
ACCOUNTING INQUIRIES
WITH NEW APPROACHES
IN THE
POST-PANDEMIC ERA

Volume 1

Editors

Prof. Dr. Iskandar MUDA

Dr. Muhammad Ali TARAR

Mr. Luigi Pio Leonardo CAVALIERE



Accounting Inquiries with New Approaches in the Post-Pandemic Era

Volume I



Editors

Prof. Dr. Iskandar MUDA
Dr. Muhammad Ali TARAR
Mr. Luigi Pio Leonardo CAVALIERE

Published by: NCM Publishing House

Publishing Date: 27.07.2022

ISBN: 978-605-73822-4-5

Copyright © The publishing rights of this book belong to **NCM Publishing**. The legal responsibility of the chapters belongs to the authors themselves. Except for the quotations to be made in accordance with the academic ethical rules and the short quotations to be made for promotional purposes, all or part of it cannot be printed, published, copied, reproduced or distributed electronically, mechanically or in part without the written permission. The authors are responsible for the content of the papers(chapters).

Accounting Inquiries with New Approaches in the Post-Pandemic Era

Volume I

Publication No:	9
Editors	<i>Prof. Dr. Iskandar MUDA</i> <i>Dr. Muhammad Ali TARAR</i> <i>Mr. Luigi Pio Leonardo CAVALIERE</i>
Cover Designer	<i>Mr. Kerim KARADAL</i>
ISBN	978-605-73822-4-5
Publisher Certificate No	51898
Publisher Type	International Publishing House
Release Date	2022



CONTACT

Phone: +90 554 888 1471
e-mail: ceocongress.info@gmail.com
www.ceocongress.org

LIBRARY INFORMATION CARD

MUDA, Iskandar; Editor, 2022. **Accounting Inquiries with New Approaches in the Post-Pandemic Era**
Volume I. NCM Publishing House, Bursa.
English
Authors: Prof. Dr. Iskandar MUDA; Dr. Muhammad Ali TARAR, Mr. Luigi Pio Leonardo CAVALIERE
ISBN **978-605-73822-4-5**

PREFACE

The development of the Industrial Revolution 4.0 brought changes to the adjustment of work in humans, machines, technology and processes in various professional fields, including the accounting profession. The Industrial Revolution requires the accounting profession to adapt to the development of information technology and big data. Facing today's latest industrial era, the development of the digital economy has opened up new possibilities while simultaneously increasing risk. These changes have a significant impact on the development of accounting. In this era, technological developments and innovations seem to keep pace with time. New innovations encourage the creation of new markets and shift the existence of old markets. Smart machines and robots are now taking on many roles and seem to rule the world. In the Industrial Revolution 4.0 there was an extraordinary shift in various fields of science and profession, therefore the way accountants work and practice needs to be changed to improve service quality and global expansion through online communication and the use of cloud computing and artificial intelligence.

Thank you for the hard work of the Steering Committee who has assessed the articles to be published in Accounting Inquiries with New Approaches in the Post-Pandemic Era - Volume.

This publication is dedicated to the world of science in the field of Accounting which is currently growing so rapidly. The development of Cloud Computing and Artificial Intelligence has played a role in changing the work order of Accountants.

Prof. Dr. Iskandar MUDA
Bursa - July 2022

CONTENTS

	<u>Page</u>
PREFACE	iii
Chapter 1 The Four Dimensions of Accounting Values and The Four Dimensions of Hofstede's Culture : Gray Hypothesis Accounting Value Putri Elysa Tarigan Hartiya Gesuri Iskandar Muda	5
Chapter 2 Accounting Policies and Changes in Accounting Policies on Retrospective and Prospective Local Governments in Indonesia Roy Satria Sri Lestari Saragih Elisa Fitri Iskandar Muda	14
Chapter 3 Approach and Criticism of Positive Accounting Theory (PAT) Juliana Safitri Nurzana Iskandar Muda	23
Chapter 4 The Models Implement of Financial Accounting Based on the Anglo-American Model Anastasia Miranda Rebecca Simatupang Rizki Isnani Fadhila Saragih Iskandar Muda	29
Chapter 5 The Effect of Budget Participation On Budget Slack With Budget Employment And Environmental Uncertainty As Moderating Variables Kaslim Sugiono Jessica Angelia Iskandar Muda	40
Chapter 6 The Origins of Positive Accounting Theory & How A Positive Theory Differs From A Normative Theory (The Anthropological Paradigm) Celine Royanti Sinaga Iskandar Muda	51
Chapter 7 Continental European Model - The Models Implement of Financial Accounting Bobby Ricardo Parasian Siregar Adela Oktaviani Simbolon Iskandar Muda	58
Chapter 8 The Types of Rewards that Organizations use and Positive and Negative Rewards Nazla Aminy	66

	Kurnia Dewi Iskandar Muda	
Chapter 9	Market-Based Bonus Schemes to Remunerate Managers in Terms of Market Value Evita Nora Manik Soraya Pramita Iskandar Muda	77
Chapter 10	Two Perspectives (Efficiency Perspective and Opportunistic Perspective) adopted by Positive Accounting Theory Research Donald J.R. Tobing Jonni William Panjaitan Iskandar Muda	87
Chapter 11	Three Key Hypotheses Often Used in the Positive Accounting Theory (PAT) Literature to Explain and Predict Support or Disapproval of Accounting Methods Dilla Nurhidayah Silvia Handayani Iskandar Muda	99
Chapter 12	Behavioral Implications of Airline Depreciation Accounting Policy Choice Abdurahman Hakim Nanda Dwi Kartika Iskandar Muda	108
Chapter 13	Cultural Dimension Model and The Effect of Culture On Accounting Systems Ricky Martin Sitorus Floren Asteria Giawa Iskandar Muda	116
Chapter 14	How Challenging Should Financial Performance Targets Be? Al Wahfi Suhada Sipahutar Ermadayani Iskandar Muda	127
Chapter 15	Debt Contracting: Agency Cost of Debt (A Monitoring Actions Between Debtholders Against Managers) Hasbi Aulia Siregar Henri Wiliam Dhani Iskandar Muda	134
	<i>Editor's Biographies</i>	146
	<i>NCM Publishing House Certificate</i>	147

CHAPTER 1

The Four Dimensions of Accounting Values and The Four Dimensions of Hofstede's Culture : Gray Hypothesis Accounting Value

Putri Elysa Tarigan¹, Hartiya Gesuri², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹ Correspondent Author Email: tyagesuri@gmail.com

ABSTRACT

The research aims to know about culture as a manifestation of social behavior and values in society plays an important role in creating accounting that is appropriate to the society in which accounting science is implemented. The hypothesis of the influence of culture on accounting. The purpose of this study is to test and produce proof of Gray's (1988) hypothesis in Indonesia in accounting values. The methods of this research is qualitative methods. The result explained the framework exploration combine four mark accountancy professionalism, uniformity, conservatism and secrecy and propose that values this can used for explain and predict difference international in system and pattern accounting.

Keywords : Value, Accounting, Hypothesis, Gray

1. INTRODUCTION

The development of accounting is influenced by various economic, social, and politics. Changes in the economic environment such as changes in ownership models companies, the level of industrialization, economic growth, to the political and legal aspects in a society will greatly affect the development of accounting in society (Noravesh, et al., 2007, Fachrizzu et al., 2020 and Sutrisno et al., 2020). Based on this research, evolution in accounting is influenced by different environmental factors, of which culture is the most important social factor (Gray and Vint, 1995 and Noravesh, et al. 2007). However, accounting research in Indonesia is still dominated by technical problems and tends to ignore the cultural values inherent in Indonesia (Chariri, 2009). Gray (1988) extended Hofstede's theoretical framework to develop a model showing the relationship between culture and accounting values. Environmental factors are constantly changing and with the increasing public demand for quality and reliable accounting, further demanding the accounting profession to be more professional and open, but with the high level of uncertainty in the economy, the idea arises of whether accounting should be carried out conservatively or optimistically (Ritonga et al., 2020). And there is also a consideration of whether accounting practices should be made uniform or flexible according to the situation and conditions.

2. LITERATURE REVIEW

2.1 Accounting and Culture Before Gray

Prior to Gray's study, no research had focused explicitly on the relationship between culture and accounting systems and practices. Previous research on international accounting differences considered the effects of various environmental factors on the development of accounting systems and the structural patterns that can be used to classify different accounting systems (Mueller, 1967; Zeff, 1971; Radebaugh LH, 1975; Nair & Frank, 1980, Simanjuntak et al., 2020). The nature of this study is discussed extensively in Gray's classic work (Gray, 1988).

2.2. Hofstede's Cultural Dimension

In his early research, Hofstede (Hofstede, 1980) identified four measurable dimensions that distinguish cultures. The data on which the development of this dimension is based comes from the results of a survey collected in one large multinational business organization (IBM) in 72 countries. The subsequent survey has a more diverse base. (Hofstede, 1980) The four original dimensions are:

1. **Individualism versus Collectivism (IDV)** - The fundamental issue addressed by this dimension is the degree of interdependence that society maintains among its members. It has to do with whether a person's self-image is defined in terms of 'I' or 'we'. In an individualist society, people are supposed to look after themselves and their immediate family only. In collectivist societies, people belong to a 'group' who cares for them in exchange for loyalty.
2. **Power Distance (PDI)** - This dimension relates to the fact that all individuals in society are not equal. It expresses the cultural attitude towards these inequalities among us. Power Distance is defined as the degree to which members of less powerful institutions and organizations in a country expect and accept that power is distributed unequally.

3. **Masculinity versus Femininity (MAS)** -A high or masculine score on this dimension indicates that society is driven by competition, achievement, and success, with success determined by the winner/best in their field – a value system that begins in school and continues throughout the lifetime of organizational behavior. Feminine scores on this dimension indicate that the dominant values in society are concern for others and quality of life. A feminine society is a society where quality of life is a sign of success. Standing out from the crowd is nothing short of awesome. The fundamental issue here is what motivates people - wanting to be the best (masculine) or liking what you do (feminine).

4. **Uncertainty Avoidance (UAI)** – This dimension has to do with the way society considers the fact that the future can never be known, i.e., should we try to control it or let it happen? This ambiguity brings anxiety, and different cultures have developed ways to deal with this anxiety. The extent to which members of a culture feel threatened by ambiguous/unknown situations and have created beliefs and institutions that avoid this is reflected in the UAI scores (Hofstede, 1980).

Furthermore, two additional cultural dimensions were established by Hofstede and colleagues. (Hofstede, 1980):

1. **Long-Term Orientation versus Short-Term Orientation (LTO)** - The Long-Term Orientation dimension is closely related to the teachings of Confucius and can be defined as dealing with society's search for virtue; that is, the degree to which society exhibits a pragmatic future-oriented perspective rather than a conventional historical short-term viewpoint.

2. **Indulgence versus Restraint (IVR)** - The Indulgence versus Restraint dimension consists of two poles. Indulgence is the tendency to allow the relatively free gratification of the basic and natural human desires associated with enjoying life and having fun. Restraint, the polar opposite, reflects the belief that such gratuities need to be limited and regulated by strict norms.

2.3. Gray's Accounting Value

Accounting values are the values used by accountants in doing accounting practice. Gray constructs a set of four accounting value dimensions derived from the four dimensions original Hofstede culture (Gray, 1988):

1. Professional versus legal control

This value reflects a preference for using professional judgment and determination of regulations based on professional judgment or instead, use judgment or statutory regulations. This value is a significant dimension of accounting value because accountants are expected to behave independently and use their professional judgment, and this value is more or less true for each country.

2. Conservatism versus optimism

This value reflects a preference to take a cautious approach to things that are uncertain in the future, or to take a more optimistic and risky approach. Conservatism or the precautionary principle in asset measurement and earnings reporting is seen as a fundamental behavior of accountants worldwide (Hendriksen and Van Breda, 2006).

3. Proximity versus transparency

This value reflects a preference to disclose information only to parties close to management and investors, or to disclose information in a more transparent, open and accountable manner. Companies tend to be less disclosing to outsiders, as a result of the asymmetric information world (Hendriksen and Van Breda, 2006). Proximity in accounting seems to be closely related to conservatism because both values apply a prudent approach to corporate financial reporting in general.

4. Uniformity versus flexibility.

This value reflects a preference to apply uniform and consistent accounting practices for all companies or apply flexible practices depending on the circumstances facing each company. This value is an important accounting value because behavior regarding uniformity, consistency and comparability is a qualitative characteristic of a financial report so that it can be used in decision making (Hendriksen and Van Breda, 2006). Uniform accounting practices will subsequently be more consistent, and easier to compare between periods and between other companies.

The relationship between the four dimensions of accounting values and the four dimensions of Hofstede's culture is shown in Table 1 and is defined in terms of the four proposed hypotheses by Gray (Gray, 1988).

Table 1. Four Hypotheses of Gray

H1	The higher a country ranks in terms of individualism and the lower it ranks in terms of uncertainty avoidance and power distance, the more likely it is to rank highly in terms of professionalism.
H2	The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism, the more likely it is to rank high in terms of uniformity.
H3	The higher a country ranks in terms of uncertainty avoidance and the lower it ranks in

	terms of individualism and masculinity, the more likely it is to rank highly in terms of conservatism.
H4	The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism and masculinity, the more likely it is to rank highly in terms of secrecy.

Gray refined the above hypothesis to reflect his assessment that for some of his accounting value dimensions, the association with Hofstede's four dimensions of culture was not as strong. For example, in the case of Conservatism, Gray noted a strong relationship with Uncertainty Avoidance (UAI), but a much weaker relationship with the other three dimensions; namely PDI, IDV, and MAS. For the value of Gray Uniformity and Professionalism, the Hofstede Power Distance dimension shows a weaker relationship than other cultural dimensions that have a determined relationship. Finally, for the accounting value dimension of Confidentiality versus Gray's Transparency, Hofstede's MAS shows a weaker relationship than any of the cultural dimensions that have a specific relationship. The above modifications made by Gray can be seen as an extension of his basic hypothesis about the relationship between his accounting value constructs and Hofstede's cultural dimensions (Gray, 1988).

Sudarwan (1994) showed in his research in Indonesia in the period 1983-1992 that power distance only affects conservatism and uniformity, where the relationship is positive. Uncertainty avoidance was positively related to professionalism, conservatism, and uniformity, and had a negative effect on closure. Individualism has a positive effect on all accounting values, and masculinity and time orientation have nothing to do with accounting values. Based on this study, accounting professionalism and flexibility in Spain increased, while conservatism and openness decreased. While individualism increased but power distance and uncertainty avoidance decreased (Noravesh et al., 2007).

In addition to comprehensive research that uses all of Gray's hypotheses, there are also several studies that use some of Gray's hypotheses. Like Hope, et al. (2008) which examined the relationship between introverts and professionalism related to choosing an auditor using a large and worldwide sample, which was 91,030 companies from 37 countries during 1992-2004. The results of this study prove that Gray's hypothesis regarding closure and professionalism is appropriate and can be applied in all countries.

Doupnik and Riccio (2006) examined the effect of conservatism and inclusiveness in relation to auditor behavior in interpreting accounting standards. uses 200 samples from Brazil and the United States, and shows that there are differences in auditor behavior in increasing earnings in the two countries with different cultures. In addition, this study also revealed that Gray. the hypothesis of Conservatism is universally applicable in Latin America.

3. METHOD

Data collection is carried out through surveys by distributing questionnaires to respondent either through an intermediary (contact person) or given directly to the individual concerned. The distribution of the questionnaire was carried out by visit one by one prospective respondents, check whether the candidates meet the requirements as a prospective respondent, then asked for their willingness to fill in the a list of questions. The distribution of this questionnaire was carried out by researchers and assisted by a number of research colleagues.

4. RESULTS AND DISCUSSION

Based on Hofstede (1980) four dimensions culture, Gray (1988) developed framework exploration combine four mark accountancy professionalism, uniformity, conservatism and secrecy and propose that values this " can " used for explain and predict difference international in system and pattern accounting. development accountancy by international” (Gray, 1988). by specifically, Gray (1988) hypothesized that dimensions Hofstede (1980) culture of distance power, individualism, avoidance uncertainty and masculinity determine mark accounting, which explains difference in system accountancy international. Framework deterministic and Gray's (1988) componential yield formulation simple hypothesis and defined by narrow like, " more " tall rating something country in Thing avoidance uncertainty and distance power and the more low the rating in Thing individualism and masculinity, more big the possibility. is rating tall in Thing secrecy" Remainder" from paper this arranged as following. Part first introduce framework mark Gray accounting and evaluate adoption and its implementation is not critical by researcher next. Part second focus on inspection disclosure finance in the accounting model Germany. Remember studies case German this part final conclude paper with highlight various reason popularity Gray skeleton in study accountancy international current main and recommend that study accountancy international will upgraded with consider factor history, social, economic and law. in something country than focus narrow on measurement, quantification, simplification and categorization (Gray, 1988). Chanchani and MacGregor adapted Table 2, placing mark Gray accounting as line and Hofstede's dimensions as column, with all notation permanent same (Chanchani & MacGregor, 1999) It is showed on Table 2.

Table 2. Summary Adaptation Relationship Between Dimensions Gray & Dimensional Accounting Hofstede Culture

	Distance Powers : PDI	Individualism : IDV	Manhood : THERAPY	Uncertainty Avoidance : UAI	Period long Orientation : LTO
Conservatism	+	-	-	+	+
Uniformity	+	+	?	+	+
Professionalism	-	-	?	-	-
Confidentiality	+	-	-	+	+

Besides adopt system different location, Chanchani and MacGregor inserts information connection addition about dimensions culture Fifth Hofstede Orientation Period Length (LTO). Information new this no explained or referred in article them. This thing could assumed for reflect opinion Chanchani and MacGregor about how dimensions mark accountancy four Gray related with Hofstede's LTO dimensions :

Table 3. Hofstede-Gray relationship for Four Dimension Original Hofstede With Notation Modifications

	Distance Powers	Individualism :	Manhood :	Uncertainty Avoidance :
--	------------------------	------------------------	------------------	--------------------------------

	: PDI	IDV	THERAPY	UAI
Conservatism	+	-	-	++
Uniformity	+	-	?	++
Professionalism	-	++	?	-
Confidentiality	++	-	-	++

In Table 3, couple Gray value and Hofstede's dimension which Gray referred to as strong by significant showed with use sign plus double (++) or double minus sign (- -), depending on strong whether or not connection that. is “ direct” or “ reverse ” (Gray, 1988). For example, in discuss Professionalism, Gray noted that IDV and UAI Hofstede are very related with mark His professionalism, while the PDI is related, but no so strong with mark Professionalism . Gray also noted that Masculinity no own clear relationship with Professionalism (Gray, 1988). All observation this reflected in Table 4 through extended notation. Noravesh et al (2007) conducted research on Gray's hypothesis in Iran for a period of 10 years (1993-2002). Noravesh et al could only confirm eight of Gray's twelve hypotheses. In their research, Noravesh et al. showed that distance power had a positive effect on professionalism, conservatism, closedness, and uniformity in accounting. Uncertainty and the power of distance avoidance have a negative effect on all accounting values. Meanwhile, masculinity has a negative effect on conservatism and inclusiveness.

5. CONCLUSION

Gray perfect hypothesis for reflect the rating that for a number of dimensions mark accounting, relationship with four dimensions Hofstede culture no same strong. For the value of Gray Uniformity and Professionalism, the Hofstede Power Distance dimension shows more connection weak compared dimensions culture others who have specified relationship. Finally, for dimensions mark accountancy Secrecy versus Gray Transparency, MAS Hofstede points out more relationship weak from on dimensions any culture that has connection certain. Modifications made by Gray can seen as expansion from hypothesis basic about connection Among construction mark the accounting and dimensions Hofstede's culture (Gray, 1988).

