different results obtained from Sellhorn Gassen (2006) as well as research DeMaria and Dufour (2007). Studies conducted by Francis et al., (2009) and Huang and Thiruvadi (2011) aimed to assess the relationship between the presence of women in top management to the application of accounting conservatism. Francis et al., (2009) was using the chief financial officer (CFO) and Thiruvadi and Huang (2011) was using a gender difference on the audit committee as a proxy of gender differences. The

results of both studies stated that the presence of women in top management (CFO and audit committee) can increase the level of the implementation of conservatism.

2.2 . Hypotheses Development

2.2.1. IFRS Convergences and Accounting Conservatism

Convergence IFRS as a guide in the preparation of financial statements in many country is a form of resistance and criticism of the principles of accounting conservatism (Safiq, 2010). The parties that criticize the accounting conservatism principle consider that the use of fair value in IFRS is more relevant for decision-making because the information is presented in accordance with economic realities. Conversely, the principles of accounting conservatism are considered more pessimistic because it does not disclose profits and losses in accordance with the economic realities but rather based on a conservative consideration.

Andre and Filip (2012) and Piot et al., (2011) failed to show evidence of a significant reduction in loss recognition asymmetry (bad news) in a timely relative to the recognition of gain (good news) after the period of convergence of IFRS on the European countries. This means that after the IFRS convergence, companies in Europe tend to be less conservative than it was before the convergence of IFRS.

Removal of the concept of conservatism on the IASB framework and the use of the fair value principle under IFRS make financial information more neutral (in the timeliness of recognition of bad news vs. good news) and relevant, under the recent economic conditions. In addition, IFRS is a principle-based standard that requires more estimates, perspective future outlook and the professional judgment of the accountants (Hoogendoorn, 2006 in Piot et al., 2011). Professional judgment may provide an incentive for management to act more aggressively in a realized gain. These things led to the convergence of accounting conservatism declined after IFRS convergence. Therefore, we expect negative relationship between IFRS convergence and conservatism. We propose the following hypotheses:

H1: *IFRS Convergence can mitigate the accounting conservatism practice.*

2.2.2. IFRS Convergence, The Presence of Women within the Audit Committee and the Accounting Conservatism Practice

In this study, we presume that the presence of women in top management weaker the effect of the implementation IFRS convergence on accounting conservatism. It is based on the argument that the presence of women at the top management level is believed to increase the application of accounting conservatism in a firm (Huang and Thiruvadi, 2011; Francis et al., 2009; Peni and Vahamaa, 2010). Francis et al., (2009) and Huang and Thiruvadi (2011) showed that the presence of women in top management (CFO and audit committee) can increase the level of the implementation of conservatism.

Conservatism is an accounting policy that relies heavily on the discretion of a company's top management. Based on the literature of psychology, there is a difference between men and women on leadership styles, communication skills, conservatism, and denial of risk to decision making. When compared with male executives, women executives tend to avoid risk, less aggressive and more conservative. The nature of women executive who avoid risk and less aggressive to avoid conflict and potential litigation that could threaten her position in the top management, can encourage women to report more conservative accounting than male executives. Therefore, we propose the following hypothesis:

H₂ : *The presence of women within audit committee weaker the relationship between IFRS convergence and accounting conservatism practice.*

III. Research Design

a. Data and Sampel Selection

In this study, we obtain data from Indonesian Stock Exchange (IDX) website and Indonesian Capital Market Directory (ICMD) with perodes from 2009 to 2011. We choosed our sample based on some criterias as follow. We exclude banking and financial industry from our observation, and choose manufacturing industry because the accrual model we used in this study is not fit for non-manufacturing industry (Na'im and Hartanto, 19996) and also in order to obtain the same characteristics. We also choose firms that have adopted Statement of Financial Accounting Standards (SFAS), which has been adopted from IFRS and that firms also have the data about audit committee. The firms also didn't do the merger activity or acquisition during the year of observation has all the data needed for the analysis and the financial statement publishes in IDR.

