

## Analysis of Unconditional Conservatism and Earnings Quality before and after the IFRS Adoption

**Authors :** Monica Santi, Evita Puspitasari

**Abstract :** International Financial Reporting Standard (IFRS) has developed the principle based accounting standard. Based on this, IASB then eliminated the conservatism concept within accounting framework. Conservatism concept represents a prudent reaction to uncertainty to try to ensure that uncertainties and risk inherent in business situations are adequately considered. The conservatism concept has two ingredients: conditional conservatism or ex-post (news depending prudence) and unconditional conservatism or ex-ante (news-independent prudence). IFRS in substance disregards the unconditional conservatism because the unconditional conservatism can cause the understatement assets or overstated liabilities, and eventually the financial statement would be irrelevant since the information does not represent the real fact. Therefore, the IASB eliminate the conservatism concept. However, it does not decrease the practice of unconditional conservatism in the financial statement reporting. Therefore, we expected the earnings quality would be affected because of this situation, even though the IFRS implementation was expected to increase the earnings quality. The objective of this study was to provide empirical findings about the unconditional conservatism and the earnings quality before and after the IFRS adoption. The earnings per accrual measure were used as the proxy for the unconditional conservatism. If the earnings per accrual were negative (positive), it meant the company was classified as the conservative (not conservative). The earnings quality was defined as the ability of the earnings in reflecting the future earnings by considering the earnings persistence and stability. We used the earnings response coefficient (ERC) as the proxy for the earnings quality. ERC measured the extent of a security's abnormal market return in response to the unexpected component of reporting earnings of the firm issuing that security. The higher ERC indicated the higher earnings quality. The manufacturing companies listed in the Indonesian Stock Exchange (IDX) were used as the sample companies, and the 2009-2010 period was used to represent the condition before the IFRS adoption, and 2011-2013 was used to represent the condition after the IFRS adoption. Data was analyzed using the Mann-Whitney test and regression analysis. We used the firm size as the control variable with the consideration the firm size would affect the earnings quality of the company. This study had proved that the unconditional conservatism had not changed, either before and after the IFRS adoption period. However, we found the different findings for the earnings quality. The earnings quality had decreased after the IFRS adoption period. This empirical results implied that the earnings quality before the IFRS adoption was higher. This study also had found that the unconditional conservatism positively influenced the earnings quality insignificantly. The findings implied that the implementation of the IFRS had not decreased the unconditional conservatism practice and has not altered the earnings quality of the manufacturing company. Further, we found that the unconditional conservatism did not affect the earnings quality. Eventhough the empirical result shows that the unconditional conservatism gave positive influence to the earnings quality, but the influence was not significant. Thus, we concluded that the implementation of the IFRS did not increase the earnings quality.

**Keywords :** earnings quality, earnings response coefficient, IFRS Adoption, unconditional conservatism

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