Qualitative Analysis of Financial Reporting Post Adoption of International Financial Reporting Standard

Comparative Study in South East Asia

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Abstract: The Implementation of Association of East Asian County Economy Community has increased the competition between countries, including the capital market competition. In the other hand, investor will analyze the information on the financial statement in making investment decision. The adoption of International Financial Reporting Standard belief will increase the financial reporting quality as it requires more disclosure, thus providing more understandable and comparable information. This study aims to analyze whether there are any changes in financial reporting quality post adoption of International Financial Reporting Standard (IFRS). We use listed companies at Indonesia Stock Exchange, Kuala Lumpur Syock Exchange and Singapore Stock Exchange as the subject in this research. We measure the financial reporting quality using qualitive measurement developed by Nijmegen Centre for Economics (NiCE), such as relevance, faithful representation, understandability, comparability, and timeliness. This study uses paired sample test for analysing the data. Based on the test, we found that qualitative characteristics of relevance, understandability and comparability are increased after the adoption, as more information being disclosed. Meanwhile the faithful representation is decreased as the new standard use principle base, which is involve more judgement. Thus, the international financial reporting standard will increase the financial reporting quality, except for representation faithfulness which involves many accounting judgment, so the financial statement user need to analyze its appropriateness, carefully.

1 INTRODUCTION

The Implementation of Association of East Asian County Economy Community has increased competition between countries, including competitions to attract the foreign capital. Many countries adopting the International Financial Reporting Standards (IFRS), which will elevate the quality of financial report, including Indonesia, Singapore and Malaysia. IFRS adoption will provide more qualified information by providing more comparable and understandable information, among companies. Formerly each country has different accounting treatment, as the accounting standard is adjusted with the needs a condition of the country. To increase the financial statement comparability and quality in the global market, we need to set an international accepted accounting standard.

Previous study on the impact of International Financial Reporting Standard adoption in the financial statement quality by Healy and Wahlen (1999), Leuz and Verrechia (2000), Daske et al. (2008), and Amstrong et al. (2008), found that the quality of financial statement is increased after the adoption. They measure the financial statement quality using quantitative measurement. However, research by Barth et al. (2008), Daske et al. (2008), Karampinis and Hevas (2011), Alali and Foote (2012), found that the financial statement will have more relevance quality after adoption of IFRS since its widely use the fair value measurement. Yurisandi and Puspitasari (2015) research on the quality of financial reporting after the IFRS adoption in Indonesia, using Nijmegen Centre for Economics qualitative measurement found that the financial reporting was increased. This study also used the qualitative measurement to analyze the financial reporting quality post the IFRS adoption in several South East Asia Countries.

Previously, Indonesia adopted the Financial Accounting Standard of US (US GAAP) into

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Standar Akuntansi Keuangan (SAK). At the beginning of 2012, as a commitment of G-20 member (Daske et al., 2008), Indonesia adopted International Reporting Standard (IFRS). The IFRS convergence in Malaysia into Malaysian Financial Reporting Standard (MFRS) begun on January 1, 2012. In 2009, the Singapore Accounting Standards Council (ASC) announced to conduct full convergence with IFRS in 2012.

This study aims to analyze whether there are any changes in financial reporting quality after International Financial Reporting Standard adoption in Indonesia, Malaysia and Singapore. We use paired sample test to analyse the data. We found that financial reporting quality is increased, for the relevance, understandability and comparability characteristic. As for representation faithfulness characteristic quality, it was decreased after the adoption.

2 LITERATURE REVIEW

Positive accounting theory (Watts and Zimmerman, 1986), says that policy and estimates for the management interest, which was supported by the study result by Healy and Wahlen (1999), and the management has intention to apply certain accounting Sweeney (1994). Therefore, we assume that after the IFRS adoption, the company will have more opportunity to apply the flexible accounting to fulfil their interest.

However, study by Healy and Wahlen (1999), Leuz and Verrechia (2000), Daske et al. (2008), and Amstrong et al. (2008), found that the asymmetry information after the IFRS adoption was decreasing, due to the increasing of the financial statement quality. Karampinis and Hevas (2011), Alali and Foote (2012), study found that implementing the IFRS will increase the information relevance on the financial statement as it uses fair value measurement, widely.

Iatridis and Rouvolis (2010), Lin and Paananen (2007), Ewart and Wagenholf (2013) performed the financial statement quality study by measuring the earnings management, before and after IFRS adoption. Ewart and Wagenholf (2013) found that more rigid accounting standard could decrease the earnings management and increase the financial statement quality. Yacoob and Ahmad (2011) found the timeliness in Malaysia was decreasing after IFRS adoption, which meant more time needed to issue the financial statement.

This research aims to evaluate whether there is any increasing in financial reporting quality after the IFRS adoption, in Indonesia, Singapore and Malaysia, use the NiCE qualitative approach. NiCE developed the comprehensive index of quality measurement based on qualitative characteristic such as relevance, faithful representation, understandability, comparability, and timeliness.