Based on Hofstede (1980) four dimensions culture, Gray (1988) developed framework exploration combine four mark accountancy professionalism, uniformity, conservatism and secrecy and propose that values this " can " used for explain and predict difference international in system and pattern accounting, development accountancy by international " (Gray, 1988). by specifically, Gray (1988) hypothesized that dimensions Hofstede (1980) culture of distance power, individualism, avoidance uncertainty and masculinity determine mark accounting , which explains difference in system accountancy international. Framework deterministic and Gray's (1988) componential yield formulation simple hypothesis and defined by narrow like, "more" tall rating something country in Thing avoidance uncertainty and distance power and the more low the rating in Thing individualism and masculinity, more big the possibility is rating tall in Thing secrecy" Remainder" from paper this arranged as following. Part first introduce framework mark Gray accounting and evaluate adoption and its implementation is not critical by researcher next. Part second focus on inspection disclosure finance in the accounting model Germany. Remember studies case German this part final conclude paper with highlight various reason popularity Gray skeleton in study accountancy international current main and recommend that study accountancy international will upgraded with consider factor history, social, economic and law in something country than focus narrow on measurement, quantification, simplification and categorization . (Gray, 1988). disclosure finance in the accounting model Germany. Remember studies case German this, part final conclude paper with highlight various reason popularity Gray skeleton in study accountancy international current main and recommend that study accountancy international will upgraded with consider factor history, social, economic and law. in something country than focus narrow on measurement, quantification, simplification and categorization.

REFERENCE

- Chanchani, S., & MacGregor, S. (1999). A Synthesis Studies Culture in Accounting. *Journal Accounting*, 18, 1-30.
- Chariri, A . (2009). Studying Financial Practices In Perspective Culture : Note For To do Research in the Indonesian Environment. *MAKSI UNDIP Journal*. 9(2). 115-138.
- Doupnik, T. S., & Riccio, E. L. (2006). The influence of conservatism and secrecy on the interpretation of verbal probability expressions in the Anglo and Latin cultural areas. *The International Journal of Accounting*, 41(3), 237-261.
- Doupnik, Timothy S., and Edson Luiz Riccio. 2006. Effects of Conservatism and Secrecy on the Interpretation of Verbal Probability Expressions in the Anglo and Latin Cultural Region. *International Journal of Accounting*. 41. 237-261.
- Fachrizzu, Nurhaliza, S & Mukhra (2020). The Radical Structuralist View in Accounting: Challenge The Social Order From A Realist, Positivist, Deterministic And Nomothetic Standpoint. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 995-999. <https://tojqi.net/index.php/journal/article/view/8213>.
- Gray, S. J. (1988). Towards a theory of cultural influence on the development of accounting systems internationally. *Abacus*, 24(1), 1-15.
- Gray, S. J., & Vint, H. M. (1995). The impact of culture on accounting disclosures: some international evidence. *Asia-Pacific Journal of Accounting*, 2(1), 33-43.
- Great, Oriol. et al. (1996). Dimensions of National Culture and the Accounting Environment - The Case of Spain. Paper work.
- Hendriksen, E. S., & van Breda, M. F. (2006). An Ethical Approach. *Accounting Ethics: Theories of accounting ethics and their dissemination*, 2, 48.

- Hofstede, G. (1980). *Consequence Culture : Difference International in Mark Related work*. Newbury Park, NJ: Sage.
- Hope, O. K., Kang, T., Thomas, W. B., & Vasvari, F. (2008). Pricing and mispricing effects of SFAS 131. *Journal of Business Finance & Accounting*, 35(3-4), 281-306.
- Mueller, GG (1967). *Accountancy International*. Macmillan.
- Nair, RD, & Frank, WG (1980). 'Impact Disclosure and Practice Measurement on Classification Accountancy International. *Overview Accounting*, 55(3), 426-450.
- Noravesh, Iraj., Dilami, Z.D, and Bazaz, M.Z. (2007). The impact of culture on accounting: Does the Gray Model Apply to Iran?. *Accounting and Financial Review*. 6(3). 254-272.
- Radebaugh, LH (1975). ' factor Environment Influence Development Objective Accounting , Standard and Practice in Peru. *Journal International Education and Study Accounting*, 11(1), 39-56
- Ritonga, R.R, Agustina, D.M Simanjuntak (2020). Is Accounting a Science? Mainstream Accounting Research Sees a Parallel Between Physical and Social Sciences and Accounting. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 984-994. <https://tojqi.net/index.php/journal/article/view/8212>
- Simanjuntak, A.M.B, Daulay, P, (2020). Feltham Model: A Framework for Determining The Value of A Change In The Information Decision (The Decision Maker). *Turkish Online Journal of Qualitative Inquiry*. 11(4). 964-977. <https://tojqi.net/index.php/journal/article/view/8209>
- Sudarwan, S. (1994). The dynamic relationship between culture and accounting: An empirical examination of the Indonesian setting (*Doctoral dissertation*, Case Western Reserve University).
- Sutrisno, Nasution, P.I.R, (2020). The radical humanist view in accounting. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 1000-1006. <https://tojqi.net/index.php/journal/article/view/8214>
- Zeff , SA (1971). *Forge Principle Accounting in Five Countries: History trend . stipe*.

CHAPTER 2

Accounting Policies and Changes in Accounting Policies on Retrospective and Prospective Local Governments in Indonesia

Roy Satria ¹, Sri Lestari Saragih ², Elisa Fitri ³, Iskandar Muda ⁴
^{1,2,,3,4} Universitas Sumatera Utara, Medan, Indonesia
¹ Email:roysatria@gmail.com

ABSTRACT

The purpose of this study is to analyze the accounting policies of retrospective and prospective local governments in Indonesia. The research method used is a literature study with a qualitative approach. Sources of data were obtained through searching articles related to accounting policies carried out by local governments in preparing financial reports. The data analysis technique was carried out by triangulating from various literature sources. The results of the study stated that local governments need to prepare financial reports in accordance with Law No. 17 of 2003 which refers to Government Accounting Standards (SAP). As a derivative of this regulation, the government has issued Government Regulation Number 24 of 2005 which was updated with Government Regulation Number 71 of 2010 concerning SAP. With this regulation, the basis of government accounting records changed from a cash basis to a cash basis to an accrual basis and to a full accrual basis.

Keywords : Accounting Policy, Local Government, Retrospective And Prospective

1. PRELIMINARY

Accounting policies relate to accounting principles that have been selected based on Government Accounting Standards to be applied in the preparation and presentation of Financial Statements (Tickell, et al., 2010). Local government accounting policies contain the main elements of Government Accounting Standards (SAP) which are described in the selection of an accounting method, both in recognition, measurement, and disclosure. Therefore, accounting policy is an accounting operational guideline for accounting functions in every regional organization (Bulycheva, 2022). In addition, accounting policies must also be guided by functions in local government, including: planning function, function of preparing Regional Revenue and Expenditure Budget (APBD), and function of implementing APBD (Ningtyas & Widyawati, 2015). Thus, there will be harmony between planning, budgeting, implementation, and regional financial reporting (Junita et al, 2019). Accounting policies are certain principles, principles, conventions, rules and practices that an entity applies in the preparation and presentation of financial statements (Atamirzaevich, 2022). Prior period errors are failures to include, and errors in recording, in the entity's financial statements for one or more prior periods arising from a failure to use, or misuse, reliable information that:

1. Available upon completion of the financial statements for the period; and
2. is rationally expected to be obtained and used in the preparation and presentation of the financial statements.

Such errors include the impact of mathematical calculation errors, incorrect application of accounting policies, errors or misinterpretation of facts, and fraud. Material An omission to include or an error in recording financial statement items is material if, alone or together, it could affect the economic decisions of users of financial statements (Prakarsa et al., 2022). Materiality depends on the size and nature of the omission or error in recording it, taking into account the circumstances. The size or nature of the financial statement items, or a combination of the two, can be a determining factor. Retrospective application is the application of a new accounting policy to transactions, events and other conditions as if the policy had been applied (Lubis et al., 2020). The prospective application of a change in accounting policy and the recognition of the effect of a change in an accounting estimate are, respectively:

1. Application of a new accounting policy for transactions, other events and conditions that occur after the date of the change in policy; and
2. Recognition of the effects of changes in accounting estimates in the current and future periods that are affected by these changes.

A retrospective restatement is the correction of the recognition, measurement, and disclosure of the amounts of the elements of the financial statements as if the prior period error had never occurred. A change in an accounting estimate is an adjustment to the carrying amount of an asset or liability, or the amount of periodic use of an asset, resulting from an assessment of the present status of, and the expected future benefits and liabilities associated with, the asset and liability. Changes in accounting estimates result from new information or new developments and, accordingly, not from correction of errors.

2. Literature review

Accounting Policy

When a PSAK specifically applies to a transaction, other event or condition, the accounting policy applied for that item uses that PSAK (Tarigan et al., 2022). In the absence of PSAK that specifically applies to transactions, other events or conditions, management uses its judgment in developing and implementing an accounting policy that produces relevant and reliable information. An entity selects and applies accounting policies consistently for similar transactions, other events and conditions, unless a PSAK specifically regulates or permits the grouping of items with different accounting policies is appropriate. If a PSAK regulates or permits such groupings, the appropriate

accounting policies are selected and applied consistently for each group. An entity changes an accounting policy only if the change:

1. Required by a PSAK; or
2. Produce financial statements that provide reliable and more relevant information about the impact of transactions, other events or conditions on the financial position, financial performance or cash flows of the entity.

Implementation of Changes in Accounting Policies:

1. The entity records changes in accounting policies as a result of the initial adoption of a PSAK as stipulated in the transitional provisions of that PSAK, if any; and
2. If an entity changes its accounting policy for the initial adoption of an SFAS that does not provide for transitional provisions for that change, or changes its accounting policy voluntarily, the entity shall apply the change retrospectively.

When a change in an accounting policy is applied retrospectively, an entity shall adjust the opening balance of each affected component of equity for the earliest period presented and other comparative amounts disclosed for each period presented as if the new accounting policy had been applied previously.

Accounting Estimation Changes

The effects of changes in accounting estimates are recognized prospectively in the income statement on: (Rautiainen et al., 2022)

1. The period of change, if the impact of the change is only in that period; or
2. Period of change and future periods, if the change affects both.

To the extent that a change in an accounting estimate results in a change in assets and liabilities, or is related to an item of equity, the change in the accounting estimate is recognized by adjusting the carrying amount of the related asset, liability or equity item in the period of the change.

Error

An entity shall retrospectively correct prior period material errors in the first complete financial statements issued following the discovery of the error by: (Nasution et al., 2022)

1. Restate the comparative amount for the previously presented period in which the error occurred; or
2. If the error occurred before the earliest presented period, restate the opening balances of assets, liabilities, and equity for the earliest period presented.

Statement of Financial Accounting Standards (PSAK) 25

1. Accounting Policy

Accounting policies are certain principles, principles, conventions, rules and practices that an entity applies in the preparation and presentation of financial statements.

1.1 Selection and Application of Accounting Policies

- SAK determines accounting policies to produce financial statements that contain relevant and reliable information on transactions, events and conditions
- When an SAK specifically applies to a transaction, other event or condition, the accounting policy applied to that item uses the relevant SAK and takes into account the relevant SAK Application Guidelines.
- In the absence of SAKs that specifically apply to transactions, other events or conditions, management uses its judgment in developing and implementing an accounting policy that produces relevant and reliable information.

1.2 Consistency of Accounting Policies

An entity selects and applies accounting policies consistently for similar transactions, other events and conditions, unless PSAK specifically regulates or permits groups of items where different accounting policies may be appropriate in the circumstances. If PSAK regulates or permits such grouping, the appropriate accounting policies are selected and applied consistently for each group.

1.3 Changes in Accounting Policies

An entity changes an accounting policy only if the change:

- Required by a PSAK
- Produce financial reports that provide reliable and more relevant information about the impact of transactions, other events or conditions on the financial position, financial performance or cash flows of the entity.

1.4 Implementation of Changes in Accounting Policies

Implementation of Changes in Accounting Policies depends on:

- An entity records changes in accounting policies as a result of the initial adoption of a PSAK.
- If no transitional provisions or policy changes are made voluntarily, the entity applies those changes retrospectively.

Types of Application of Changes in Accounting Policies: (Schmidhuber et al., 2022)

a . Retrospective Application

Retrospective application is the application of a new accounting policy to transactions, events and other conditions as if the policy had been applied since the beginning of the transaction. When a change in accounting policy is applied retrospectively, an entity shall adjust the opening balance of each affected component of equity for the earliest presented period and other comparative amounts are disclosed for each period presented as if the new accounting policy had been applied previously.

b . Prospective Application

Prospective Application is an application of the impact of changes in new accounting policies to transactions, events and other conditions that occur after the date of the change in policy.

1.5 Disclosure of changes in Accounting Policies

When a new standard or policy is applied, the entity must disclose the change if it has an effect on the current or prior periods or has an effect on future periods, but it is not practicable to determine the amount of adjustment required in the current or prior periods or required in future periods.

Entities must disclose:

1. PSAK title.
2. That the changes made are in accordance with the transitional requirements;
3. The nature of changes in accounting policies;
4. Where applicable, explanation of transitional provisions;
5. When applicable, transitional provisions that have an impact on future periods
6. For the current period and for each prior period present, as far as practicable, the adjustment amount for each affected financial statement item.

2. Accounting Estimation

2.1 Definition of Accounting Estimate

Accounting estimates are entity estimates that can affect elements in the financial statements.

2.2 Changes in Accounting Estimates

Changes in Accounting Estimates include Adjustments to the carrying amount of the asset or liability, or the amount of periodic use of the asset, resulting from an assessment of the current status of, and the expected future benefits and liabilities associated with, the asset and liability. Estimates may need to be revised if there are changes in the circumstances on which the estimates are based or as a result of new information or additional experience.

2.3 Disclosure of Changes in Accounting Estimates

An entity shall disclose the amount and nature of changes in accounting estimates, which have an effect in the current period. Likewise, the entity shall disclose the expected effect of the changes in future periods, if it is not practicable to do so.

3. Error

3.1 Scope of Errors

Errors may arise in the recognition, measurement, presentation or disclosure of elements of financial statements. A financial statement is not in accordance with PSAK if it contains:

- material error
- immaterial to achieve a certain statement of financial position, financial performance or cash flow presentation.

3.2 Past Period Error

Failure to include and misrepresentation in the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information.

3.3 Past Period Error Correction

An entity shall retrospectively correct prior period material errors in the first complete financial statements issued following its discovery by:

- Restate the comparative amount for the previous period the presentation in which the error occurred
- If the error occurred before the earliest presented prior period, restate the opening balances of assets, liabilities, and equity for the earliest presented prior period.

3.4 The Concept of Materiality

An omission or misstatement of an item is material if it, individually or collectively, affects the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size and nature of the omission or mis-recording taking into account the circumstances surrounding it. For example, an error of only a few thousand rupiah in the recording of assets that is declared as an expense on a company that has millions of rupiah in assets will be considered an immaterial error and no correction is needed.

3.5 Disclosure

In applying an error correction, an entity shall disclose:

- The nature of past period errors
- For each period presented, as far as practicable, the amount of correction:
 - For each affected financial statement item; and
 - If you apply PSAK 56: Earnings Per Share, then disclose basic and diluted earnings per share
- Amount of correction at the beginning of the earliest serving period
- If retrospective restatement is impracticable for a given period, the circumstances under which the condition existed and an explanation of how and since when the error has been corrected.

3. METHOD

This study uses a qualitative approach with the type of literature study research. Sources of data obtained from various references, both legislation, documentation of local government reports, as well as research related to accounting policies. The data that has been collected from the research process will then be analyzed by descriptive analysis. The process of analyzing qualitative data includes testing, selecting, categorizing, evaluating, comparing, synthesizing, and reflecting on the data that the researcher has obtained to build inferences and then draw conclusions so as to achieve a holistic understanding.

4. Results and Discussion

The Government is Responsible for the Implementation of the APBN/APBD/APBDes

The government is an institution of an organization that has supporting parts. In principle, in our government system there are 3 (three) elements of government, including: central government, regional government (consisting of provincial government, district/ city government), and village government. These three spheres of government, in accordance with statutory regulations, are

required to compile accountability reports from the implementation of the APBN, APBD, and APBDes.

In an effort to support clean government management, the government tries to continuously implement various reform efforts to support transparency and public accountability in terms of public finances. One of the concrete efforts to achieve transparency and accountability is through the presentation and submission of financial reports. The report is prepared based on the principles of preparing financial statements with reference to SAP which is generally understood, in accordance with Law no. 17 of 2003.

Local Governments are required to compile Financial Reports

Regional finances managed by local governments must be managed in an orderly manner, complying with laws and regulations, effective, efficient, economical, transparent, and responsible by taking into account the principles of justice, propriety, and benefits for the community. The preparation of financial statements must be presented in a form that is in accordance with the accounting standards regulated in PP. 24 of 2005 and PP No. 71 of 2010 on SAP. So, SAP is a reference in the presentation and preparation of financial statements that contain standard accounting principles that have legal force and are internationally recognized.

The preparation of financial statements depends on the accounting system adopted. So far, local governments, as explained by Suryanto (2018), have undergone several changes in the preparation and presentation of financial reports. Before the issuance of PP No. 24 of 2005, the preparation of financial statements adheres to the cash basis. However, since the issuance of the PP, in compiling financial statements using a cash toward accrual basis (cash toward accrual). Changes in the accounting system occurred again after the issuance of PP No. 71 of 2010 which requires the accounting system to use the accrual basis (Dewi et al., 2018). Especially with the issuance of Permendagri No. 64 of 2013 concerning accrual-based SAP in local governments certainly has an influence on the accounting system used by local governments.

Regional Government to Implement Accrual-Based Accounting

a. Government Accounting Standards (SAP)

SAP are accounting principles applied in preparing and presenting government financial statements (El Sima, 2020). Thus, SAP is a requirement that has legal force in an effort to improve the quality of government financial reports in Indonesia. Government Regulation No. 24 of 2005 regulates the Government's Accounting Standards based on cash basis and based on cash to accrual basis. Government Regulation Number 71 of 2010 regulates Government Accounting Standards on an accrual basis. Meanwhile, Permendagri Number 64 of 2013 concerning the application of accrual-based SAP to local governments.

b. Accounting Policy

Local government accounting policies are the basis for the preparation of financial statements. This policy contains the principles, or more specific rules chosen by local governments as financial reporting entities. Local government accounting policies usually regulate the basis of recognition, local government accounting policies regulate the basis of recognition, measurement methods, and accounting disclosure procedures for assets, debt, capital, income, expenditure, and financing as well as appearance in financial statements.

c. Local Government Accounting System (SAPD)

SAPD is an instrument to operationalize the accounting principles that have been set in SAP and accounting policies. SAPD shows a series of accounting processes consisting of identifying financial transactions, journalizing into journals, posting to ledgers, compiling trial balances, compiling consolidated working papers, and ending with the preparation of financial statements. SAPD is an important instrument that needs to be prepared in an effort to implement accrual-based SAP. SAPD is also a tool that can support the basic principles that are compatible with SAP.

Stages in Developing Accounting Policies in Local Government

The process of preparing local government accounting policies is carried out in stages. The first stage, the local government determines the basis for the preparation of accounting policies, namely SAP. The legal basis for determining accounting standards for government entities is PP No.71 of 2010 concerning SAP.

The second stage, the determination of accounting policies must be adjusted to each entity. The purpose of determining the most appropriate policy that is able to describe the economic reality of the accounting entity accurately with its financial condition and activities.

There are 3 (three) things that become the basis for consideration in determining the implementation of the most appropriate accounting policies, among others: First, sound considerations related to uncertainty in terms of transactions. Second, substance over form or substance that excels the formal form. Transactions need to be accounted for in accordance with the nature and reality of events, not only relying on the legal form of the transaction. Third, materiality, namely that each report needs to present sufficiently material components that can influence an assessment or decision.

After applying accounting principles, the next step is to determine the accounting method. The accounting method is a recording procedure related to economic transactions that have been carried out by local governments. To decide which accounting method to use, local governments can be assisted by conducting several analyzes. Accounting methods are generally standardized in a book that is part of a local government accounting system. Success in the preparation and implementation of accounting policies is determined by the Human Resources (HR) in the local government. Therefore, local governments must prepare their human resources to be able to work in accordance with the accounting policies adopted. This can actually be implemented by carrying out socialization and training.

5. CONCLUSIONS AND SUGGESTIONS

Accounting Policies and Changes in Accounting Policies are based on Transparency and accountability of regional financial management as reflected in the use of reported finances in accordance with applicable regulations and depending on the Entity recording changes in accounting policies due to the initial application of a PSAP as stipulated in the transitional provisions in the PSAP, if any, and If an entity changes an accounting policy for initial adoption of an PSAP that does not provide for transitional provisions or a voluntary change in accounting policy, the entity shall apply the change retrospectively. according to regulations, regional financial management must be carried out in an orderly, effective, efficient, economical and responsible manner by taking into account the principles of justice, propriety, and benefits for the community.