From these criteria, initially we obtain 114 firm-years observation. But then we exclude data that has outlier, and finally we have 113 firm-years observation obtain from Indonesian Stock Exchange (IDX).

b. Model Development

The following study will examine the effect of the implementation of IFRS converged on accounting conservatism and the role of gender differences within the audit committee membership in mitigating the relationship. Here is the model used in this research:

$$DACC_{it} = \beta_0 + \beta_1 IFRS + \beta_2 Women\ Size + \beta_3 |IFRS - Women\ Size| + \beta_4 Size + \beta_5 Profit + \beta_6 Lev + \beta_7 Sales\ Growth + \varepsilon_{it}$$

C. Variabel Operationalisation

1. Accounting Conservatism

Accounting conservatism in this study was measured using the Kasznik's model (1999) by using Discretionary Accrual. This study was using the accrual approach because according to Givoly and Hayn (2000) conservatism would create a consistent negative pattern of accruals. Discretionary accruals models used in this study is a Kasznik's model (1999), since these models cover the lack that exist in the Jones and Modified Jones models. (Haniati and fitriany, 2010:16). The formula discretionary accrual (DA) Kaznik's model is as follows:

$$DA_{it} = \frac{TA_{it}}{A_{t-1}} - \left(\alpha_1 \left(\frac{1}{A_{i,t-1}} \right) + \alpha_2 \left(\frac{\Delta REV_{it} - \Delta REC_{it}}{A_{i,t-1}} \right) + \alpha_3 \left(\frac{PPE_{it}}{A_{i,t-1}} \right) + \alpha_4 \left(\frac{\Delta CFO_{it}}{A_{i,t-1}} \right) + \varepsilon_{it} \right)$$

Where:

TA_{it} = Total accruals of firm i in t period

ΔREV_{it} = Income of firm i in t period less income of t-1 period

ΔREC_{it} = Accounts receivable (net) of firm i in t period less in t-1 period

ΔCFO_{it} = Cash flows from operating activities of firm i in t period less period t-1

$A_{i,t-1}$ = Total assets for firm i at the end of year t-1

$\varepsilon_{i,t}$ = Error term in year t for firm i

t = Years 1,2,3,, t (estimation period for firm i)

i = Firms 1,2,3.....,n

2. IFRS

The independent variable in this study is IFRS which is a dummy variable, where value of 1 for the period after the convergence of GAAP to IFRS, and 0 otherwise (Andre and Filip, 2012).

3. The Presence of Women in The Audit Committee

Gender differences which measured by the presence of women within the audit committee membership, be a moderating variable in this study. The presence of women in the membership of the audit committee was measured by women size. Women size define as the number of women in the membership of the audit committee (Thiruvadi and Huang, 2011).

IV. Analysis of Results

a. Descriptive Statistic

Description of the data in this study can be seen in table 2. In general it can be concluded that discretionary accruals (DACC) for the sample firms is 0.0579 and this number is positive. We also see the minimum value of the DACC at -0.17 million and a maximum value of 0.28, which means the company with the highest of accounting conservatism practice has a value of discretionary accruals equal to -0.17 and companies with the implementation of the low conservatism has a value of discretionary accruals amounting to 0.28. From the results of descriptive statistics can also be shown there is a minimum value of 0 indicates that there is a sample of firms that do not have an audit committee member with the female gender. The maximum value of 2 indicates that the sample firms have the highest number of female members of the audit committee by 2 people.

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
DACC	113	-.17	.28	.0579	.08237
IFRS	113	0	1	.66	.475
Women_Size	113	0	2	.50	.656
Size	113	11.12	18.71	14.1849	1.55569
Profit	113	-.21	.57	.1235	.13134
Lev	113	.01	.72	.1328	.14702
Sales_Growth	113	-.61	.78	.0993	.23390
Valid N (listwise)	113				

4.2. Analysis of the Implementation of IFRS Convergence Effect on Accounting Conservatism

Table 4 shows the hypotheses testing about the effect of the IFRS variable on the DACC variable. From table 4, we can see that IFRS variables significantly influence DACC variable because it resulted t value of 2.037, significance at 0.044 ($p < 0.05$). From the test results, coefficient β_1 is 0.017. This means that hypothesis one is supported statistically.

Coefficient of β_1 give positif sign, which means that the convergence of IFRS has positive effect on discretionary accruals (DACC). The convergence of PSAK to IFRS will increase the discretionary accrual. According in Sulistiawan, et al (2011: 51), the higher values of accruals indicate a strategy increasing profits because the profits are affected by accounting policy (discretionary accrual). A strategy of increasing profits is not consistent with the conservatism principles that produce consequences reporting lower profits. Thus,

this study concluded that the convergence of PSAK with IFRS can reduce the accounting conservatism practice. The results are consistent with Piot et al., (2011) and Andre and Filip (2012).