3 RESEARCH METHOD

3.1 Empirical Design

The purpose of this research is to empirically evaluating the financial reporting quality before and after the IFRS adoption, in each country. We perform mean comparation test using paired sample test. We use this model in order to find the level of significance of the financial reporting quality changes before and after IFRS adoption. We use SPSS program and Microsoft excel to run the data.

As we state earlier, researcher use the NiCE qualitative approach in measuring the financial reporting quality. NiCE developed the comprehensive financial reporting quality measurement in a form of index quality measurement based on the IASB (2008) and FASB (2008) each qualitative characteristic such as relevance, faithful representation, understandability, comparability, and timeliness. Here is the Nice measurement that we use in evaluating the financial reporting quality:

Table 1: NiCE quality measurement.

No	Question	Operationalization
Relevance		
R1	To what extent does the presence of the forwardlooking statement help forming expectations and predictions concerning the future of the company	1=no forward looking information; 2=forward looking information not an apart subsection; 3=apart subsection; 4=extensive predictions ; 5=Extensive predictions useful for making expectations
R2	To what extent does the presence of non financial information in terms of business opportunities and risks complement the financial information	1=No non-financial information; 2=little non-financial information, no useful for forming expectations; 3=useful non-financail information; 4=useful non financial information, helfpul for developing expectations
R3	To what extent does the company use fair value instead of historical cost	1=Only Historical cost (HC); 2=Most HC; 3=Balance Fair value (FV)/HC; 4=Most FV; 5=Only FV
R4	To what extent do the reported results provide feedback to the users of the annual reports as to how various market events and	1=No feedback; 2=Little feedback on the past; 3=Feedback is present; 4=Feedback helps understanding how events and

No	Question	Operationalization
	significant transactions affected the company	transactions influenced the company; 5=Comprehensive feedback
Faithful Representation		
F1	To what extent are valid arguments provided to support the decision for certain assumptions and estimates in the annual report	1=Only described estimations; 2=General explanations; 3=Specific explanation of estimations; 4=Specific explanation, formulas explained, etc; 5=Comprehensive argumentation
F2	To what extent does the company base its choice for certain accounting principles on valid arguments	1=Changes not explained; 2=Minimum explanation; 3=Explained why; 4=Explained why + consequences- 5=No changes or comprehensive explanation
F3	To what extent does the company, in the discussion of the annual results, highliht the positive events as well as the negative events	1=Negative events only mentiond in footnotes; 2=Emphasize on positive events; 3=Emphasize on positive events, but negative events are mentioned; no negative events occured; 4=Balance positive/negative events; 5=Impact of positive/negative events is also explained
F4	Which type of auditors' report is included in the annual report	1=Adverse opinion; 2=Disclaimer of opinion; 3=Qualified opinion; 4=Unqualified opinion: Financial figure; 5=Unqualified opinion: Financial figures + Internal Control
F5	To what extent does the company provie information on corporate governance	1=No description CG; 2=Information on CG limited, not in apart subsection; 3=Apart subsection; 4=Extra attention paid to information concerning CG; 5=Comprehensive description of CG Continue
Understandability		
U1	To what extent is the annual report presented in a well organized manner	Judgment based on: -Complete tabel of contents; -Headings; -Order of components; -Summary/conclusion at the each subsection
U2	To what extent are the notes to the balance sheet and the income statement sufficiently clear	1=No explanation; 2=Very short description, difficult to understand; 3=Explanation that describes what happens; 4=Terms are explained (which assumptions etc); 5=Everything that might be difficult to undertand is explained
U3	To what extent does the presence of graphs and tables clarifies the presented information	1=No graphs; 2=1-2 graphs; 3=3-5 graphs; 4=6-10 graphs; 5=>5graphs
U4	To what extent is the use of language and technical judgment in the annual report easy to follow	1=Much jargon (industry), not explained; 2=Much jargon, minimal explanation; 4=Not much jargon or well explained; 5=No jargon or extraordinary explanation
U5	What is the size of the glossary	1=No glossary; 2=Less than 1 page; 3=Approximately one page; 4=1-2 pages; 5=>2 pages
Comparability		
C1	To what extent do the notes to changes in accounting policies explain in the informations of the change	1=Changes not explained; 2=Minimum explanation; 3=Explained why; 4=Explain why + consequences; 5=No changes or comprehensive explanation
C2	To what extent do the notes to revisions in accounting estimates and judgements explain the implications of the revision	1=Revision without notes; 2=Revision with few notes; 3=No revision/clear notes; 4=Clear notes + implications (past); 5=Comprehensive notes
C3	To what extent did the company adjust previous accounting periods figures for the effect of the implementation of a change in accounting policy or revisions in accounting estimates	1=No adjustments; 2=Described adjustments; 3=Actual Adjustments (one year); 4=2 Years; 5=>2 years + notes
C4	To what extent does the company provide comparation of the current accounting periode with previous accounting period	1=No comparation; 2=Only with previous year; 3=With 5 years; 4=5 years + description of implications; 5=10 years + description of implications
C5	To what extent is the information in the annual report comparable to information provided by the other organizations	Judgment based on: -accounting policies; -structure -explanations of events; In other words: an overall conclusion of comparability compared to annual reports of other organizations
C6	To what extent does the company presents financial index numbers and ratios in the annual reports	1=No ratios; 2=1-2 ratios; 3=3-5 ratios; 4=6-10 ratios 5=>10ratios
Timeliness		
T1	How many days did it take for the auditor to sign the auditors' report after bookyear end	Natural logarithm of amount of days 1=1-1,99; 2=2-2,99; 3=3-3,99; 4=4-4,99; 5=5-5,99