To obtain financial reports that meet the principles of transparency and accountability and are in accordance with SAP, the Regional Head must establish a general policy in the accounting field. Local government accounting policies are the specific principles, bases, conventions, rules, and practices chosen by a reporting entity in the preparation and presentation of financial statements. Local government accounting policies regulate the recognition principle, measurement principle, and disclosure principle in accounting for assets, liabilities, equity funds, income, expenditure, and financing as well as their presentation in financial statements.

Reference

- Alfian, F, Purba, V,(2020). The Contingency Approaches to the Design of Accounting Systems. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 949-956. <https://tojqi.net/index.php/journal/article/view/8207>
- Atamirzaevich, O. A. (2022, April). Factors Influencing The Formation Of Accounting Policies. In *E Conference Zone* (pp. 4-7).

- Bulycheva, T. V., Busheva, A. Y., Eliseeva, O. V., & Zavyalova, T. V. (2022). Innovative Approach to Accounting Policy Development in Accordance with International Financial Reporting Standards. In *Cooperation and Sustainable Development* (pp. 897-907). Springer, Cham.
- Dewi, C.; Rambe, P.; Muda, I. and Ginting, S. (2018). Application of Accrual Accounting to Government. In *Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES*, ISBN 978-989-758-432-9, pages 938-942. DOI: 10.5220/0009494309380942. <https://www.scitepress.org/PublicationsDetail.aspx?ID=Fq42rvrU0Ac=&t=1>
- El Sima, A.H, Siregar, C (2020). Inventory Accounting System Analysis and Design (Overview about Providing Good Service to Consumers). *Turkish Online Journal of Qualitative Inquiry*. 11(4). 1088-1097. <https://tojqi.net/index.php/journal/article/view/8227>.
- Hope, OK (2003). Accounting policy disclosures and analysts' forecasts. *Contemporary Accounting Research*, 20(2), 295-321.
- Junita, A; Erlina; Abubakar, E; Muda, I; Abdullah, S; (2019). Influence of budget participation and leadership style against rebudgeting on work unit of apparatus, *JBRMR* , 13(02). 272-282 <https://doi.org/10.24052/JBRMR/V13IS02/ART-25>.
- Lubis, W.S and Kamil, T (2020). Analysis Implementation of Service Concession Agreements - Service Providers Retrospective (ISAK 16). *Turkish Online Journal of Qualitative Inquiry*. 11(4). 1016-1024. <https://tojqi.net/index.php/journal/article/view/8217>
- Nasution, A.A., Erlina, & Atmanegara., A.W (2022). Learning Validation Control and Input Error Correction on Implementation of Computer Assisted Audit Techniques (CAATS) (Review New Trends in Sustainable Development of Learning Education Management Models for the Accounting Student). *Webology*. 19(1). 1850-1861. DOI: 10.14704/WEB/V19I1/WEB19124. <https://www.webology.org/abstract.php?id=887>
- Ningtyas, PE, & Widyawati, D. (2015). Effect of Effectiveness of Implementation of Government Accounting Standards on the Quality of Local Government Financial Reports. *Journal of Accounting Science and Research*, 4(1). 89-103.
- Prakasa M, B, Gulo, W.V.A Muda. (2022). Use of Journal in the Recording Process in Accounting System. *Journal of Positive School Psychology*. 6(3). 2368–2374. <https://journalppw.com/index.php/jpsp/article/view/1965>
- Rautiainen, A., Järvenpää, M., & Mättö, T. (2022). Non-IFRS and changes in accounting institutions—lessons from Nokia. *Accounting History*, 10323732221094033.
- Schmidhuber, L., Hilgers, D., & Hofmann, S. (2022). International Public Sector Accounting Standards (IPSASs): A systematic literature review and future research agenda. *Financial Accountability & Management*, 38(1), 119-142.
- Tarigan, A., Ramadhani, I. F., (2022). Principles and Assumptions in Financial Reporting Based on IFRS. *Journal of Positive School Psychology*, 6(3), 2333-2342.
- Tickell, G. (2010). Cash to accrual accounting: One nation's dilemma. *International Business & Economics Research Journal*, 9(11), 71-78.

CHAPTER 3

Approach and Criticism of Positive Accounting Theory (PAT)

Juliana Safitri¹, Nurzana², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹Correspondent Email : julianasafitri123@yahoo.co.id

ABSTRACT

This paper reviews the approaches and criticisms of positive accounting theory (PAT). This paper also discusses the development of positive accounting theory and criticism of research on positive accounting theory. The writings of Watts and Zimmerman (1978) on Positive Accounting Theory (PAT) have contributed a lot to the development of accounting research that is used to explain and predict phenomena that exist in nature. WZ's writings also caused a lot of criticism and debate from other researchers. Positive accounting theory tries to understand how accounting practices are used by accountants in different corporate situations and by different situations. To understand the concept of an economic approach, a positive accounting theory is needed.

Keywords : Positive Accounting Theory, Economic Approach, Criticism Of Positive Accounting Theory.

1. Introduction

The first time the development of accounting theory produced a normative theory, then on the basis of the objectives of accounting theory it can be divided into two types, namely normative accounting theory which provides a formulation of accounting practice and positive accounting theory which seeks to explain and predict phenomena related to accounting (Ghozali and Anis, 2007). Explained by Watts and Zimmerman (1986) about normative theory that seeks to explain which information must be communicated to all users of accounting information and accounting will be present to users. Normative theory will try to explain information about what accountants should do in the process of presenting financial information to all users, and not explain what is actually contained in financial information and why it happens. According to Watts and Zimmerman (1978) positive accounting theory should be developed to explain why accounting is as it is today, why accountants do what they do, and what effect the accounting phenomenon has on the utilization of existing resources. Without such a positive theory, no academic or professional would be able to provide answers to the normative questions they always raise.

Watts and Zimmerman (1986) reveal that there are three basic reasons for the shift in the positive normative approach, namely 1) the inability of the normative approach to test the theory, because it is based on wrong premises or assumptions so that its validity cannot be tested, 2) the normative approach is more focuses on the prosperity of individual investors rather than the prosperity of the wider community, 3) the normative approach does not encourage or allow for an optimal allocation of economic resources in the capital market. This is considering that in an economic system based on market mechanisms, accounting information can be a controlling tool for the community in allocating economic resources efficiently. Furthermore, Watts and Zimmerman stated that the rationale for analyzing accounting theory in a normative approach was too simple and did not provide a strong theoretical basis. For the weakness of normative theory, Watts and Zimmerman developed a positive approach that is applicable in a certain scientific period(1970-present).

This study discusses the approach and criticism of positive accounting theory (PAT) conducted by several researchers. One of them Whittington (1987) reviewed PAT Watts and Zimmerman in 1986 with the article title 'Positive Accounting: a Review Article. Whittington criticized parts of the chapters discussed in the book that he thought were inaccurate or lacked more detailed discussion. Furthermore, Hines (1988) discusses the criticisms raised by Cristenson (1983) and the methodology. Robert R. Sterling (1990) assessed Accounting Positively, by explaining the main pillars of PAT, namely the study of phenomena, and value free, while the basic assumptions of PAT were Economics and Science.

2. Literature review

2.1. Positive Accounting Theory

Positive Accounting Theory or what is often referred to as PAT explains the observed accounting phenomena based on the reasons that cause an event to occur. However, over time developing at the present time this positive theory tends to emphasize explaining the reasons for the role of accounting and related information in economic satisfactions, individuals, companies, and other parties who play a role in capital market and economic activities (Prayogi et al., 2020). According to Watts and Zimmerman (1978) positive accounting theory should be developed to explain why accountants do what they do and what effect these accounting phenomena have on existing resources. The ideas of Watts and Zimmerman became controversial and caused a lot of criticism from other researchers.

Boland and Gordon (1992). Boland and Gordon provide the basic assumption that Watts and Zimmerman define PAT from Economic-Based Accounting Theory. According to Boland, the

assumptions used by Watts and Zimmerman in 1978, 1979 and 1980 were a combination of the instrumentalism of Milton Pridmen, and the positivism of Paul Samuelson. The 1986 assumption comes from a combination of Poincare, Hemple and Popper, namely Conventionalism. Meanwhile, according to Graffikin (2005), criticized the assumption of PAT. He argued that Watts and Zimmerman did not prescribe, and that science was not value-free, assuming simplistic behavior. From the description of the criticism of PAT which has been described in outline above, the content of the criticism can be classified into critical issues regarding: research methods (including interested inferences), methodology (including philosophy of science); and other scopes.

2.2. Positive Approach In Accounting Theory

As explained in the introduction above, the emergence of positive theory in the accounting field is caused by a gap in the normative approach and the tendency to view accounting theory normatively (Watts and Zimmerman, 1986). To reduce the gap in the normative approach, Watts and Zimmerman develop a positive approach that is more oriented towards empirical research to justify various accounting techniques or methods currently used or look for new models for the development of accounting theory in the future.

Theories (containing a set of hypotheses) are compiled through logical thinking and scientific methodologies both deductively and inductively and tested through scientific and empirical research. If empirical research can prove the validity of a theory, it is said that the theory has been verified. The development of positive accounting theory is more intended for the benefit of making accounting information for investors in the capital market which is very closely related to empirical research to test the validity of theories regarding the capital market that have existed before (Hasibuan et al., 2020). This concept has the impact of a shift in the preparation of accounting theory from a positive normative approach. In his book *Positive Accounting Theory* (Watts and Zimmerman, 1986), he explains that there are three basic reasons for the shift in the positive normative approach, namely:

1. The inability of the normative approach to test the theory empirically. Even though a theory is logically consistent enough, it may not match the observations in the real world because the underlying premises or assumptions are wrong, or the observations are inadequate (sufficient), or the objective is wrong. So that the validity of these assumptions cannot be tested empirically.
2. The normative approach focuses more on the prosperity of individual investors than on the prosperity of the wider community.
3. The normative approach does not encourage or enable optimal allocation of economic resources in the capital market. In an economic system based on market mechanisms, accounting information can be a controlling tool for the public in allocating economic resources efficiently.

3. Methods

This study uses a qualitative approach. The qualitative is an analytical method based on post-positivism philosophy, used to examine the condition of natural objects, where the researcher is the key instrument (Bakar et al., 2021). The method used in this research is a case study on government accounting standards. Case study research is a research conducted intensively and in detail.

2.3. Result and Discussion

There have been many articles criticizing and evaluating positive accounting theories published since 1982. In this case the critics are usually grouped into three groups, namely (Lawrence AB, 1992):

1. Criticism of research techniques or methods. In this case it is stated that the writings on positive accounting that have been surveyed fail to describe the multiperson / human model as a whole and are weak in both strategies, namely: in consideration and theoretically. Approaches that may be useful in formal theory development.
2. Criticism of philosophy is based more on the emphasis that Watts and Zimmerman provide positive/normative boundaries. Watts and Zimmerman did not rely on other philosophical arguments of science in their first writings to support the methodology they developed (Ritonga et al., 2020). Watts and Zimmerman assume that the social world and its structure can be seen separately from the individual being studied, this is not objective because it is impossible for research to be separated from the object under study.
3. Criticism of economics-based accounting research.
 - a. An individual methodology, describing each social phenomenon as a consequence of individual decision making. In short, individuals make decisions but do not implement them. When the committee sets the standards, the director makes the decisions, the individual methodologies say it is a group decision with an explanation of the decisions made by the committee members.
 - b. The neochisic approach is to maximize the hypothesis because the assumption or maximization assumption is only one of the many assumptions needed in neochial, under this claim that each individual makes a decision, the subject is subject to a limit that exclusively maximizes everyone's profit.

The Positive Accounting Theory (PAT) initiated by Watts and Zimmerman (1978, 1979, 1986) has been widely criticized by scientists and researchers. The ideas of Watts and Zimmerman were controversial. On the one hand, PAT has contributed a lot to the development of accounting research, especially mainstream research, but on the other hand, there are also many shortcomings from the thoughts of Watts and Zimmerman, which have led to a lot of criticism and rebuttal from other researchers (Nasution et al., 2018). Positive theory develops because of dissatisfaction with normative theory, namely (1) the inability of normative to test empirically; (2) normative focus is more on the prosperity of individual investors than on broader prosperity; (3) the normative does not encourage or allow the optimal allocation of economic resources in the capital market.

3. Conclusion

Criticism of positive accounting theory can contribute to accounting science. Criticism arises because Watts and Zimmerman's framework is more motivated by the utility of pragmatism of accounting research knowledge, where the measure used is determined according to the contribution it makes, namely positive theory can provide direct benefits in the form of the ability to explain and predict accounting practices that behave with individual behavior in maximization of its utility. From the description of the criticism of PAT which has been described in outline above, the contents of the criticism can be classified into critical issues regarding: research methods (including interested inferences), methodology (including the philosophy of science); and other scopes.

Reference

Bakar, E. A., Nedelea, A., & Wardhani, M. M. (2021). The Influence of Using SAP CRM On Increasing Customer Satisfaction Index at Pt. Bank X In Medan, Indonesia. *The USV Annals of Economics and Public Administration*, 21(1).33-44. <http://annals.seap.usv.ro/index.php/annals/index>

- Boland Lawrence A, Irene M Gordon. (1992). *Criticizing Positive Accounting Theory*, Contemporary Accounting Research.
- Ghozali, Imam & Anis Chariri, (2007). *Accounting Theory*, Edition 3, Semarang: Diponegoro University Publishing Agency.
- Graffikin, (2005). *Positive Accounting: Where About?. Notes for an Introduction to Theoretical Foundations of Research*. Brawijaya University. March, 1, 2005.
- Hasibuan, D.R.F, Islamiati, H, (2020). The Behavioral Effects of Accounting Information. *Turkish Online Journal of Qualitative Inquiry*. 11(4). <https://tojqi.net/index.php/journal/article/view/8202> .
- Murtoto, A.B, (1999). *Accounting Theory: From a Normative Approach to a Positive*. 1. 163-183
- Nasution, S.; Putri, R.; Muda, I. and Ginting, S. (2018). Positive Accounting Theory: Theoretical Perspectives on Accounting Policy Choice. Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES, p.1128-1133. DOI: 10.5220/0009506011281133. <https://www.scitepress.org/PublicationsDetail.aspx?ID=t2D6UTYq+/M=&t=1>
- Prayogi, W, Liska, J , (2020). The Cognitive Relativism In Accounting Have An Impact On The Quality Of Decisions Made By Decision Makers *Turkish Online Journal of Qualitative Inquiry*. 11(4). 896-900. <https://tojqi.net/index.php/journal/article/view/8198>
- Ritonga, R.R, Agustina, D.M Simanjuntak (2020). Is Accounting a Science? Mainstream Accounting Research Sees a Parallel Between Physical and Social Sciences and Accounting. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 984-994. <https://tojqi.net/index.php/journal/article/view/8212>
- Watts RL, JL Zimmerman. (1986). *Positive Accounting Theory*, Prentice Hall International. Inc., Englewood Cliffs, NJ, USA.
- Watts, Ross L., Jerold L. Zimmerman, (1978). Toward a Positive Theory of the Determination of Accounting Standards. *The accounting Review*.
- Whittington, G. (1987). Positive Accounting: A Review Article. *Accounting and Business Research*, 17(68). 327-336.

CHAPTER 4

The Models Implement of Financial Accounting Based on the Anglo-American Model

Anastasia Miranda Rebecca Simatupang¹, Rizki Isnani Fadhila Saragih², Iskandar Muda³
^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹ Correspondent Author Email: anastasiasimatupang16@gmail.com

ABSTRACT

Anglo Saxon is a legal system that originated in England and then developed in the United States and its former colonies. The purpose of this paper is to describe and explain the application of the Anglo American model of accounting system which is more widely used by countries in the world than the continental system, because Anglo American is considered easier to implement and simpler when compared to other systems. Anglo Americans have an emphasis on a “true and fair view” of audited financial statements. "True and fair view" or a true and fair view is a true statement about the company's financial position as shown in his account and confirmed by the auditor. Like the Indonesian state which initially implemented the continental system as a bookkeeping system, then switched to the Anglo-American system because of foreign investment in Indonesia which had a positive impact on accounting developments. The method used in this paper uses a literature study. Literature study is research that uses library data collection techniques or existing literature to be studied and processed as research material in accordance with the theme.

Keywords : Anglo - American, True and Fair View, Continental

1. INTRODUCTION

The development of economic transactions encourages professional organizations to create standards for recording and financial reporting in each country, either with or without national government intervention (Nasution et al., 2021). International accounting is international transactions, comparison of accounting principles in various countries and harmonization of various world accounting standards. The preparation of financial statements by management is based on accounting standards that apply in a country (Siallagan, 2020).

There are two general financial reporting models that have evolved in economic countries proceed. Namely the Anglo American model and the continental model. Anglo American model has the virtues of a strong presence in the accounting profession, limited role of the government, the importance of the securities market for improving equity models, and an emphasis on a “true and fair view” of audited financial statements (Lubis et al., 2021 and Warae et al., 2021). The continental model generally presents the accounting profession as relatively weak, reflects the strong influence of government on accounting regulation, and organization, including the primacy of the effect of taxes and creditor protection on the presentation of financial statements not to the needs of investors, and emphasizes the importance of financing debt through large banks rather than increasing equity capital (Shulha O et al., 2022 and Zainal et al., 2022).

The term Anglo American is also known as Anglo Saxon, because of the Anglo Saxon accounting model growing in America. So this system originated in England and was then brought to America and various other countries. Anglo American model followed by many countries, namely England (United Kingdom), America (United States), Canada, Australia, Netherlands, and New Zealand. We can see the connection between colonialism and the development of Anglo - Saxon accounting. America, Canada, Australia, New Zealand, were British colonies and used the Anglo American model. Because they feel they fit into this system. In addition, Indonesia itself also applies the Anglo - American model system as the accounting system.

Indonesia initially used a continental system, as applied in the Netherlands. This system is also called bookkeeping which is actually different from accounting practice, where bookkeeping consists of constructive activities starting from the process of recording, summarizing, classifying and other activities aimed at creating accounting information based on data (Nasution et al., 2021 and Yulisfan et al., 2021). Meanwhile, accounting practices are constructive and analytical activities such as analysis and interpretation activities based on accounting information. So bookkeeping is part of accounting.

Subsequent developments, bookkeeping is no longer used. In company Indonesia is increasingly implementing the Anglo American accounting system. The development of the Anglo American accounting system in Indonesia was due to foreign investment in Indonesia which had a positive impact on the development of accounting, because most foreign investment used the United States (Anglo America) accounting system. Another reason is that most of those who play a role in accounting development activities completed their education in America, then applied accounting knowledge in Indonesia (Oktavia, 2009). So, along with the development of the business world in Indonesia, the use of accounting systems also developed from the continental system originating from Europe to the Anglo American system originating from America.

2. LITERATURE REVIEW

2.1 Anglo American

This grouping includes England (England, Wales, Scotland and Northern Ireland), many members of the British Commonwealth and the United States which certainly a British colony until 1776.

1) Great Britain

The roots of accounting have its origins in England (UK). The oldest professional accounting societies emerged in England in the middle of the 19th century in Scottish cities such as Edinburgh, Glasgow and Aberdeen. However, the core underlying British accounting has been found in various Company Acts from 1844 to Kali (1989). Prior to 1981, the Company Acts were mostly related to disclosure. In Acts since 1981, Company Acts previously been consolidated . In addition, several directives from the European Union have been passed. There is no UK equivalent to the Securities and Exchange Commission (SEC). The accounting profession in the UK consists of six major organizations. They:

- a) Institute of Chartered Accountants in England and Wales
 - b) Institute of Chartered Accountants of Scotland
 - c) Institute of Chartered Accountants in Ireland.
 - d) Association of Certified Accountants
 - e) Institute of Cost Accountants and Management
 - f) Chartered Institute of Public Finance and Accounting
- 2) United States of America

Accounting in the United States is regulated by a sector-specific agency the Financial Accounting Standards Board (FASB), but the governing agency for their standardization is the Securities and Exchange Commission (SEC). The accounting system in the United States is very similar to that in the UK, perhaps this is a result of the history and investment relationship between the two countries. In the United States, accounting is more focused on large companies and the interests of investors, the needs of creditors and other users. Information relevant to business requirements is a prime subject for return limits (Wardhani et al., 2021). The securities market has a dominant influence on accounting regulations in the United States. Investor safety and protection is regulated and required at the federal government level under the Securities Act of 1933 and the Securities Act of 1934. Both acts were the first national securities laws in the United States. The 1933 law regulates the issuance of securities on the interstate market; the 1934 law deals primarily with the trading of securities. The laws of 1933 and 1934 gave the SEC both broad and specific powers to determine the form and content of financial information filed with the SEC (Wolk et al., 2000).