4.3. Analysis the presence of women in Audit Committee in the Relationship Between IFRS Convergence and Accounting Conservatism

Table 4 shows results of hypothesis 2. t value is -1.688, significance at 0.094 ($p < 0.10$) and values for the coefficient β_3 of -0.014. It means the interaction of IFRS convergence and the presence of women in the audit committee membership negatively affect the discretionary accrual, interaction between IFRS convergence and the presence of women in the audit committee membership will decrease discretionary accruals. Decreasing discretionary accruals indicate implementation of more conservative accounting policies by the company. Based on the test results, it can be compared to the value of the coefficient β_1 IFRS convergence at 0.017 ($p < 0.05$) with a coefficient β_3 Absx1_x2 at -0.014 ($p < 0.10$) (see Table 4). This may imply that the presence of women in the audit committee could mitigate the influence of the convergence of PSAK with IFRS on the accounting conservatism practice. Accounting conservatism practice after PSAK convergence with IFRS which is previously has declined to increase the presence of women in audit committees (hypothesis 2 accepted).

$DACC_{it} = 0.074 + 0.017IFRS + 0.013Women\ Size - 0.014Absx1_x2 + 0.016Size - 0.015Profit - 0.024Lev + 0.013Sales\ Growth + \epsilon_{it}$					
Variabel	Predictied Sign	Coef	t	Sig.	
(Constant)	?	.074	6.211	.000 **	
Zscore(IFRS)	+	.017	2.037	.044 **	Significant
Zscore(Women_Size)	-	.013	1.836	.069 *	Significant
Absx1_x2	-	-0.014	-1.688	.094 *	Significant
Zscore(Size)	-	.016	2.303	.023 **	Significant
Zscore(Profit)	-	-0.015	-2.106	.038 **	Significant
Zscore(Lev)	-	-0.024	-3.171	.002 **	Significant
Zscore(Sales Growth)	+	.013	1.584	.116	Not Significant

The results explains that despite of convergence of PSAK with IFRS can mitigate accounting conservatism practice, the presence of women in the membership of the audit committee is another factor which can affect the relationship IFRS convergence towards the accounting conservatism practice. The presence of women in the audit committee membership could mitigate the effect the convergence of PSAK with IFRS on accounting conservatism practice. According Thiruvadi and Huang (2011) the presence of women in the audit committee membership could inhibit earnings management by increasing the negative discretionary accruals (earnings decline). The decline in earnings indicates the application of accounting policies are more conservative by the company. By nature, women in top management will tend to make judgments about accounting policies are more conservative. Conservatism is an accounting policy that relies heavily on the discretion of a company's top management.

V. Concluding Remark and Limitation

This study examines the effect of the convergence of PSAK with IFRS on accounting

conservatism practice in Indonesia, which proxies by discretionary accruals (DACC). In addition, this study also includes a variable of women size to test whether the presence of women in the audit committee membership could mitigate the effect of the application of IFRS convergence on accounting conservatism practice in Indonesia. The results of this study indicate that the convergence of PSAK with IFRS can significantly decrease accounting conservatism practice.

Furthermore, the results showed that the presence of women in the audit committee could mitigate the effect of the convergence of PSAK with IFRS on accounting conservatism practice. The results of this hypothesis explains despite of convergence of PSAK with IFRS can mitigate accounting conservatism practice, but the presence of women in the audit committee membership was another factor which can affect the relationship IFRS convergence towards the accounting conservatism practice. The presence of women in the audit committee membership could mitigate the effect of the convergence of PSAK with IFRS on accounting conservatism practice.

This study has several limitations, that is: (1) This research use only one method to measure conservatism. Future studies may add some method of measuring conservatism for more accurate results, (2) sample of companies who have women member in audit committee still a bit. Future studies may add observations from sectors other than manufacturing industry to get more samples of companies who have women member in audit committees(3) There are limitations in the use of proxy IFRS convergence. Future studies may develop this research by using another proxy for IFRS convergence in order to get more accurate results.

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