Source: Nice Working Paper 09-108

3.2 Sample

Companies stock which is included in LQ-45 index at Indonesian Stock Exchange, most active stock at Kuala Lumpur Stock Exchange (KLSE), and Singapore Stock Exchange (SGX) for the period 2009 - 2013 are used as the subject in this research. These listed companies consist of the companies with the highest market capitalization. We are using these companies as the sample with the consideration that they could work as a representation for the implementation of the IFRS adoption.

The financial reporting quality before the IFRS adoption is represented by the period 2009-2010, while the financial reporting quality after the adoption is represented by the period 2012-2013. The research is excluding 2011 period with the consideration it is the starting point of IFRS implementation. We also use the data provided in the company annual report.

4 RESULTS

Table 2 displays the mean of the financial reporting quality before and after IFRS adoption, the paired sample test result for LQ 45 stock, which being used as a sample.

From the table we found that the mean for relevance, understandability and comparability characteristic post IFRS adoption are increased. The mean for representational faithfulness characteristic is decreased after the adoption. Meanwhile for the timeliness characteristic, the mean is almost the same, before and after the adoption.

The study in Singapore Stock exchange and Kuala Lumpur Stock Exchange found that the mean for qualitative characteristics of relevance, understandability and comparability is increased, post IFRS adoption. Meanwhile for faithful representation and timeliness, the mean post IFRS adoption are relatively the same with the pre-adoption.

Table 2: Financial reporting quality result & t-test for LQ 45.

Quality		Mean		T test	Sig
		Before IFRS Adoption	After IFRS Adoption		
Relevance		3.2105	4.1058	-12.380	0.000
	R1	3.0455	4.0818		
	R2	3.6091	4.6909		
	R3	2.7636	3.5909		
	R4	3.4182	4.0545		
Representational Faithfulness		3.4055	3.0618	6.129	0.000
	F1	2.8182	3.7909		
	F2	2.9091	3.8364		
	F3	3.1000	3.6636		
	F4	4.0364	4.0182		
	F5	4.1636	4.7727		
Understandability		3.4455	3.8618	-9.662	0.000
	U1	4.1727	4.7727		
	U2	3.5455	4.3818		
	U3	4.0273	4.4727		
	U4	3.9455	4.2000		
	U5	1.5364	1.5273		
Comparability		3.0798	3.8351	-11.753	0.000
	C1	2.9636	3.7545		
	C2	3.1364	3.9909		
	C3	2.2091	3.8818		
	C4	1.9091	2.3818		
	C5	4.2182	4.7000		
	C6	4.0455	4.3000		
Timeliness	T1	2.6785	2.7347	-1.082	0.284
Financial Reporting Quality		3.2941	3.8827	-16.166	0.0000

Source: Data Calculation

5 DISCUSSION

The overall financial reporting quality after the IFRS adoption has increased the result is significant with the level 1% significance. We found the quality of financial reporting post IFRS adoption is increased for qualitative characteristics of relevance, understandability and comparability. However, we found that faithful representation is decrease and for timeliness it relatively the same. We presumed this empirical result for the timeliness is caused by the increasing demand for disclosures under IFRS, which make the company may need longer time in preparing the financial information. As for the representational faithfulness, we found the decreasing trend which we believe caused by the extensive use of the estimation and fair value in presenting financial information using the IFRS. The result is in accordance with the Barth et al. (2008), Yurisandi and Puspitasari (2015) study which revealed that there was an elevating in the accounting quality after the implementation of the IFRS. By using the IFRS, the relevance of the financial reporting is increasing compared to the use of the US GAAP.

Completing the previous study, this research found evidence that the comparability and understandability is higher after the IFRS adoption. The researchers presumed this happens because the company is required to provide more disclosures. In other word, our study proves that there is an increasing in the financial reporting quality after IFRS adoption. Further, the use of the principle-based standard is elevating the quality of the financial reporting by extending the disclosures.

6 CONCLUSIONS

This research aims to evaluate whether there is any increasing in financial reporting quality after the IFRS adoption, measured by the Nice measurement. From the test result we concluded that IFRS adoption increased the quality of financial reporting, for qualitative characteristics of relevance, understandability and comparability. Yet, faithful representation level is decreased and timeliness level remain the same, before and after IFRS adoption. We conclude that IFRS adoption did increase the quality of financial reporting. In the future, we suggest other researchers to expand this research by involving some other variables, such as involving the professional judgments in evaluating the financial reporting quality.

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