The Securities and Exchange Commission (SEC) was founded on a legal basis to require securities laws and formulas as well as to require accounting standards. Thus, the SEC was introduced as an authority on Generally Accepted Accounting Principles (GAAP) which was standardized by the Financial Accounting Standards Board (FASB), which was founded in 1973. The SEC has full authority to explain accounting standards and reports to public companies, but relies on the private sector to implement these standards (Yulisfan and Nedelea 2021). As part of the regulatory process, the SEC issues accounting series releases, financial reporting releases, and staff accounting bulletins.

The type of annual financial report for a large US company has the following components:

- a) Management reports.
- b) Independent auditor's report.
- c) Primary financial statements (income statement, balance sheet, cash flow statement, comprehensive income statement, changes in shareholder equity).
- d) Management discussion, analysis of operational results and financial condition.
- e) A description of the accounting policies with the most critical impact on financial statements.
- f) Notes to financial statements.
- g) Comparison of financial data for five or ten years, and
- h) Selected quarterly data. (Yuesti and Saitri, 2021).

3) Canada

Canada, like some members of the British Commonwealth, initially looked to the UK for guidance in financial reporting, but over time it has become more influenced by the US approach. Because of the importance of Ontario in the Canadian federation, the Ontario Companies Acts are important when it comes to financial statement disclosure. American influence can be noted from the Ontario Securities Acts of 1966, which gave the Ontario Securities Commission oversight powers over the Toronto Stock Exchange and an equal position with the SEC relative to its standard-setting function.

4) Australia

Australia is an interesting study. While relying on the British Companies Acts, various Australian states also have their own Companies Acts. Their actions emphasize disclosure, not measurement of the rules, and do not always agree with one another. An equally complex duality exists in the standard-setting arena. There are two main accounting organizations in Australia: the Institute of Chartered Accountants in Australia and the Australian Society of Accountants.

5) ASEAN countries

ASEAN (Association of Southeast Asian Nations) is a group of developing countries in Southeast Asia. This association was formed in 1967 with charter members being Malaysia, Indonesia, Singapore, Thailand, and the Philippines. New members include Brunei, Vietnam, Laos, and Myanmar. In general, government agencies pay more attention to disclosure in charter member groups by setting audit standards and rules made by private sector organizations. Accounting standards have influenced many of the United States, United Kingdom, and the International Accounting Standards Board. As a result, we classify ASEAN countries with the Anglo American group

6) Other Countries

Two other countries, the Netherlands and New Zealand. The Netherlands is a continental country, the accounting situation is largely Anglo American in reference, with corporate law and the accounting profession playing an important role. New Zealand is an important follower of the Anglo American approach, though Unlike its larger neighbour, New Zealand's professional body of accountants is the New Zealand Society of Accountants (NZSA).

In Anglo American countries, the shareholder model of corporate governance applies. Shareholders are the main partners of the company. Shareholders elect a governing board and they monitor directors through an audit committee, nominations, and remuneration. Compared to Continental European countries, there is greater monitoring of managers by external board members and by financial analysts as well as by the financial press. Demand for accounting income in Anglo American countries presents a special feature compared to the accounting demands in the countries of the Continent of Europe. Financial reporting is based on a conceptual framework that has priority to satisfy the needs of shareholders for accounting information. The capital market has a vital role in providing financing. As a result, the financing pattern of Anglo American firms is dominated by equity and there is more separation between owners and managers. Firms are characterized by a dispersed ownership structure and are thus more likely than owner-controlled firms to manage earnings, and to do so more frequently (Bakar et al., 2021). Shareholders, financial analysts and the financial press are placing greater pressure on Canadian managers. Canadian managers use discretionary attitudes to avoid pressure from dynamic capital markets (Othman and Zeghal, 2006).

Anglo America also places emphasis on a “true and fair view” of audited financial statements. "True and fair view" or a true and fair view is a true statement about the company's financial position as shown in his account and confirmed by the auditor. The view that is right and just is a broad and general concept. When accounts are reported

according to a true and fair view, is it an attempt to provide unbiased information of the different components, which affect the intrinsic value of the company. When true and fair views are being defined, criteria need to be met for information to be true and fair need to be determined. The problem of justice in economic theory is a classic problem (AL-Kasasbeh et al., 2021). Account records must state that annual accounts provide a true and fair view. Balance sheets, income statements, income statements and records must be prepared in their entirety and provide a true and fair view of the company's position and results. If it is necessary to provide a true and fair view, additional information should be left out. If there are some discrepancies from the general advice and recommendations of standard-setting bodies, information about this and about the reasons for the discrepancy should be included in the notes (Samuelsson et al., 2003).

2.2 The Development of the Anglo American Accounting System in Indonesia

The development of accounting in Indonesia cannot be separated from the Dutch colonial period and students who graduated from the United States of America who worked for Indonesian companies. The development of accounting in Indonesia can be traced back to the Dutch colonial era in 1642. In 1747 it was related to accounting practices in Indonesia, namely the bookkeeping practices carried out by the Amphioen Society domiciled in Jakarta. In the Dutch era, they introduced a double-entry bookkeeping system as developed by Luca Pacioli.

In the 1950s, although the Dutch had left Indonesia, the Dutch model of accounting practice was still used during the post-independence era. In addition to the practice in various companies, accounting training education is also still dominated by the Dutch accounting system. At that time, his bookkeeping records emphasized the debit and credit mechanism, which was found in the books of the Amphioen Society, which was a Dutch monopoly business. The bookkeeping records are a modification of the Venetian-Italian system, and there is no conceptual framework for developing a record-keeping system because the conditions place great emphasis on trading practices solely for the benefit of Dutch companies.

In various movements towards national independence, the people urged the Indonesian government to nationalize Dutch-owned companies. In 1958 the process of nationalization of companies and the migration of the Dutch from Indonesia resulted in a shortage of accountants and bookkeeping experts. The nationalization and scarcity of accountants and experts in the country eventually turned to the American model of accounting practice. However, in this era the American model of accounting practice was able to blend in with the Dutch model of accounting, especially in government institutions. The increasing number of higher education institutions offering accounting education, such as the opening of the accounting department at the University of Indonesia in 1952, the Institute of Financial Science (STAN) in 1990, Padjadjaran University 1960, North Sumatra University 1960, Airlangga University 1960 and Gadjah Mada University 1964 has encouraged the replacement of the Dutch model of accounting practice with the American model in 1960. Furthermore, in 1970 all institutions had to adopt the American model of accounting system (Sanoto, 2013).

The preparation of Indonesian accounting standards basically refers to the American model with a few modifications. Since IAI was founded, three standards have been produced financial accounting as follows:

- 1) In 1973, for the first time, IAI published a book on Indonesian Accounting Principles (PAI), which was mostly a translation of Paul Grady's book. This publication was triggered by the activation of the capital market in Indonesia in 1973.
- 2) In 1984 the book Indonesian Accounting Principles 1984 which replaced the 1973 PAI was published. The PAI Committee made a fundamental revision of the 1973 PAI.

3) In 1994, IAI again made a total revision of the 1984 PAI and has since issued a series of financial standards named the Financial Accounting Standards (SAK) which has been issued since October 1, 1994. The development of this third accounting standard is intended to meet the needs of the business world and the accounting profession in order to follow and anticipate international developments. Many of the standards issued are in accordance with or equal to the international accounting standards issued by the IASC.

Currently there are 2 PSAK issued by 2 Financial Accounting Standards Boards.

- 1) Conventional PSAK
- 2) Sharia PSAK

This SAK will certainly continue to be added and revised according to the needs of business developments and the accounting profession. Furthermore, there are Three Pillars of Indonesian Accounting Standards, namely:

- 1) Financial Accounting Standards

Financial Accounting Standards are SAKs that have been in force now. With SAKs that have been converged to IFRS, it is hoped that it will provide the same understanding perspective for foreign investors in reading the financial statements of Indonesian companies or Indonesian investors who want to expand overseas.

- 2) Accounting Standards for Entities without Public Accountability (ETAP)

On July 17, 2009, IAI issued SAK for Entities without Public Accountability (SAK ETAP) or The Indonesian Accounting Standards for Non-Publicly-Accountable Entities , and was approved by DSAK IAI on May 19, 2009.

- 3) Sharia Accounting Standards

IAI as the institution authorized to stipulate SAK and audit for various industries is an important element in the development of Islamic banking in Indonesia, where the Islamic economy cannot run and develop properly without good SAK.

According to the Financial Services Authority (OJK) in Indonesia, the components of a complete financial report consist of:

- 1) Statement of Financial Position
- 2) Income statement
- 3) Statement of Changes in Equity
- 4) Cash flow statement
- 5) Notes to Financial Statements

2.3 International Accounting Harmonization

As international trade increased, efforts began to measure differences in accounting standards and practices in different countries and different regional groups. The FASB and IASB have started efforts to harmonize these accounting standards. Harmonization is a process to improve the compatibility (suitability) of accounting practices by setting limits on how much these practices can vary.

Harmonization was developed by the International Accounting Standards Committee (IASC), a private independent body that issues several International Accounting Standards relating to topics that affect financial statements (Khomsiyah, 2001).

Accounting harmonization includes harmonization of:

- 1) Accounting standards (related to measurement and disclosure)
- 2) Disclosures made by public companies related to the offering of securities and listing on the stock exchange
- 3) International Harmonized Survey auditing standards

Advantages of International Harmonization:

- 1) Capital markets are becoming global and investment capital can move around the world without a hitch. High quality financial reporting standards used consistently around the world will improve the efficiency of capital allocation.

- 2) Investors can make better investment decisions, portfolios will be more diversified and financial risk is reduced
- 3) Companies can improve strategic decision-making processes in the area of mergers and acquisitions
- 4) The best ideas arising from PAT standard-setting activities are disseminated in developing the highest quality global standards

3. METHODS

The method used in this paper uses a literature study. Literature study is research that uses library data collection techniques or existing literature to be studied and processed as research material in accordance with the theme. Literature study is a collection of activities related to collecting library data, reading, taking notes, and then processing the data as research material.

4. RESULT AND DISCUSSION

4.1 Result

Along with the development of accounting science, many countries prefer to use the Anglo- American system. This is because:

- 1) Anglo American is considered easier to implement and simpler when compared to other systems.
- 2) The Anglo Saxon system keeps the books contained in one accounting department. Likewise in Indonesia, companies or people are increasingly applying the Anglo Saxon accounting system rather than using the continental system.
- 3) Anglo Saxon -influenced legislation respects the interests of shareholder protection with a focus on information relevant to decision making (Meuthen, 2017).

4.2 Discussion

Anglo Saxon is a legal system originating from England which later spread to the United States and its former colonies, and is known as Common Law or Unwritten Law (unwritten law). The Anglo Saxon system is a legal system based on jurisprudence, namely the decisions of previous judges which then become the basis for the decisions of subsequent judges. This legal system is applied in Ireland, England, Australia, New Zealand, South Africa, Canada (except the Province of Quebec) and the United States (although the state of Louisiana uses this legal system in conjunction with Napoleon's Continental European legal system). In addition to these countries, several other countries also apply a mixed Anglo Saxon legal system , for example Pakistan, India and Nigeria which apply most of the Anglo Saxon legal system , but also apply customary law and religious law. The Anglo Saxon legal system is actually easier to implement, especially for people in developing countries because it is in accordance with the times. The opinions of experts and legal practitioners are more prominently used by judges in deciding cases.

The differences between the Dutch system (continental system) and the United States system (Anglo American system) are as follows:

Table 1. The differences between the Dutch system (continental system) and the United States system (Anglo American system)

Object	Continental System	Anglo American System
1. Daily Journal	Debit / credit grouping has not been detailed	Debit/credit grouping is detailed
2. Ledger Account		
a. Shrinkage	Using a reserve account and recorded credit	Using a depreciation expense account and recorded on the debit side

b. Mixed Account	Using mixed accounts	Not using an account
c. Private	There is a private deposit	There is no private deposit
3. Work sheet	Archive saved as document	The archive is not saved because it is only as a tool
4. Financial statements	Consists of: <ul style="list-style-type: none"> • Balance • Profit and loss statement • Statement of changes in capital 	Consists of: <ul style="list-style-type: none"> • Balance • Profit and loss statement • Statement of changes in capital • Cash flow statement • Notes to financial statements

The Table 1 above shows the differences between the continental accounting system and the Anglo American model . **Namely , the recording of the continental accounting system has not specified using debit/credit), this is because the continental system is usually used by small companies, while in the Anglo American accounting system the grouping of debit credit accounts is more detailed, because the Anglo Saxon accounting system is used to large companies, where both external and internal parties require the company's accounting information to be used in making company decisions.**

5. CONCLUSION

Anglo Saxon is a legal system originating from England which later spread to the United States and its former colonies, and is known as Common Law or Unwritten Law (unwritten law). Anglo America also places emphasis on a “true and fair view” of audited financial statements. "True and fair view" or a true and fair view is a true statement about the company's financial position as shown in its accounts and confirmed by the auditor. The Anglo Saxon system is more widely used by countries in the world because it is considered easier to implement and simpler than other systems, as well as more detailed in the recording of the accounting system. Anglo American accounting can characterize accounting in Europe, Asia, Latin America and in many other parts of the world. The practice is not only in the United States and United Kingdom but also extends to several regions and countries. For example, Britain had great colonial influence, such as in Australia, Canada, Hong Kong, India, Ireland, Kenya, Malaysia, New Zealand, Nigeria, Singapore, and South Africa. Anglo American accounting is becoming more relative and less conservative and more transparent than in Latin countries, Germany, and Japan.

REFERENCE

- AL-Kasasbeh, O.M, Muda, I, Abderrazak, Z (2021). COVID-19 Pandemic: Macroeconomic Impacts and Understanding its Implications for Jordan. *International Journal of Applied Engineering Research*. 6(2). 51-58. ISSN: 2666-2795. https://romanpub.com/resources/ijaer%20v6-2-2021-%20COVID.edited-raj_pagenumber.pdf
- Bakar, E. A., Nedelea, A., & Wardhani, M. M. (2021). The Influence of Using SAP CRM On Increasing Customer Satisfaction Index at Pt. Bank X In Medan, Indonesia. *The USV Annals of Economics and Public Administration*, 21(1).33-44. <http://annals.seap.usv.ro/index.php/annals/index>
- Khomiyah. (2001). The Influence of Culture on Differences in Accounting Systems/Practices and the Harmonization Process of International Accounting Standards. *Journal of Business and Accounting*. 3(1). 353-366.

- Lubis, P. D. K., Lubis & Nedelea, A. M. (2021). Management Process Administration In Enterprise Resources Planning (ERP) Systems Applications and Products In Data Processing (Sap) In Ptpn Iii Sei Dadap. *Ecoforum Journal*, 10(1). <http://www.ecoforumjournal.ro/index.php/eco/article/view/1203/761>
- Meuthen, M., H. (2017). *Quo vadis european true and fair view? The integration of continental european and anglo-saxon stakeholder protection interests*. *Corporate Ownership & Control*, 14(4-1), 276-283. doi:10.22495/cocv14i4c1art9
- Nasution, A. P., Iskandar, R., & Abubakar, E. (2021). Identification of Success Strategies for E-Government Services in Medan City. In *BICED 2020: Proceedings of the 2nd EAI Bukittinggi International Conference on Education, BICED 2020, 14 September, 2020, Bukittinggi, West Sumatera, Indonesia* (p. 230). European Alliance for Innovation. <http://dx.doi.org/10.4108/eai.14-9-2020.2305668>
- Nasution, D. A. D., Sumekar, A., & Abubakar, E. (2021, March). Analysis of The Economic Behavior of Society E-Commerce as An Impact on The Development of The 4.0 Industrial Revolution and Society 5.0. *BICED 2020: Proceedings of the 2nd EAI Bukittinggi International Conference on Education, BICED 2020, 14 September, 2020, Bukittinggi, West Sumatera, Indonesia* (p. 217). European Alliance for Innovation. <http://dx.doi.org/10.4108/eai.14-9-2020.2305669>
- Octavia. (2009). Development of Accounting in Indonesia. *Accounting Journal*. Krida Wacana Christian University.
- Othman, H., B., Zeghal, D. (2006). A study of earnings-management motives in the Anglo-American and Euro-Continental accounting models: The Canadian and French cases. *The International Journal of Accounting*. 41 (2006) 406-435.
- Samuellson, M., Svensson, J. (2003). *True and fair view (a study of the implications of this concept within IAS and Swedish GAAP)*. Masters thesis in Business Economics Accounting and Business Economics
- Sanoto, J., F. (2013). Foreign Policy on Accounting in Indonesia. *Accounting journal*. 1(1). 14-27.
- Scott, R., W. (2015). *Financial Accounting Theory*. Seventh Edition. Pearson Prentice Hall: Toronto.
- Shulha O, Yanenkova I, Kuzub M, Muda I, Nazarenko V. (2022). Banking Information Resource Cybersecurity System Modeling. *Journal of Open Innovation: Technology, Market, and Complexity*. 8(2):80. <https://doi.org/10.3390/joitmc8020080>
- Siallagan, H. (2020). *Accounting Theory*. Medan: LPPM UHN Press
- Warae, Y., Sigalingging, E. D., Abubakar, E., & Nedelea, A. M. (2021). Revealing Auditor and Auditee Satisfaction In The Evolution Of Accounting Software (Phenomenology Study In The Regional Government Of South Nias District). *Ecoforum Journal*, 10(2). <Http://www.Ecoforumjournal.Ro/Index.Php/Eco/Article/View/1210/744>
- Wardhani, M. M., Padang, N.N & Nedelea, A. M. (2022). Indicators of Giving Interest Rates to Customers and Debtors at PT. Bank X in Medan, Indonesia. *Ecoforum Journal*, 11(1). 1-6. <http://www.ecoforumjournal.ro/index.php/eco/article/view/1284/789>
- Wolk, H., I., Dodd, J., L., Tearney M., G. (2000). *Accounting Theory; A Conceptual and Institutional Approach*, 5th ed. South-Western: College Publishing.
- Yuesti, A., Saitri, P., W. (2021). *International Accounting*. Bali: CV. Noah Aletheia.
- Yulisfan, Y., & Nedelea, A. M. (2021). The Evolution of Payroll Software That Can Replace The Manual Method In Indonesia. *Ecoforum Journal*, 10(2).1-6.
- Yulisfan, Y., Muda, I., & Nedelea, A. M. (2021). Implementation of Digitalization On The Revenue Cycle To Improve The Quality Of Decision Making More Timely In Indonesia. *Ecoforum Journal*, 10(3). <http://www.ecoforumjournal.ro/index.php/eco/article/view/1217/762>
- Zainal, M A.G, Borda, R.F.C, Algani, Y.M.A, Yakkala, B, Sanjith, S, Muda, I, Kalaichelvi, T, Mahendran, M, B. Bala, K (2022). A decentralized autonomous personal data management

system in banking sector. Computers and Electrical Engineering, Volume 100, 108027, ISSN 0045-7906, <https://doi.org/10.1016/j.compeleceng.2022.108027>.

Accounting Inquiries with New Approaches in the Post-Pandemic Era
Volume I

CHAPTER 5

The Effect of Budget Participation On Budget Slack With Budget Employment And Environmental Uncertainty As Moderating Variables

Kaslim Sugiono¹, Jessica Angelia², Iskandar Muda³

^{1,2,3}Universitas Sumatera Utara, Medan, Indonesia

¹ Email: kaslim@gmail.com

ABSTRACT

This research aims to know about the Effect of Budget Participation On Budget Slack With Budget Employment And Environmental Uncertainty As Moderating Variables. Partial budget participation has a significant negative effect on budget slack for star hotels in Bogor City, or in other words, higher budget participation will tend to reduce the creation of budget slack for star hotels in Bogor City. The research design is a quantitative method with a causal relationship approach. Causality or causality is a causal relationship. Where there are independent variables (influenced variables) and dependent variables. The result of this research are the interaction between the budget participation variable and budget emphasis partially has no significant effect on the budget slack of star hotels in Bogor City, or in other words the budget emphasis variable is not able to act as a moderating variable (strengthens or weakens) the relationship between budget participation and budget slack

Keywords : Effect of Budget Participation, Budget Slack, Budget Employment, Environmental Uncertainty

1. Introduction

The more rapid the rate of tourist arrivals makes a fairly rapid growth in the hospitality business. Conditions like this make the development of visits to hotels experience a positive growth rate. Therefore, the hospitality business is experiencing relatively tight and competitive competition. The growth rate of tourists visiting Bogor City hotels is reflected in the growth data in 2008-2014 in Table 1 below:

Table 1. The growth rate of tourists visiting Bogor City hotels

years	Visits to attractions					
	Traveler/Tourist		Total	Traveler/Tourist		Total
	Domestic	Mancanegara		Domestic	Mancanegara	
2008	1 370 119	18 174	1 388 293	716 807	31 443	748 250
2009	1 163 110	42 377	1 205 487	1 086 374	102 737	1 189 111
2010	1 524 044	42 812	1 566 856	1 205 628	104 076	1 309 704
2011	1 630 687	43 837	1 674 524	1 190 793	102 055	1 292 848
2012	1 802 539	45 618	1 848 157	1 309 875	106 137	1 416 012
2013	996880	58 491	1 055 371	2 428 331	108 515	2 536 846
2014	1 137 575	71 032	1 208 607	2 632 212	112 775	2 744 987
2015	2 429 470	36 496	2 465 966	1 168 263	165 612	1 333 875

Source: Bogor City Culture and Tourism Office (2016)

Its growing and competitive in the hospitality business, basically achieved because of management skills when supervising, controlling and predicting several possibilities and opportunities that are good for the long term. One of the factors that determine the success or decline of a company in its business activities is how the company's management, especially in the financial sector, controls the available funds or those that are expected to be received as well as cash flow records or at the bank effectively and efficiently. The role of management in the operation of the company is able to perform management functions on its decisions, namely planning, organizing, directing, coordinating and controlling, and the most important management activity is the effort to create a detailed and detailed control system, namely the planning and control function (Munandar, 2010:16) . Therefore, the budget is used by management as a reference for achieving the previously outlined success.

The behavioral aspect of budgeting exerts on the emergence of individual/organizational behavior. The behaviors seen in budgetary participation can be positive and negative. Improved performance because the motivation on the budget is used as the basis for performance appraisal is defined as positive behavior. The negative behavior that may arise is the tendency to provide information on participation and make slack on the budget which tends to apply slack in the budget. This behavior is usually relatively done by managers who tend to make budget slack. If the organization uses the budget as a target for performance evaluation, managers have an additional incentive to lie. Managers have an incentive to create budget slack, namely by over-presenting the budgeted costs or under-presenting the budgeted income in order to create budget targets that are easier to achieve (Horngren, et al., 2014: 283).

Slack is the difference between the actual resources needed to efficiently complete the task and a larger amount of resources allocated for the task, in other words slack is an inflated budget (Ishak and Ikhsan, 2005:176). If the organization uses the budget as a target for performance evaluation, managers have an additional incentive to lie. Managers have incentives to make budget slack, namely to overstate budgeted costs or understate budgeted revenues in order to create budget targets that are easier to achieve (Horngren et al, 2014: 283). Budget slack also helps buffer managers

against high-level management budget cuts and provides protection against increased costs or decreased revenues as a result of unforeseen impacts.

2. Literature Review

Budget or budget, has an important role as a management tool to control the company's operations, which are set, can be used to achieve company goals, often referred to as a tool to control the company's cash flow. Budget is a very important management tool for communicating management plans within an organization, allocating resources and coordinating activities.

The budget is an important element and focal point in the planning and control process. As a planning tool, the budget is used to plan various activities of a responsibility center so that the implementation of its activities is in accordance with what was planned. In addition, in its function as a planning tool, the budget consists of a number of targets to be achieved by the departmental/business unit managers of a company in carrying out certain activities in the future. The budget can function as a control tool if in its preparation it involves superiors and subordinates. Budgets are not only able to strengthen cooperation between employees, clarify policies, and realize plans but can also create optimal harmony within the company and goal harmony between superiors and subordinates. The budget can be used as a reference for controlling the company's activities.

Budget or budget, has an important role as a management tool to control the company's operations, which are set, can be used to achieve company goals, often referred to as a tool to control the company's cash flow. Budget is a very important management tool for communicating management plans within an organization, allocating resources and coordinating activities.

The budget is an important element and focal point in the planning and control process. As a planning tool, the budget is used to plan various activities of a responsibility center so that the implementation of its activities is in accordance with what was planned. In addition, in its function as a planning tool, the budget consists of a number of targets to be achieved by the departmental/business unit managers of a company in carrying out certain activities in the future. The budget can function as a control tool if in its preparation it involves superiors and subordinates. Budgets are not only able to strengthen cooperation between employees, clarify policies, and realize plans but can also create optimal harmony within the company and goal harmony between superiors and subordinates. The budget can be used as a reference for controlling the company's activities.

Budget participation has a direct impact on the behavior of superiors and subordinates in budgeting (Junita et al., 2019). Therefore, there are human behaviors that will arise as a result of the budget, both positive and negative behavior. Positive behavior will arise if the personal goals of each manager are aligned, harmonious and balanced with the company's goals (goal congruence) and managers have the will to fulfill them. Participation in the budgeting process also gives business unit managers the authority to determine the content of their budgets.

This authority provides an opportunity to abuse the authority they get by facilitating the achievement of the budget so that it can harm the organization or company. Managers tend to budget lower revenues and budget higher costs. This abuse can be done by making budget slack or budgetary slack. By doing slack, the company's performance will look good because the budgeted amount is easy to achieve.

Budget Emphasis (Budget Emphasis) is a variable that causes budget slack. Budget emphasis is a condition when the budget is used as the most dominant factor in measuring the performance of subordinates in an organization. Performance measurement based on the budget that has been prepared makes subordinates will try to get profitable variants by creating slack, among others, by

lowering income and increasing costs during budget preparation. If the subordinate believes that the reward given depends on the achievement of the target in the budget, the subordinate will try to build slack in his budget. As explained by (Suartana, 2010), regarding budget emphasis factors that can lead to budget slack, namely: "Often companies use the budget as the only measure of management performance, because it is available. Budget pressures like this can allow slack to arise. Performance appraisal based on whether or not the budget target is achieved will encourage subordinates to create slack with the aim of increasing the prospect of compensation in the future.

Budget slack in the budgeting process can also be caused by information asymmetry between business unit managers and directors. Information asymmetry is the difference in information held by top-level managers with lower-level managers due to differences in sources and access to that information. Business units in budgeting can provide opportunities to include local information. Thus, subordinates can communicate/disclose some of their personal information that may be included in the budget. In addition, subordinates can also hide some personal information so that it can affect slack.

According to (Anthony and Govindarajan, 2005), "Budget is an important tool for effective short-term planning and control in organizations". As a management plan, the budget has several characteristics. These characteristics are: (1) Expressed in units of money, even though the figures come from figures that are not financial units (eg the number of products sold). (2) Covers a certain period of time. (3) It contains management commitments, (4) The budget proposal is examined and approved by people who have higher authority than the compilers, (5) If the budget has been approved, then the budget cannot be changed except in special circumstances, (6) Budget realization compared with the budget periodically, and deviations that occur are analyzed and explained.

The budget is a short-term work plan that is prepared based on the long-term activity plan set out in the process of preparing the work program. If the budget is not prepared based on a previously prepared long-term activity plan, the budget actually does not lead the company anywhere. Budgeting is often referred to as profit planning. In profit planning, management prepares operational plans whose financial implications are stated in short-term and long-term income statements, balance sheets, cash flows and projected working capital in the future.

Budgeting has four main objectives, namely: (1) to adjust the strategic plan; (2) to help coordinate the activities of various parts of the organization; (3) to assign responsibilities to managers, to authorize the amounts they are authorized to use, and to inform them of the performance expected of them, and; (4) to obtain a commitment that is the basis for evaluating the actual performance of managers. And according to (Ikhsan and Ishak, 2005), there are several benefits of the budget:

1. The budget is the final result of the company's planning process. As a result of negotiations between members of the dominant organization, the budget reflects the organizational consensus regarding the operating objectives for the future.
2. The budget is the company's guide to action, which reflects management's priorities in the allocation of organizational resources.
3. The budget acts as an internal communication tool that connects the various departments or divisions of the organization with one another and with top management.
4. By setting goals in measurable performance criteria, the budget serves as a standard against which actual operating results can be compared.
5. The budget serves as a control tool that allows management to find areas that are the company's strengths or weaknesses.

6. Budget attempts to influence and motivate both managers and employees to continue to act in a manner that is consistent with effective and efficient operations and is aligned with organizational goals.

Budgets have become an accepted management tool for planning and controlling organizational activities. Budgets are implemented with varying degrees of complexity and success by many business and nonprofit organizations.

According to (Hasibuan et al, 2020) the benefits of budgeting are as follows:

- a. All activities can lead to the achievement of common goals.
- b. Can be used as a tool to assess employee strengths and weaknesses.
- c. Can motivate employees
- d. Assign certain responsibilities to employees
- e. Avoid waste and unnecessary payments
- f. Resources (such as manpower, equipment) and can be utilized as efficiently as possible .
- g. Educational tool for Managers

Budget benefits according to (Purba et al, 2022) are as follows:

- a. Forcing Managers to Plan
- b. Provide information that can be used to improve decision making
- c. Provide performance evaluation standards
- d. Improve communication and coordination

Budgets are an important tool for effective short-term planning and control in organizations. According to (Anthony and Govindarajan, 2005), the budget has the following characteristics:

1. The budget estimates the profit potential of the business unit
2. Expressed in monetary terms, although monetary amounts may be supported by non-monetary amounts (Example: Units sold or produced)
3. Usually covers a period of one year. In businesses that are heavily influenced by seasonal factors, there may be two budgets per year—for example, a fashion company usually has a fall budget and a spring budget.
4. It is a management commitment which means that the manager agrees to accept responsibility for the achievement of budget goals.
5. The budget proposal is approved and reviewed by an official with higher authority than the budget maker
6. Once approved, the budget can only be changed under certain conditions
7. Periodically, actual financial performance is compared with budget and variances are analyzed and explained.

There are several types of budget disclosed (Anthony and Govindarajan, 2005) including:

- a. Operating Budget
Is a budget that contains income and expenses revenues and expenses in one period.
- b. Capital Budget
Capital represents capital projects that have been approved, plus lump sums for small projects that do not require higher level approval.
- c. Balance Sheet
The balance sheet budget shows the balance sheet implications of the decisions included in the operating budget as well as the capital budget.
- d. Cash Flow Statement Budget

The cash flow statement budget shows how much cash required during the year will be supplied by retained earnings and how much, if any, must be obtained from borrowing or from other outside sources.

There are several approaches to budgeting. As stated by (Mardiasmo, 2011) that the approach in budgeting is as follows:

1. **Traditional Budget**

Traditional budgets have two main characteristics, namely the method of budget preparation based on an incrementalism approach and a line item budget structure.

a. **Line Item Budgeting**

The preparation of the budget using a line-item structure is based on the reason that the orientation of the budget system is intended to control expenditures, not based on the objectives to be achieved with the expenditures made.

b. **Incremental Budgeting**

Traditional budgets are incremental in nature, that is, they only increase or decrease the amount of rupiah on pre-existing items using the previous year's data as a basis for adjusting the amount of addition or subtraction without in-depth study.

Broadly speaking, the preparation of the budget is divided into 3 groups:

1. **Top Down Approach (from top to bottom)**

In preparing this budget, senior management sets the budget for lower levels so that the budget implementer only does what has been prepared. But this approach rarely works because it leads to a lack of commitment on the part of the budget maker and this jeopardizes the success of the budget plan

2. **Bottom up Approach (from bottom to top)**

In the bottom-up approach, the budget is fully prepared by subordinates and then submitted to superiors for approval. In this approach, lower level managers participate in determining the size of the budget. A bottom-up approach can create a commitment to achieving budget goals, but if not carefully controlled can result in an amount that is too easy or that doesn't match the company's overall goals.

3. **Combination of top down and bottom up**

The combination of these two approaches is the most effective. This approach emphasizes the need for interaction between superiors and subordinates to jointly determine the best budget for the company.

This budgetary participation has a positive impact on managerial motivation for two reasons:

a. Leads to greater personal commitment to achieving budget goals.

b. The result of participatory budgeting is a more effective exchange of information. Budget makers have a clearer understanding of their work through interaction with superiors during the review and approval phase.

c.

3. Methods

The research design is a quantitative method with a causal relationship approach. Causality or causality is a causal relationship. Where there are independent variables (influenced variables) and dependent variables. The data used is primary data obtained directly by the survey method and distributing questionnaires to respondents and processed and tested through SPSS 20.0 for windows.

3.1 Research Variable

1. Independent Variable (Variable X)

The independent variable is the variable that causes changes in the dependent variable (Juliansyah, 2011:48-49). The dependent/independent variable is budget participation (X1). The measurement is carried out with 6 indicator items developed by Milani, 1975 in Triana, et al, 2012 , with a Likert scale of 1-5.

2. Moderating Variable

Budget Emphasis (X2). Measurements were made with 8 question indicator items developed by Hopwood, 1972 in Triana, et al, 2012. Using a Likert scale of 1-5.

Environmental uncertainty (X3). Measurements were made with 12 question indicator items developed by Duncan, 2002. Using a Likert scale of 1-5.

3. Devended Variable (Variable Y)

Dependent variable is the part that you want to explain or predict and is influenced by several other factors (Robbin in Juliansyah, 2011:49). The dividend variable is budget slack (Y). Measurements were carried out with 6 question indicator items developed by Dunk, 1993 in Triana, et al, 2012. By using a Likert scale of 1-5.

3.2 Population, Sample and Sampling Technique

The management work unit of a company that occupies the position of middle manager (department head) and below with certain criteria at five-star hotels in Bogor City is the population in this study. The sample is a number of elements from the population, so that the research sample and an understanding of its properties or characteristics will make us generalize the characteristics of the population. The sampling technique used is to use purposive sampling in the hope of getting a representative sample according to the specified sample criteria. The sample criteria are:

1. Hotels that have an organizational structure.
2. Criteria for position as Manager (department head) who plays a role in coordinating hotel budgets.
3. Served as manager for at least one year.

There are 38 star hotels located in Bogor City based on data obtained from the Bogor City Culture and Tourism Office. For each hotel, 3 questionnaires or questionnaires were distributed, with a total of 114 respondents.

3.3 Data Analysis Method

Before conducting the analysis, the data was tested and processed in order to understand the respondents' beliefs in answering the questions, namely by testing the validity, reliability and classical assumption tests. In this study, the assumptions used were tests for normality, multicollinearity and heteroscedasticity.

Data analysis used multiple linear regression. The multiple linear regression equations in this study are as follows:

$$Y = \alpha + b_1X_1 + b_2X_2 + b_3X_3 + e$$

Y = Slack budget

α = constant

X₁ = Budget participation

X₂ = budget emphasis

X_3 = environmental uncertainty

b_1 - b_3 = multiple coefficient

$X_1.X_2$ = Interaction between budget participation and budget emphasis

$X_1.X_3$ = Interaction between budget participation and environmental uncertainty

e = error

From the regression analysis, the model feasibility test (F test) and hypothesis test (T test) were carried out.

4. Result and Discussion

4.1 Result

According to research I.C. Kusuma and H. Hidayat from the Accounting Study Program, Faculty of Economics, Djuanda University, Bogor, entitled "INFLUENCE OF BUDGET PARTICIPATION ON BUDGET SLACK WITH EMPLOYMENT OF BUDGET AND ENVIRONMENTAL UNCERTAINTY AS MODERATING VARIABLES (SURVEY ON STAR HOTELS USING 38 STAR HOTELS) IN THE STAR CITY Bogor city. The number of samples is 114 respondents, only 20 star hotels are willing to participate in filling out the questionnaire or questionnaire, totaling 60 respondents. The number of questionnaires that were collected and processed were 48 samples.

Table 2 Results of Questionnaire Data Acquisition

Information	Amount	Percentage
Questionnaire distributed	60	100%
Questionnaire back	48	80%
Questionnaire not returned	12	20%
Questionnaire can be processed	48	80%

Source: Processed Data (2017)

The summary of instrument test results is as follows:

1. Validity test shows that the data is normally distributed, as follows:
 - The histogram graph distribution forms a bell-like pattern;
 - The normal p-p plot regression graph shows the distribution of data following the direction of the diagonal line or at spreading points and following the direction of the diagonal line;
 - Classical assumption test with one sample kolmogrov smirnov statistical method produces Asymp value. Sig. (2-tailed) or two-tailed test of 0.935 greater than 0.05 (0.935 > 0.05).
2. Multicolonearity test shows that the regression model of this study does not occur multicolonearity, where the test results using the tolerance value and VIF (variant inflation factor) show that all independent variables have their respective VIF values, namely budget participation of 1.899, budget emphasis of 1.845, and environmental uncertainty of 1.050.
3. Heteroscedasticity test explains that the data is free of heteroscedasticity, where the test results using scatter plots show that the points do not form a certain pattern, and the points spread around the zero line on the Y axis.

4.2 Discussion

1. Multiple Regression Analysis with moderation model, processed using SPSS 20.0 with the following equation:

$$Y = 23,386 - 0,873X1 + 0,007X1.X2 + 0,013X1.X3$$

Where :

- Y = Budget Slack
X1 = Budget Participation
X2 = Budget Emphasis
X3 = Environmental Uncertainty
X1.X2 = Interaction Between Budget Participation and Budget Emphasis
X1.X3 = Interaction Between Budget Participation and Environmental Uncertainty

The interpretation of the above equation, can be explained,

- The constant value of 23.386 means that it shows the effect of budget participation, the moderating relationship between budget participation and budget emphasis and the moderating relationship between budget participation and environmental uncertainty. If the value is equal to 0, then budget slack is predicted to be 23,386.
 - Budget participation regression coefficient (X1) = - 0.873 means that if the other independent variables have a fixed value and budget participation (X1) has increased by one unit, then budget slack (Y) will decrease by 0.873 units. A negative coefficient means that there is a negative relationship between budget participation and budget slack, where the higher the budget participation, the lower the tendency for budget slack to arise.
 - The regression coefficient on the moderating relationship of the budgetary participation variable with budget emphasis is 0.007, meaning that if the other variables have a fixed value and the bond between budget participation and budget emphasis has increased by one unit, then budgetary slack (Y) has increased by 0.007 units.
 - The regression coefficient on the moderating relationship between budgetary participation variables and environmental uncertainty is 0.013, meaning that if the other variables remain constant and the association between budget participation and environmental uncertainty increases by one unit, then budgetary slack (Y) has increased by 0.013 units.
2. The correlation coefficient shows an R value of 0.474 which means that it shows a "moderate" level of relationship between the independent variables of budget participation, the moderating relationship between budget participation and budget emphasis, and the moderating relationship between budget participation and environmental uncertainty and the dependent variable on budget slack.
 3. Coefficient of Determination with a value of R Square or (R²) of 0.224 or (22.4%), which is the moderating relationship between budget participation and budget emphasis, and the moderating relationship between budget participation and environmental uncertainty simultaneously on budgetary slack as the dependent variable. with a percentage of 22.4%. While the remaining 77.6% (100% - 22.4%) was influenced by other factors that were not included in the study.
 4. Hypothesis Testing shows as follows:
 - a. Accepted H1 = Budget Participation Affects Budget Slack: The higher the budget participation, the lower the probability of budget slack.
 - b. Rejected H2 = Budget Emphasis Moderates The Relationship Between Budget Participation To Budget Slack: partial budget emphasis has no effect and is significant and

is not a moderating variable on the relationship between budget participation and budget slack.

- c. Accepted H3 = Environmental Uncertainty Moderates The Relationship Between Budget Participation and Budget Slack: the environmental uncertainty variable is a moderating variable or Quasi Moderation.

5. Conclusion

1. Partial budget participation has a significant negative effect on budget slack for star hotels in Bogor City, or in other words, higher budget participation will tend to reduce the creation of budget slack for star hotels in Bogor City.
2. The interaction between the budget participation variable and budget emphasis partially has no significant effect on the budget slack of star hotels in Bogor City, or in other words the budget emphasis variable is not able to act as a moderating variable (strengthens or weakens) the relationship between budget participation and budget slack. .
3. The interaction between budget participation variables and environmental uncertainty has a significant effect on the budget slack of star hotels in Bogor City, or in other words the environmental uncertainty variable moderates (strengthens) the relationship between budget participation and budget slack. environmental uncertainty acts as a moderating variable and is a quasi moderating.

Reference

- Anthony A. Atkinson, Robert S. Kaplan, Ella Mae Matsumura, S. Mark Young (2012), *Management Accounting: Information for Decision Making and Strategy Execution*, 6th edition, Pearson.
- Govindarajan, V. 2005, Fall. "Impact of Participation in the Budgetary Process on Managerial Attitude and Performance: Universalistic and Contingency Perspectives". *Decision Science* 17. No. 4.
- Mardiasmo. (2011). *Taxation*. Revised Edition. Yogyakarta. CV Andi Offset Merchant, K. A. and J. Manzoni. 1989, July. "The achievability of Budget Targets in Profit Centers: Field Study". *The Accounting Review*. LXIV. No.3.
- Suartana. I Wayan (2010). *Behavioral Accounting: Theory and Implementation*, Andi. Yogyakarta
- I.C. Kusuma, H. Hidayat, (2018). The Effect of Budget Participation on Budget Slack With Budget Emphasis and Environmental Uncertainty as Moderating Variables (Survey on Star Hotels in Bogor City). *Journal of Accountida*, Vol.1. June 2018. Bogor
- Winnie O'Grady et al. *Beyond Budgeting: Distinguishing Modes of Adaptive Performance Management*. *Advances in Management Accounting* - March 2017
- Junita, A; Erlina; Abubakar, E; Muda, I; Abdullah, S; (2019). Influence of budget participation and leadership style against rebudgeting on work unit of apparatus, *JBRMR* , Volume 13 Issue 02, 272-282 <https://doi.org/10.24052/JBRMR/V13IS02/ART-25>.
- Hasibuan, A.W, Siregar, Y.S, (2020). Budget Realization Report (Cash Basis Principle). *Turkish Online Journal of Qualitative Inquiry*. 11(4). 1030-1037. <https://tojqi.net/index.php/journal/article/view/8219>
- Purba, S., Muda, I., Lumbanraja, P., Kholis, A., & Bukit, R. (2021). The Influence of Budget Process, Internal Control, Organizational Characteristics on the Performance of Church Organizations in Indonesia. *Webology*,. 18(Special Issue). 765–772. <https://www.webology.org/data-cms/articles/20211101022951pmWEB18163.pdf>
- Becker, S. W. and David O. Green, Jr. 1962. October. "Budgeting and Employee Behavior". *Journal of Business*.

CHAPTER 6

The Origins of Positive Accounting Theory & How A Positive Theory Differs From A Normative Theory (The Anthropological Paradigm)

Celine¹, Royanti Sinaga², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹ Email : celinecang098@gmail.com

ABSTRACT

The purpose of this study is to summarize the origins of positive accounting theory, how accounting theory progress and how positive accounting theory differs from normative accounting theory. The progress of positive accounting theory cannot be separated from the dissatisfaction with normative theory, where references to Normative Accounting Theory began to be questioned again in the mid-1960s with the emergence of the efficient capital market hypothesis, such as the opposite idea began to emerge, which stated that the capital market was systematically wrong by certain accounting methods or techniques. Recognizing the existence of theoretical gaps in this strip, developed an approach started in positivism. If normative theory shows the best way to do something based on premises, norms, and standards, positive theory tries to predict real phenomena and test them empirically. That's why it stated that the rationale for analyzing normative accounting theory is too simple and does not provide a strong theoretical basis.

Keywords : The Origins Of Positive Accounting Theory, Accounting Theory, Normative Theory, Positive Theory, The Different A Positive Theory and Normative Theory.

1. INTRODUCTION

The evolution of accounting practices began in BC. The practice of accounting records at that time began with the single entry method and then developed into a double entry which has been documented since the publication of Luca Pacioli's writings in the 15th century. Research by Ball and Brown (1968) has changed accounting studies and the nature of capital market research (Kothari, 2001). Ball and Brown show that notification of corporate earnings has a significant effect on stock prices (Williams 2019).

The next development is the Positive Accounting Theory developed by Watts and Zimmerman (1986). Positive Accounting Theory, hereinafter shorted as PAT, is one of the accounting studies that predicts accounting practices when managers make decisions. Then it was developed with various writings like Demski (1988) by evaluating empirically, Boland and Gordon (1992) who criticized positive accounting theory and other authors by testing the opportunistic hypothesis.

The progress of positive accounting theory cannot be separated from the dissatisfaction with normative theory, where the reference to Normative Accounting Theory began to be questioned again in the mid-1960s with the emergence of the efficient market hypothesis which had a major influence on various accounting research, such as starting the opposite idea arises, which states that the capital market is systematically misled by certain accounting methods or techniques. Recognizing the theoretical gaps in this field, (Watts and Zimmerman, 1986) developed an approach started in positivism. If normative theory shows the best way to do something based on premises, norms, and standards. positive theory seeks to predict real phenomena and test them empirically (Godfrey et al, 1997). Therefore, it is stated that the rationale for analyzing normative accounting theory is too simple and does not provide a strong theoretical basis. The anthropological paradigm, which has had a positive response to this research, is the basis of the approach used to try to develop accounting theory from the explanation of certain actions and choices made in practice.

This research information is taken from various scientific insights, including the progress of positive accounting theory and normative theory. This study reviews those conducted by previous researchers such as Ball and Brown (1968), Wats and Zimmerman (1986), Demski (1988), Godfrey et la (1997), Khotari (2001), Setijaningsih (2012), and other researchers who discuss the development of accounting theory. Therefore, the author tries to summarize and focus this research on the origins of positive accounting theory and how positive accounting theory differs from normative accounting theory.

2. LITERATURE REVIEW

According to Ball and Brown (1968) investors do not necessarily believe that the company's financial statements have value. Kothari (2001) explains that accounting research does not scientifically discuss the effect of capital markets on financial statements, on the contrary, accounting research is a normative discussion of what is the purpose of accounting? What is should added with sentiment that report finance no useful for investors because assumed that accountant will choose method accountancy based on objective which they select. Ball and Brown's research is a modern foundation in accounting capital market research (Kothari, 2001).

Furthermore, positive accounting theory was developed by Watts and Zimmerman in 1978. The article has made positive accounting theory the dominant accounting research paradigm based on qualitative empirical and can be used to justify various accounting techniques or methods currently used or look for new models for theory development. accounting in the future (Bakar et al., 2021 and Warae et al., 2021). Explanations or predictions are made according to their correspondence with observations with the real world. an understanding of direct practice will lead to a more meaningful accounting system design (Ghozali, 2000).

Normative theory concentrates on the creation of true income during an accounting period or on the type of information that is useful in decision making (decision-usefulness). True income theory concentrates on creating a single, unique and true measure of assets and profits (Wardhani et al., 2022). While the decision usefulness approach assumes that the basic purpose of accounting is to assist the decision-making process by providing relevant or useful accounting data.

The demand for a positive approach to accounting occurred when Jensen and Meckling (1976) argued that research in accounting (with one or two notable exceptions) was unscientific. Furthermore, Jensen and Meckling expect the development of a positive accounting theory that will explain why accounting is what it is, why accountants do what they do, and what influence the phenomenon has on the use of people and resources.

There are three basic reasons for the shift in the normative to positive approach, namely (Watts and Zimmerman, 1986): (1) The inability of the normative approach to test theory empirically, because it is based on false premises or assumptions so that its validity cannot be tested empirically. (2) The normative approach focuses more on the prosperity of individual investors than on the prosperity of the wider community. (3) The normative approach does not encourage or enable the optimal allocation of economic resources in the capital market. This is considering that in an economic system based on market mechanisms, accounting information can be a controlling tool for the community in allocating economic resources efficiently.

3. METHOD

The basis of this research uses qualitative research methods that are used from the beginning to the end of the study. In this way, it is hoped that there will be overall consistency of the data in the research analysis. The data analysis used in this research is logical, because this research is descriptive. Anthropological paradigm is a meaningful and productive paradigm that is able to explain significant phenomena critically and comparatively.

The inductive method is a way of scientific analysis that moves from things that are specific to things that are general (Suaedi, 2016). On the basis of this research is generating theory, so that the resulting theory is a substantive theory (Enny and Andi 2017).

4. RESULTS AND DISCUSSION

4.1. Results

Theory Accountancy Positive

Transition PAT is key factor in describe importance creation Ball and Brown on year 1968 (Kothari, 2001). Next Watts and Zimmerman build step beginning and popularize PAT (Kothari, 2001). Watts and Zimmerman in year 1970s make accountancy more towards objective than normative. Before Watts and Zimmerman research, there is no agreement about objective accountancy, and believed that accountant only will choose method accountancy based on usage subjective they or opinion subjective they about how financial statement them by using document (Kothari, 2001).

PAT has been widely tested using accounting method choices. Christie (1990: 15-36) concludes that there are six proxies that are known to have the ability to explain practices that are a reflection of the application of positive accounting theory. The six proxies include company size, level of risk, managerial compensation, portion of debt to assets or capital, limits on debt settlement, and dividend payout ratio.

Lev's (1979) research relates to the bonus-debt covenant hypothesis, where there is a tendency for managers to be opportunistic by saving bonuses and ignoring changes in debt covenants when the expected market efficiency reacts negatively.

The research wants to prove that managers who base their bonuses on net income prefer to use accrual accounting policies for reporting their income so that they can maximize bonuses. The results of the study found strong evidence that management's decision to choose or adopt an accounting regulation is closely related to how sensitive the bonus is associated with achieving profit targets. These results reflect the importance of understanding the behavior of managers towards the existence of a compensation plan that can affect their current and future prosperity.

Normative and Positive Issues

Theorists are very careful to distinguish between positive and normative meanings. According to Budiarto and Murtanto (1999), positive issues are feared to have a very wide influence and can lead to missions of interpretation in actual practice. Suppose they make an analogy that "If A then B is proven incorrect" and formulated in a positive question to be "if the company changes its inventory valuation method from FIFO to LIFO and the capital market does not anticipate the change. In the sense that the capital market does not directly absorb the information of the change, then the stock price will rise. The statement indicates that the change in method from FIFO to LIFO cannot be proven empirically with existing or available data. This is the essence of a positive approach.

In the normative approach, there is a tendency to interpret the above statement on a more prescriptive basis than descriptive. For example, they ask question A, there is a tendency for change or group of companies in condition C, then alternative D will be chosen. Then the normative formulation is made as follows: When prices rise, the LIFO method tends to be used.

So the existence of a tendency towards certain goals to be achieved from a statement can provide clues to researchers in predicting a certain condition and as a basis for assessing empirical validity, or in other words a statement does not have to be empirically proven and tested for validity alone, but also see the objectives to be achieved from the statement and this is a social choice that has economic consequences that can change at any time if the environment changes.

The positive approach looks at "why accounting practice and/or accounting theory develops as it is with the aim of explaining (to explain) and predict (to predict) accounting events. Therefore, the positive approach seeks to determine the various factors that might influence rational factors in the accounting field. Basically the positive approach seeks to determine a theory that explains the observed phenomena. The positive approach is generally distinguished from the normative approach which seeks to define a theory that explains "what ought to be" rather than "what is". The positive approach seems to have generated considerable optimism among its supporters. But this sense of optimism is not shared naturally by everyone.

The early development of accounting theory resulted in a normative theory which is defined as a theory that requires. The normative theory uses a value judgment that contains a minimum premise (Wolk & Tearney, 1997:32). At the beginning of its development, the writing of normative accounting theory did not use a formal investigative approach. Theories are structured primarily to develop accounting postulates.

4.2. Discussion

This research information is taken from various scientific insights, including the theory of development of positive accounting theory and normative accounting theory. Some of the theories proposed in this study are the development of positive accounting theory and how positive theory differs from normative.

For those who adopt this research, the basic research material is accounting theory which consists of normative accounting theory which provides formulas for accounting practice and positive accounting theory that seek to explain and predict accounting-related phenomena. The normative approach that has victorious for a decade turns out to be unable to produce accounting theory that is ready to be used in everyday practice. Design The accounting system resulting from normative research is in fact not used in practice. As a result, there are suggestions for a descriptive understanding of the functioning of the accounting system in real practice.

The presence of positive accounting theory has had a great influence on the development of accounting, namely generating systematic patterns in accounting choices and providing specific explanations for these patterns, providing a clear framework for understanding accounting, explaining why accounting is used and providing a framework for predicting accounting choices. encourage relevant research where accounting emphasizes the prediction and explanation of accounting phenomena.

5. CONCLUSION

The progress of accounting theory through research conducted by accounting experts. The progress of accounting theory began at the beginning of the 20th century, much later than the progress of double entry accounting practices that could be drawn back several centuries ago. Accounting experts began to develop normative accounting theory without a formal methodology.

The use of formal deductive and inductive methods in accounting research has succeeded in developing accounting theory out of leading to a wider strip. Accounting researchers use theories from various sciences such as economics, psychology, management, sociology, and other sector in their research, so that accounting theory develops as it is today.

The main purpose of accounting theory is to provide a basis for predicting and explaining accounting behavior and events. The normative theory uses value considerations, while the positive theory (descriptive theory) attempts to find the relationships that actually occur.

There are several basic reasons for the shift from a normative approach to a positive one, namely (Budiarto and Murtanto, 1999): (a) the inability of the normative approach to test theory empirically, (b) the normative approach focuses more on the prosperity of individual investors rather than the prosperity of society. broad, (c) the normative approach does not encourage or enable the optimal allocation of economic resources in the capital market.

REFERENCE

Bakar, E. A., Nedelea, A., & Wardhani, M. M. (2021). The Influence of Using SAP CRM On Increasing Customer Satisfaction Index at Pt. Bank X In Medan, Indonesia. *The USV Annals of Economics and Public Administration*, 21(1).33-44.
<http://annals.seap.usv.ro/index.php/annals/index>

- Ball, Ray and P. Brown (1968). An Empirical Evaluation of Accounting Income Numbers”, *Journal of Accounting Research* (Autumn 1968). 159-178.
- Baridwan, Zaki, (2000). Theory Development and Accounting Research. *Indonesian Journal of Economics and Business* (October 200). 486 – 497
- Boland, L.A and I.M. Gordon, (1992). Criticizing Positive Accounting Theory,” *Contemporary Accounting Research* (Fall 1992). 147-170.
- Budiarto, A and Murtanto (1999). Accounting Theory: From a Normative to a Positive Approach. *Journal of Business and Accounting* (December 1999). 163-182
- Christie, A.A. and J. Zimmerman (1994). Efficient and Opportunistic Choices of Accounting Procedures: Corporate Control Contests,”*The Accounting Review* (October 1994), pp.539-566.
- Damn, Hamonangan. (2020). Accounting Theory. Medan : LPPM UHN Press.
- Demski, J. (1988). Positive Accounting Theory: A Review. *Accounting, Organizations & Society* (October 1988). 623-629.
- Ghozali, Imam. (2002). Accounting Research Paradigm, National Accounting Dialogue Seminar, Semarang, November.
- Godfrey, J., Allan Hodgson, and Scott Holmes. (1997). *Accounting Theory*. 3rd ed. New York: John Wiley & Sons, 1997.
- Kothari, S.P., (1999). Capital markets research in accounting. *Journal of Accounting and Economics* (November 1999). 105-231.
- Lev, Baruch dan James A. Ohlson, (1982). Market Based Empirical Research in Accounting: a Review, Interpretation, and Extension”, *Journal of Accounting Research*. .249-322.
- Setijaningsih, Herlin Tundjung, (2012). Positive Accounting Theory and Economic Consequences. *Journal of Accounting* (September 2012), 427-438.
- Suaedi. (2016). Introduction to the Philosophy of Science. Bogor : PT. Publisher IPB Press.
- Suryandi, Budi. (2012). Introduction to Anthropology. Banjarmasin : P3AI UNLAM
- Warae, Y., Sigalingging, E. D., Abubakar, E., & Nedelea, A. M. (2021). Revealing Auditor and Auditee Satisfaction In The Evolution Of Accounting Software (Phenomenology Study In The Regional Government Of South Nias District). *Ecoforum Journal*, 10(2). [Http://www.Ecoforumjournal.Ro/Index.Php/Eco/Article/View/1210/744](http://www.Ecoforumjournal.Ro/Index.Php/Eco/Article/View/1210/744)
- Wardhani, M. M., Padang, N.N & Nedelea, A. M. (2022). Indicators of Giving Interest Rates to Customers and Debtors at PT. Bank X in Medan, Indonesia. *Ecoforum Journal*, 11(1). 1-6. <http://www.ecoforumjournal.ro/index.php/eco/article/view/1284/789>
- Watts, R., Zimmerman, J. (1990). Positive accounting theory: a ten-year perspective”, *The Accounting Review*. 131–156.
- Wolk, Harry I. And M.G. Tearney. (1997). Accounting Theory. A Conceptual and Institutional Approach. 4th ed. Cincinnati, Ohio: South-Western College Publishing.

Accounting Inquiries with New Approaches in the Post-Pandemic Era
Volume I

CHAPTER 7

Continental European Model - The Models Implement of Financial Accounting

Bobby Ricardo Parasian Siregar¹, Adela Oktaviani Simbolon², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹ Correspondent Author Email:bobby.ricardo@student.usu.ac.id

ABSTRACT

The aim of the study is to see how the Continental European accounting model is implemented in accounting principles that apply and are used in Italy, France and Germany. In Germany, the driving force for reforming the financial reporting regime is that compliance with national accounting regulations appears to prevent firms from fully profiting in international capital markets. In Italy, the most significant changes to accounting regulations were caused by European and international pressure on the use of international accounting standards as a means to increase the competitiveness of companies. This study describes the European continental model in the financial accounting implementation model. For example, in the EU context, IFRS is required for consolidated accounting, using France

Keywords : Continental European Model, Implementation, Financial Accounting, IFRS, France, Germany, Italy, Descriptive Approach.

INTRODUCTION

Accounting regulations in Europe are undergoing a period of major change. The introduction of International Financial Reporting Standards (IFRS) for financial reporting has added further impetus to the goal of convergence of international accounting rules (Caroline et al., 2022). As of January 1, 2005, more than 7,000 listed companies are required to set up their consolidated accounts using IFRS. The pressure to integrate capital markets in Europe has prompted the European Commission to introduce uniform financial reporting standards for EU listed companies (van Hulle, 2003). Recognizing the advantages of harmonization of international financial reporting for EU companies with lists outside the EU acknowledging that no European corporate accounting standard can be used for this purpose, IFRS was introduced as a mandatory standard (Hellemann, 2013). Legal instrument EU Regulation (No. 1606/2002) adopted by the European Commission to have a direct effect on listed companies (Unurenau, 2012). However, member country options are permitted for the application of IFRS on individual company accounts and on consolidated accounts of unregistered companies. When comparing developments and approaches used to integrate current accounting reforms in France, Germany and Italy, it becomes clear that although the process of internationalization of financial reporting has increased rapidly in these countries in recent years, the impact is different and the process varies in speed in each. -each country. 1606/2002) was adopted by the European Commission to have a direct effect on listed companies. However, member country options are permitted for the application of IFRS on individual company accounts and on consolidated accounts of unregistered companies. When comparing developments and approaches used to integrate current accounting reforms in France, Germany and Italy, it becomes clear that although the process of internationalization of financial reporting has increased rapidly in these countries in recent years, the impact is different and the process varies in speed in each. -each country. 1606/2002) was adopted by the European Commission to have a direct effect on listed companies. However, member country options are permitted for the application of IFRS on individual company accounts and on consolidated accounts of unregistered companies. When comparing developments and approaches used to integrate current accounting reforms in France, Germany and Italy, it becomes clear that although the process of internationalization of financial reporting has increased rapidly in these countries in recent years, the impact is different and the process varies in speed in each country (Delvaile et al., 2021).

In the mid-1990s, the French financial reporting system continued to evolve and aimed at increasing the transparency of information published in response to market pressures. In particular, larger French companies can use some of the options opened by the 1986 decree on consolidated accounts to allow them to converge towards internationally accepted accounting standards and seek government permission to structure their accounts directly according to the standard (Kuhlmann, 2010). The government finally approved and passed a law on April 6, 1998, whereby companies registered in France are no longer required to follow French law for the preparation of their consolidated accounts. In 2003, the publication of Loi de Sécurité Financière (LSF 2003-706, Financial Security Act) introduced a number of important changes (Ooghe et al., 2002). This law resulted not only from changes introduced by the European Commission but also as a consequence of the American Sarbanes Oxley Act, as it implements new procedures for regulation of financial markets, the auditing profession and financial information in order to increase transparency and control over financial reporting and securities transactions. .

In Germany, the driving force for reforming financial reporting regimes is that compliance with national accounting regulations appears to prevent firms from fully profiting in international capital markets (Ebke, 1997). companies registered in Germany are required to apply IFRS in their consolidated accounts from 2005 onwards. Registered companies that have applied US GAAP in the past will have permission to apply IFRS from January 1, 2007 in accordance with the art transition rules. 9 in EU Regulations. The Accounting Law Reform Act, which was also effective January 1, 2005, requires non-listing companies to use IFRS. All companies that are not publicly traded have the option to use IFRS in their consolidated accounts. If a company adopts IFRS, it

must comply with all IFRS (Daulay, 2020, Tiosanna, 2020). In addition, the law contains the option to apply IFRS in individual accounts for publication purposes (Federal Gazette). However, it is important to note that this option is limited to informational purposes only. All companies must present their respective financial statements in accordance with the German Commercial Code (HGB) for the purpose of calculating taxes and distributing dividends. Therefore, HGB remains mandatory for individual accounts in Germany, however, companies can only publish their IFRS accounts. In addition, the Accounting Law Reform Act introduced a number of other important changes with respect to financial reporting (Haller and Eierle, 2004). For example,

In Italy, the most significant changes to accounting regulations were caused by European and international pressure on the use of international accounting standards as a means to increase the competitiveness of firms (Lumbantobing et al, 2022). Italy was the first country in Europe to pass a law allowing registered companies to use 'internationally recognized' accounting standards in their consolidated accounts. Legislative Decree n.58 of 24 February 1998 in art. 117, section 2, states: The Minister of Justice identifies, by separate decision, accounting standards that are internationally recognized and compatible with the relevant EU Directives, on the basis of which listed companies can prepare their consolidated accounts departing from applicable local rules, This study describes the European continental model in the financial accounting implementation model. For example, in the EU context, IFRS is required for consolidated accounting, using France, Germany and Italy as case studies.

LITERATURE REVIEW

The dominant taxonomy in international accounting is Nobes (1998) classification which divides the accounting system into two classes which are labeled Class A and Class B. These two classes are known as the Anglo-American accounting model and the Continental European accounting model, respectively. Nobes points out that the main difference between these two classes is attributed to one major variable, namely the financing system, and considers Germany as a clear example of a country that is expected to have a Continental European accounting model.

The Financial Reporting Control Act and the Accounting Law Reform Act are particularly driven by EU legislation and the need for greater convergence within the EU (Haller, 2002). However, this Act greatly affects the consolidated financial statements. Importantly, neither of these regulations significantly changes the fundamental recognition and valuation principles included in HGB. Thus, many of the characteristics that have been described as typical of the Continental European model for binding individual firm financial statements for which the Nobes classification can still be valid.

The British/American model of accounting, the South American Model, the Continental European Model, the Communist Model, the Mixed Economy Model, and the International Accounting Model have explicit roles in the economy and the accounting profession. in general. The largest group is referred to as the Continental European System, because all the countries in this group (except Canada) are located in Europe and these countries (except the UK) have played an important role in the development of the Continental European accounting system (Delville et al., 2011). Despite these differences in accounting models, they have helped in uniformity among various aspects of the financial presentation of the countries that practice them.

Ooghe (2002) observe that international accounting standards have an impact on the preparation of the financial statements of multinational organizations when they are adhered to in increasing comparisons between different countries. Lubis et al (2022) notes that the purpose of using an international accounting information system is very similar to that of accounting transactions that are treated equally by companies around the world, resulting in globally comparable financial statements. According to Tarigan (2022) there are factors that have gradually led to the existence and development of international accounting as an indispensable subdiscipline of the accounting discipline. These include Economic Globalization, Emerging Markets, the World Bank, Foreign Investment, Multinational Enterprises, and Regional Trade Arrangements. Assert

that the move towards a free-standing international standards model is gathering momentum when the European Union (EU) embarks on a major push to align accounting directives with the International Accounting Standards Board (IASB).

3. Method

In this study, a descriptive approach was chosen by collecting previous literature. This journal contains examples of possible cases that may occur in your company. The purpose of this journal is to examine the accounting behavior of companies that apply international reporting requirements and to interpret whether and to what extent annual reports have been produced using IFRS.

4. Results and Discussion

4.1. Results

Nearly all 30 DAX companies adopted IFRS or US GAAP in their consolidated accounts in 2003 (see Table 1). As can be seen, the majority of German DAX companies implement IFRS, only nine companies adopt US GAAP for the main financial statements. In contrast, in France and Italy, generally no pure compilers of IFRS or US GAAP can be found. However, exceptions exist: in France two of the companies included in the CAC 40 index – EADS and ST Microelectronics – use IFRS and US GAAP, respectively. CONSOB using foreign currency GAAP is considered appropriate financial information: reports under US GAAP presented by Luxottica obtain this approval. evaluate, on a case-by-case basis, whether the financial reporting presented for mandatory convergence to IFRS in 2005, German companies have developed significant experience with all using international standards for consolidated financial statements. In contrast their French and Italian counterparts were generally all 'First-time adopters' of IFRS in 2005. Our empirical results have been compared with a survey on the preparation of European firms for the switch to IFRS published by Mazars (2003) which supports the findings in the empirical research of this paper. . However, ST Microelectronics must issue a reconciliation statement of equity and income (from a US GAAP number to a French GAAP number). Of the 15 French companies listed in the US, half chose to include a reconciliation from French GAAP to US GAAP in the annual report while the other half published this statement only on Form 20-F. Furthermore, a number of French companies state that their financial statements are at least partially compliant with IFRS, but generally with significant exceptions. For example, during the investigation period Renault applied international accounting standards, with the exception of IAS 39. It should be noted that prior to 2000, several French companies referred to their financial statements as (“generally” or “with some exceptions”) in accordance with IAS. In fact, since 1986, the consolidated account regulations in France allow companies as an option to depart from the generally accepted accounting principles used for individual accounts in France. during the investigation period Renault applied international accounting standards, with the exception of IAS 39. It should be noted that prior to 2000, several French companies referred to their financial statements as (“generally” or “with some exceptions”) in accordance with IAS. In fact, since 1986, the consolidated account regulations in France allow companies as an option to depart from the generally accepted accounting principles used for individual accounts in France. during the investigation period Renault applied international accounting standards, with the exception of IAS 39. It should be noted that prior to 2000, several French companies referred to their financial statements as (“generally” or “with some exceptions”) in accordance with IAS. In fact, since 1986, the consolidated account regulations in France allow companies as an option to depart from the generally accepted accounting principles used for individual accounts in France.

However, several researchers (Dick and Walton, 2001; Stolowy and Ding, 2003) have provided evidence that firms use “IAS lite” and exhibit a certain degree of “opportunism”. In fact, when the IASC revised IAS 1 to prevent companies from referring to conformity with the IAS unless they comply with all standards, the study observed a reduction in references to international standards by the French group even if no change in accounting policy occurred. For example, of the

13 large French companies that appeared to implement 'IFRS' before 31 December 1999, 8 companies omitted the IFRS reference even though this group did not change their accounting principles and financial disclosures from one year to the next (Dick and Walton, 2001). In 2001, To provide investors with more transparent financial information, COB requires French companies registered in the US to present their reconciliations not only on Form 20-F but also in their annual reports. At that time, 14 French industrial companies (from the CAC index 40) were concerned but not all provided information. It seems that in the meantime more companies are following the COB recommendations.

As can be seen in the table between 2002 and 2003, two more companies followed the recommendation to publish reconciliation statements in their annual reports, not just Form 20-F. A study conducted by FinHarmony (2005) showed that the main causes of differences are the treatment of intangible assets and their depreciation (IAS 36 and 38), goodwill arising from consolidation (IFRS 3), stock options (IFRS 2), financial instruments (IAS 39) and pension obligations (IAS 19). Quantitatively, however, the reconciliation did not lead to significant differences, and the adjustments partially offset each other. For example, LVMH balanced a deferred tax adjustment on trademarks with a minority rights adjustment in 2003. In Germany, with the exception of two companies, all German DAX 30 companies apply IFRS or US GAAP for the financial year ending 2003. Companies with US listings apply full US GAAP accounting or provide reconciliations to US GAAP in either annual reports (Ra) or Form 20-F (rf). Compliance with IFRS or US GAAP is controlled by auditors or the SEC. Two companies that are still implementing HGB are Deutsche Telecom and BASF, both US issuers that have disclosed reconciliations with US GAAP. In Italy, although a large number of Italian S&P/MIB companies are registered in the US and required to provide US GAAP reconciliations, only two companies, Luxottica and ST Microelectronics, apply US GAAP directly. Furthermore, despite the legislative indications and CONSOB statements in favor of IFRS, in Italy there was no significant use of IFRS in the financial statements during the investigation period. However, similar to France, in Italy, a number of companies refer to 'international accounting standards' particularly when accounting matters are not covered by national GAAP. References to the use of IFRS are not very precise. For example, in its 2003 consolidated accounts Bulgari SpA stated that the reports were prepared 'with respect to commercial law and the CNDC&R accounting standards and, if necessary, There is no evidence of complete IFRS financial statements. However, IFRS was used as a reference source (18 companies). It is not clear whether this statement corresponds to the partial application of IFRS in Italy as only in some cases information about a particular IFRS is provided in the notes. For example, FIAT stated in the notes to the consolidated accounts in 2003 that IAS 39 for financial instruments was applied while Mondadori applied IAS 17 for leases in the 2003 consolidated accounts. A number of companies referred to projects transitioning to IFRS. In 2003, the nine companies referred to in the IFRS transition project were: Benetton Group, Capitalia, FIAT, Finmeccanica, Fondiaria SAI, RCS Mediagroup, TIM, Telecom Italia, Tiscali.

Table 1. Comparison of the use of international and national standards (in 2003)

2003			
GAAP disclosed	German (DAX 30)	France (CAC 40)	Italy (S&P/MIB)
As the main reporting standard			
National GAAP	2	38	38
IFRS	19	1	-
US GAAP	9	1	2
Total	30	40	40
Reconciliation Statement From GAAP national to IFRS From GAAP national to US GAAP From IFRS to US GAAP	2 4	15	6

From US GAAP to national GAAP		1	2
-------------------------------	--	----------	----------

4.2. Discussion

The introduction of EU Regulations had a relatively higher impact in France and Italy, where effectively listed companies first adopted IFRS in January 2005. In particular, Italy will experience significant changes due to the mandatory requirement to apply IFRS on individual accounts in 2006. On the one hand, the extension of the application of EU Regulations to individual accounts in Italy seems contradictory. IFRS is issued with the aim of making useful decisions and providing relevant information for investors. While some believe that the informational relevance of IFRS will also benefit creditor protection purposes (Niehus, 2001), in general there seems to be more to the disadvantage for European companies to adopt IFRS in individual accounts, because IFRS is not designed to account for taxes or dividend payments, in particular for small companies, unless the IASB is rapidly expanding its projects on SMEs. However, recent legislative intervention in Italy aims to eliminate the link between commercial and fiscal rules and thus appears to have facilitated the process. Elimination of the relationship between tax rules and accounting numbers seems to be a prerequisite for applying IFRS to individual company accounts.

In Germany, this step is not expected in the medium term (Herzig, 2005). Similarly in France, the relationship between accounting and taxation is currently maintained. However, it could be abandoned in the future if the evolution of French accounting law towards IFRS is not compatible with the tax approach applicable to individual accounts. As required by the CESR in the first standard of financial information published in April 2003,30 all three countries have instituted bodies to deal with the enforcement of accounting rules by listed companies. While in Germany, a separate enforcement authority has been established by German industry, in France and Italy a capital market authority handles law enforcement. Recent Italian corporate scandals (e.g. Cirio),

5. Conclusion

The conclusion that can be drawn from the explanation of the implementation of the Continental European model above is that the use of IFRS is most prominent in Germany. In fact, the decision of German legislators in 1998 to exempt companies from applying the HGB rule in consolidated accounts and use IFRS or US GAAP instead, had a significant impact on financial reporting practices. Nearly all 30 DAX companies implemented IFRS or US GAAP in their consolidated accounts in 2003.

Reference

- Caroline, Davy, S., Baihaqi S., (2022). The Five Financial Statements based on IFRS and How They are Prepared. *Journal of Positive School Psychology*. 6(3). 2343–2354. <https://journalppw.com/index.php/jpsp/article/view/1962>
- Daulay, G.P.D, Syahputra, R , (2020). How to Account The Accounts for Current Liabilities Based on IFRS Standard?. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 890-895. <https://tojqi.net/index.php/journal/article/view/8198>
- Delvaille, Pascale, Ebberts, Gabi, and Saccon, Chiara, (2011). International Financial Reporting Convergence: Evidence from Three Continental European Countries, *Accounting in Europe*, 2:1, 137-164, London
- Hellman, Andreas, Perera, Hector, and Patel, Chris, (2013). Continental European accounting model and accounting modernization in Germany, Macquire University, Sydney, NSW 2109, Australia
- Herzig, R. (2005). *Suffering for science: Reason and sacrifice in modern America*. Rutgers University Press.
- Kuhlmann, Sabine, (2010). New public management for the 'Classical Continental European Administration': modernization at the local level in Germany, France, and Italy, Blackwell Publishing Ltd, Malden, USA

- Lubis, M. G., Dai, M., Sitorus, S., & Muda, I. (2022). The Usefulness and Format of The Statement Of Cash Flows Based on IFRS. *International Journal of Mechanical Engineering*. 7(1). 6796-6803. https://kalaharijournals.com/resources/IJME_Vol7.1_721.pdf
- Lumbantobing, W.A, Marina, N.L & Muda, I. (2022). Apply Horizontal Analysis and Vertical Analysis To Financial Statements Based On IFRS. *International Journal of Mechanical Engineering*. 7(1). 6791 - . 6795. https://kalaharijournals.com/resources/IJME_Vol7.1_720.pdf
- Niehus, H., Blum, R. P., & Ahlbehrendt, D. (2001). Formation of vanadium oxide films on Cu₃Au (100). *physica status solidi (a)*, 187(1), 151-159.
- Ooghe, Hubert and DeLanghe, Tine, (2002). The Anglo-American versus the Continental European corporate governance model: empirical evidence of board composition in Belgium, *European Business Review*, Vol. 14.
- Stolowy, H., & Ding, Y. (2003). Regulatory flexibility and management opportunism in the choice of alternative accounting standards: an illustration based on large French groups. *The International journal of accounting*, 38(2), 195-213.
- Tarigan, A, Ramadhani, I.F, (2022). Principles and Assumptions in Financial Reporting Based on IFRS. *Journal of Positive School Psychology*. 6(3). 2333–2342. <https://journalppw.com/index.php/jpsp/article/view/1961>
- Tiosanna, A, Rosadi, A.F, (2020). Presentation of Financial Statements of Cash Item Based On IFRS International Standards. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 957-963. <https://tojqi.net/index.php/journal/article/view/8208>
- Unurenau, Mihaela (2012). Models and practice of corporate governance worldwide, Leibniz Information Center for Economics.
- Walton, T. A., Dick, D. J., Hudson, D., Johansson, M. K., Lyttle, M. H., Songster, M. F., & Cook, R. M. (2001). New Quencher Derivatives for Fluorescence Quenching Peptide Assays. In *Peptides: The Wave of the Future* (pp. 54-55). Springer, Dordrecht.

Accounting Inquiries with New Approaches in the Post-Pandemic Era
Volume I

CHAPTER 8

The Types of Rewards that Organizations use and Positive and Negative Rewards

Nazla Aminy¹, Kurnia Dewi², & Iskandar Muda³

^{1,2,3} Master of Accounting, Universitas Sumatera Utara, Medan, Indonesia

¹ Corresponding Email: nia.tanimas@yahoo.com

ABSTRACT

Each employee's performance is important in an organization. A way to motivate it is through the application of reinforcement theory which is developed by B. F. Skinner. One of the most commonly used methods is positive reinforcement in which one's behavior is strengthened or increased based on consequences. This paper aims to review the impact of positive reinforcement on the performances of employees in organizations. It can be applied by utilizing extrinsic reward or intrinsic reward. Extrinsic rewards include salary, bonus and fringe benefit while intrinsic rewards are praise, encouragement and empowerment. By applying positive reinforcement in these factors, desired positive behaviors are encouraged and negative behaviors are eliminated. Financial and non-financial incentives have a positive relationship with the efficiency and effectiveness of staffs.

Keywords : Positive Reinforcement; Employees' Performance; Motivation

1. Introduction

Organizational Behavior is a scientific discipline that studies behavior at the individual level and at the group level in an organization and its impact on performance (both individual, group, and organizational performance). Organizational behavior is also known as the study of organizations (Siregar, 2019). This study is a special academic field of study that studies organization, by utilizing the methods of economy, sociology, political science, anthropology and psychology. The scope of organizational behavior is quite broad and numerous, but here we will discuss "Goal setting in organizational performance and reward systems". Other disciplines related to this study are the study of human Resources and industrial psychology. The organization in the view of some experts seems to be an "animal" that has many forms, but still has conceptual similarities. Or in other words, the formulation of the organization is very dependent on the particular context and perspective of the person who formulates it. Every human being has a different goal in life, because of the influence of different knowledge and experiences. But every human being will be the same in one thing, namely wanting to maintain life and fulfill their needs. For people in the current era of industrialization, work is a very important aspect of life. For modern society, work is a basic demand, either in order to obtain rewards in the form of money or services, or in order to develop themselves. Organizations use rewards to attract and retain people and motivate them to achieve personal and organizational goals. The manner and timing of the distribution of rewards are important issues that managers have to deal with on an almost daily basis. Managers distribute rewards such as salaries, transfers, promotions, praise and recognition. Because these rewards are considered important by employees, they have a significant effect on behavior and performance.

2. Literature Review

2.1. Definition Of Purpose

Employee performance is the level against which employees achieve job requirements. What is meant by a performance appraisal system is a process that measures employee performance. Meanwhile, according to Katou (2021): High performance can be achieved because of the high reciprocal trust among its members, meaning that members trust the integrity, characteristics, and abilities of each other member. To achieve high performance takes a long time to build, requires trust, and demands careful attention from management.

3. Method

The method of writing this paper uses the literature method, this method is the method used to collect data or sources related to the topic raised in a study, literature studies can be obtained from various sources, journals, documentation books, internet and libraries

4. Result and Discussion

4.1 Result

The purpose of holding a performance appraisal for employees can be divided into two, namely:

a. Evaluation purpose

A manager assesses the past performance of an employee by using descriptive ratings to assess performance and with this data useful in promotion decisions, demotion, termination and compensation.

b. Development goals

A manager tries to improve the performance of an employee in the future.

While the main objectives of the employee performance appraisal system are: something that produces accurate and valid information regarding the behavior and performance of members of the organization or company. A goal is an end result, an end point or anything to be achieved Organizational Mission and Goals. Before the organization determines its goals, it must first

determine the mission / goals of the organization. Mission is a general and enduring statement of an organization's purpose. While the mission of the organization is a distinctive (unique) and fundamental purpose that distinguishes the organization from other organizations and identifies the scope of operations in terms of products and markets.

Bushi et al (2021) defines organizational goals as a statement about the desired state which the organization intends to realize and as a statement about a future state which the organization as a collective tries to achieve. Organizational goals are statements about circumstances or situations that do not exist now but are intended to be achieved in the future through organizational activities. So, the two important elements of organization are:

- a. The desired end results in the future, with which
- b. Efforts or activities are now directed. These goals can be general or specific goals, ultimate goals, or intermediate goals.

OBJECTIVE FUNCTION

- a. Guidelines for Activities, through the description of future results (Soto et al., 2021). The objective function provides direction and centralization of organizational activities regarding what should and should not be done;
- b. Legitimacy Resources, will increase the organization's ability to get resources and support from the surrounding environment;
- c. Implementation Standards, if the objectives are clearly and understood, will provide a direct standard for evaluating the implementation of the organization's activities (achievements);
- d. Motivation Standard, serves as an important employee motivation and identification. In fact, organizational goals often provide incentives for members;
- e. Rational Basis for Organizing, organizational goals are a basis for organizational design.

TYPES OF OBJECTIVES

In achieving goals, there are several types that help the process of setting organizational goals. The five types of goals can be broken down as follows:

- a. Social goals (social goals), society in general and concerned with broad organizational classes that meet human needs;
- b. Output goals (output goals), the public in relation to the organization and with respect to certain types of output in the form of consumer functions;
- c. System goals (system goals), the way the organization functions do not depend on the goods or services produced. Example: Profit;
- d. Product goals (product goals) or product characteristics objectives, characteristics of goods or services produced;
- e. Derived goals, which the organization uses to put its power in achieving goals.

GOAL-SETTING PROCESS

It is an effort to create certain values through various activities that will be carried out by the organization. Some of the basic elements of setting an organization's goals to create these values are:

- a. That the goods and services produced by the organization will be able to provide various benefits at least equal to the price;
- b. That goods and services can satisfy the needs of consumers/subscribers;
- c. That the technology used in the production process will produce goods and services at competitive costs and quality;
- d. That with hard work and the support of all its resources, the organization can operate better than just to survive, namely for growth and can generate profits;
- e. That management services will provide a favorable public image, so that they are willing to invest and contribute their energy to help the organization's success;

- f. That the company has a self-concept that can be communicated and transmitted to employees and organizational shareholders.

OBJECTIVE FORMULATION

Objectives are formulated taking into account all the forces involved in the organization's operations. The formulation of goals is the result of a combined effort to satisfy all parties or a set of various individual and organizational goals. In order to formulate effective goals, managers need to pay attention to the following conditions.

- a. The process of goal formulation should involve individuals who are responsible for achieving the goals;
- b. Top managers as formulator of general goals, should be responsible for deriving goals at lower levels;
- c. Goals must be realistic, aligned with the internal and external environment, both now and in the future;
- d. Goals must be clear, reasoned and challenging for the members of the organization;
- e. General objectives should be stated in a simple manner so that it is easy for implementers to understand and remember;
- f. The objectives of the functional areas of the organization must be consistent with the general objectives;
- g. Management must always review the goals that have been set, and if necessary change and improve them according to environmental developments.

4.2 Discussion

A. MANAGEMENT BY PURPOSE

1. MANAGEMENT BY OBJECTIVE (MBO)

It was first introduced by Peter Drucker in his book *The Practice of Management* in 1954. Management by objectives can also be referred to as management by objectives, management by results (Management by Result), Goals management, Work planning and review and so on which are essentially the same (Ogochukwu et al., 2022).

Management by objective emphasizes the importance of the role of goals in effective planning, by establishing procedures for achieving both formal and informal, first by setting goals to be achieved, followed by activities to be carried out until completion, then a review of the work that has been carried out is carried out. MBO activity stands for management by objective, which is a participatory process involving subordinates and managers at every level of the organization which is formulated in the form of a mission or target, which can be measured using this measure as a guide for the operation of the work unit.

2. Effective Management By Objective System

- a. There is a commitment of managers to personal and organizational goals, so he must meet with his subordinates to provide goal setting and evaluate them;
- b. Determination of top management goals expressed in certain measurable values, so that between managers and subordinates have a clear idea of what is expected by top management, so that it can be known between individuals and the goals of the organization as a whole;
- c. Individual goals, where between managers and subordinates must formulate common goals and responsibilities for their parts clearly in order to understand what will be achieved;
- d. The need for the participation of all parties, where the greater the participation of all members, the greater the goals to be achieved;
- e. Autonomy and implementation of plans, here subordinates and managers are free to develop and implement programs to achieve their goals;

- f. Periodic review of achievements against progress towards goals.

3. The Pros and Cons of MBO

Kind:

- a. Knowing what is expected of the organization;
- b. Helping managers set goals and objectives;
- c. Improve vertical communication between managers and subordinates;
- d. Create an evaluation process.

Weakness:

- a. The weaknesses inherent in the MBO process, in the consumption of time and large costs;
- b. In terms of development and implementation of MBO programs.

4. MBO Effectiveness Elements

- a. In order for MBO to be successful, managers must understand and have the skills to know the benefits and uses of MBO;
- b. Goals are realistic and easy to understand by anyone, so they are often used to evaluate the work performance of a manager, whether he succeeds in his duties or fails;
- c. Top managers must keep these MBO systems up and running as they should;
- d. Without the participation of all parties it is impossible for this MBO program to run, so all parties must know their position in relation to the goals to be achieved, feedback on them is very useful.

B. FEEDBACK

Feedback or Feedback are two invented / formed words in English which consist of the words feed (meaning: giving) and back (meaning: back). The literal meaning of this word is “to give back”, but its real meaning is “to give back”.

1. Definition of Feedback

- a. In the social sciences, especially Communication Studies, the notion of feedback is a process in which a person tells based on his feelings and observations about a person's behavior or attitude;
- b. The purpose of Feedback is to help develop a person's personality for his or her own good;
- c. The feedback given is very useful for someone to find out whether his behavior (when he communicates) has really been effective in achieving his goals or even disrupting efforts in achieving the desired goals.

2. Feedback Forms

The following are forms of feedback, including:

- a. *External Feedback*
Good feedback is received directly by the communicator from the communicant.
- b. *Internal Feedback*
The feedback received by the communicator is not from the communicant but comes from the message itself or from the communicator itself.
- c. *Direct Feedback or Immediate Feedback*
Direct feedback in a communication, the communicant moves one of his limbs.
- d. *Indirect Feedback or Delayed Feedback*
In the form of letters to newspaper editors, radio broadcasters, etc. This feedback takes time.
- e. *Inferential Feedback*
The feedback received in mass communication which is concluded by the communicator, although indirectly, is quite relevant to the message conveyed.
- f. *Zero Feedback*

This means that the communication conveyed by the communicator to the communicant even though the communicant conveys the feedback is not understood by the communicator.

g. *Neutral Feedback*

Neutral feedback means that the information received back by the communicator is irrelevant to the message originally conveyed.

h. *Positive Feedback*

The communication conveyed by the communicator to the communicant gets a positive response, for example by accepting the message conveyed.

i. *Negative Feedback*

The communication delivered by the communicator is challenged by the communicant.

3. Terms of Giving Feedback

a. Descriptive, not evaluative

Feedback evaluative ones tend to upset the recipient's emotions rather than provide ideas that can be thought out and acted upon. By giving descriptive feedback, we are also actually avoiding labeling that can make the recipient refuse because it was insulted, not because our idea was bad.

For example :

“What you are talking about is inconsequential!”

“What you say is different from the purpose of this discussion.”

b. Specific

Provide feedback with specific reasons.

“This group's performance is terrible!”

“This group produced 10 units, while another group produced 15.”

c. Appreciative

Sometimes we only focus on the things that need to be improved, but forget the things that need to be maintained. Also express positive things so that people's performance survives and improves.

d. As soon as possible

Don't delay. Feedback given too long will make people late to improve themselves. Although it is recommended as soon as possible, but also pay attention to the emotional state of the recipient.

e. Before giving feedback, you can also ask for clarification

Sometimes we need to ask for clarification before submitting feedback so that the feedback we give can be accurate.

For example, “You did that with the intention of...., is that right what I caught? Well, I think...”

f. Use the correct person substitute language

Proper pronouns provide clarity about who is giving feedback. Namely: “I think....”

However, if there is a group agreement, then say "In our opinion..."

g. Ask for clarification after giving Feedback

“Is my input easy to understand?”

h. Give alternative solutions

Feedback it is delivered for mutual progress and is not meant to test or test anyone let alone make you look great. Therefore, if you know there are alternative solutions, then convey them clearly and openly.

4. Terms of Receiving Feedback

a. Listen actively.

Use active listening techniques. Listen without prejudice, follow while marking, in particular, things that you think are not clear/too general. Ask things that are not clear.

Do not immediately answer if you do not understand correctly. Just ask about the things you find while listening is active.

b. Don't be defensive.

There's no point being defensive. You could be wrong, so instead of wasting valuable input. Listen and be open.

c. Thank you.

Understand that people give feedback with effort and intent on your progress. So, appreciate their efforts, thank you.

5. Feedback Benefits

The benefits of feedback are:

a. Improve the performance.

b. It can also improve communication with other people.

C. ORGANIZATIONAL REWARD SYSTEM

Rewards is an exchange (award) given by a company or service that is given an award, which is broadly divided into two categories, namely: (a) salary, benefits, vacation; (b) promotions and positions, bonuses, promotions, symbols (stars) and attractive assignments.

An effective reward system must provide employees with both financial and non-financial rewards. Managers must use the organizational reward system as effectively as possible, so that employees can be motivated and work productively.

There are three important dimensions that underlie the success of employee performance, namely (1) the value of the rewards offered; (2) rewards based on productivity; and (3) employees can directly affect their performance and productivity through their efforts.

An effective system for providing rewards to employees must: (a) meet the needs of employees; (b) compared to rewards given by other companies; (c) distributed fairly and fairly; (d) can be provided in various forms; (e) associated with achievement.

1. AWARD CATEGORIES

There are 2 categories of reward systems, including:

a. Intrinsic Reward System

According to Schuster (1985), the intrinsic reward system contains rewards that come from the individual's response to the work itself, which comes from transactions between an individual and his duties without the participation of third parties. Intrinsic rewards are determined by individuals in their interactions with their work. For example, intrinsic rewards can be a sense of responsibility, a sense of challenge, a sense of superiority, a sense of control, a sense of participation, and so on. Management must design work in such a way that intrinsic rewards can be achieved by employees who fulfill them.

b. Extrinsic Reward System

Extrinsic rewards according to Schuster (1985) and Byars and Rue (1997), are compensation that is directly delivered and controlled by the organization (third party) and is more visible (easily seen). The extrinsic reward system refers to all rewards outside the work itself. Thus, the extrinsic reward system includes both financial and non-financial rewards given by the organization in its efforts to respond to employee performance, both in quality and quantity.

Although intrinsic and extrinsic rewards are different, they are closely related. Intrinsic and extrinsic rewards; financial and non-financial, jointly interact to form part of a single reward system (not independent). For example, employees who receive extrinsic rewards in the form of an increase in wages, for example, will immediately feel a sense of inner satisfaction, namely being able to complete a job well. The employee's inner satisfaction is an intrinsic

reward, namely the employee concerned interprets that the increase in wages is a sign of doing a good job. The following are examples of intrinsic and extrinsic rewards

2. RELATIONSHIP BETWEEN REWARDS AND PERFORMANCE

Basically the relationship between performance and rewards is not only desired at the organizational level, but also at the individual level. The theory underlying the performance-reward relationship, is that employees will be motivated to achieve high performance if they believe that high motivation will result in the rewards they desire.

Therefore, organizations need to link formal rewards, such as leave allowances, insurance programs, holiday allowances with performance. That is, the amount of benefits that will be received by employees is determined by the performance achieved by the employee, not determined by the organization or aspects of seniority.

In order for the relationship between performance-reward to be effective, several conditions are needed, such as performance must be measured accurately, there must be a serious discipline linking performance with rewards.

Based on the results of the study, it shows that if the amount of wages depends on performance, then the performance of individuals and groups will consistently be higher than if there is no dependence on these wages. Vroom's expectancy theory states the importance of linking performance with wages to motivate employee performance. The Expectation Model has three main components, namely:

- a. Hope itself. It is an individual's perception of the likelihood that their efforts will result in job completion or performance;
- b. Instrumentality, namely the employee's perception of the possibility that the resulting performance will result in an award (eg wages or awards);
- c. Valence, which is the employee's subjective value of the award he will receive.

3. The main objective of the award program

The main objectives of the award program that need to be known include:

- a. Attract qualified people to join the organization;
- b. Keeping employees coming to work;
- c. Motivate employees to achieve high levels of performance.

Positive Reinforcement (Positive Reinforcement)

Reinforcement is an important conditioning principle. Managers often use positive reinforcement to influence behavior. A positive reinforcement is a stimulus that, when added to a situation, strengthens the likelihood of a behavioral response. Therefore, if positive reinforcement has value (desirable) for someone.

Reinforcement theory states that behavior is influenced by its consequences and by controlling the consequences we can influence behavior. Desired behavior is reinforced through rewards, while unwanted behavior can be eliminated through punishment.

Positive reinforcements reinforcement based on the principle that the frequency of response increases because it is followed by a supportive stimulus (rewarding). Forms of positive reinforcement are in the form of gifts (candy, gifts, food, etc.), behavior (smiles, nodding head in agreement, clapping, thumbs up), or awards (A grade, 1st place, etc.). Positive reinforcement is something that is added or gained.

This means that there is a positive response when an individual shows the required positive behavior. For example, praising students for arriving early. This will increase the likelihood that the behavior will occur again. Reward is positive to reinforce or stimulate, but not necessarily so, if and only if the student's behavior improves, the reward can be said to be a positive encouragement. Positive reinforcement stimulates behavior.

There are four types of reinforcement, namely: (a) positive reinforcement, namely reinforcement that is carried out towards positive performance; (b) negative reinforcement (negative reinforcement), namely reinforcement that is carried out because it reduces or stops a situation that is not liked. For example, trying to finish work quickly because you can't stand to hear your boss nagging constantly; (c) extinction, namely not confirming a behavior, so that the behavior subsides or becomes extinct altogether. This is done to reduce unexpected behavior; (d) punishment, namely the unpleasant consequences of certain behavioral responses

5. Conclusion

Based on the descriptions above, in this chapter several main conclusions can be drawn as follows:

We already know what goals are, and it can be concluded that organizational goals are statements about conditions or situations that do not exist now but are to be achieved in the future through organizational activities. Our group concludes in the contents of this paper that goals are very important in any company or organization, because with a goal, the organization has a benchmark for what it wants to achieve or be targeted according to the goal itself.

Organizations cannot exist without a purpose, and vice versa, there is no purpose if there is no organization.

The objective functions include:

- A. Guidelines for activities
- B. Source of Legitimacy
- C. Implementation Standard
- D. Motivation Standard
- E. Rational Basis of Organizing

Management by objectives or known as MBO (Management by objective) emphasizes the importance of the role of goals in effective planning, by establishing procedures for achieving both formal and informal, first by setting goals to be achieved, followed by activities to be carried out until completion, then a review of the work that has been carried out is carried out.

Knowing the purpose of feedback (feedback) in the organization, The feedback provided is very useful for someone to find out whether his behavior (when he communicates) has really been effective in achieving his goals or even disrupting efforts in achieving the desired goals. The various forms of feedback (feedback), including:

- A. *External Feedback*
- B. *Internal Feedback*
- C. *Direct Feedback or Immediate Feedback*
- D. *Indirect Feedback or Delayed Feedback*
- E. *Inferential Feedback*
- F. *Zero Feedback*
- G. *Neutral Feedback*
- H. *Positive Feedback*
- I. *Negative Feedback*

There are three important dimensions that underlie the success of employee performance, namely (1) the value of the rewards offered; (2) rewards based on productivity; and (3) employees can directly affect their performance and productivity through their efforts.

Organizational rewards can be classified as extrinsic and intrinsic. Extrinsic rewards include salaries, benefits, promotions and certain types of interpersonal rewards. Intrinsic rewards can include such things as feelings of accomplishment, achievement of autonomy and personal growth. Both intrinsic and extrinsic rewards can be used to motivate job performance. For this to happen, several conditions must exist: the reward must be of value to the employee and must be linked to the level of job performance to be motivated.

Positive reinforcement is the process of forming behavior that is closer to the expected behavior. This is supported by the existence of rewards to inspire someone to do better things in the future. In this theory the words that motivate someone are positive words, so it is hoped that the person who gives the stimulus also gets a good response. This positive thing stimulates you to do it over and over again and get better.

REFERENCE

- Bushi, F. (2021). An Overview of Motivation Theories: The Impact of Employee Motivation on Achieving Organizational Goals. *Quality-Access to Success*, 22(183).
- Handoko, T Hani, (2009). *Management*. Yogyakarta: Edition 2. BPF.
- Ivancevich, John M (2006). *Organizational Behavior and Management*. Jakarta: Erlangga, 2006), Volume 1, Edition 7.
- Katou, A. (2021). Employee high-performance work systems-experience attributions of well-being and exploitation: a multilevel study of Greek workplaces. *Employee Relations: The International Journal*.
- Ogochukwu, O. E., Amah, E., & Okocha, B. F. (2022). Management by Objective and Organizational Productivity: A Literature Review. *South Asian Res J Bus Manag*, 4(3), 99-113.
- Siregar, H., Muda, I., & Fachrudin, K. A. (2019, January). The Impact of Locus of Control, Ethics Audit, Time Pressure, and Commitment to Deviant Behavior in Audit at Foreign Affiliated Public Accountants in Medan, Indonesia. In *1st Aceh Global Conference (AGC 2018)*. Atlantis Press.
- Soto Setzke, D., Riasanow, T., Böhm, M., & Krcmar, H. (2021). Pathways to digital service innovation: The role of digital transformation strategies in established organizations. *Information Systems Frontiers*, 1-21.

CHAPTER 9

Market-Based Bonus Schemes to Remunerate Managers in Terms of Market Value

Evita Nora Manik¹, Soraya Pramita², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹Correspondent Author Email: manikevita@gmail.com

ABSTRACT

The main purpose of this paper is to investigate schemes of market-based bonus to remunerates managers. This research is based on the principal-agent theory and this research conduct literature review regarding market-based bonus schemes to remunerate managers in terms of market review. Research literatures shows positive and negative side of the managers equity-based schemes. Prior to the application of equity-based schemes, it is needed to consider individual performance rather than corporate performance. This research is solely literature review and have not conducted interview to know reasonings of market-based remuneration before the compensation issued to managers. This research can be used as considerations and reference for applying market-bonus schemes to remunerate firm's managers. This research adds knowledge of literature comparations regarding topic of equity-based compensation for managers.

Keywords : Market-Based Bonus, Equity-Based Compensation, Agency Theory.

1. INTRODUCTION

An important part of the general compensation package is the bonus. Companies can use compensation policies through bonuses that function to adjust accounting procedures related to company profits. Bonus is one of the popular compensation policies, because it concerns the welfare of executives in internal companies. Related to this problem, accounting researchers have long studied managerial behavior when faced with choices among the best accounting alternatives related to bonus schemes in accounting decisions.

A profit-based compensation plan suggests an efficient contract, but an efficient manager contract motivates managers to maximize firm value. Therefore, compensation plans that directly relate managers' compensation to their impact on the firm's market value appear to be more efficient than profit-based plans. There are two basic types of compensation plans to reward managers' performance as measured by accounting numbers, namely bonus plans and performance plans. Performance separation is a motivating factor for accounting profit-based compensation plans (Hanum and Muda, 2020). Bonus planning provides managers with incentives to maximize firm value. The performance index in the bonus calculation must be correlated with the effect of the manager's actions on firm value. Therefore, the greater the correlation between earnings and the effect of a particular manager's actions on firm value, the more likely it is that profit-based bonus plans are used to reward managers.

Many empirical studies have examined the effect of bonus plans. The parameters of the bonus plan are determined so that the bonus is awarded almost annually (Smith and Watts, 1982). Warren Buffet also explains in Cunningham (2001) that it is possible to use stock options to build a managerial culture that will encourage owner-like thinking to managers. However, the alignment will not be perfect. Buffett also argues that performance would be better used as a basis for deciding executive pay. Executive performance should be measured by profitability, the net capital employed by the relevant business or the income retained by it (Lubis et al., 2018). In the case of executive payouts using stock options, they should be tied to individual performance, not company performance, and priced based on business value. In addition, stock options should not only be considered as a compensation scheme, as managers can buy shares if they are given a cash bonus. If yes, then the manager really is walking in the owner's shoes.

There are certain situations in which anticipating future wage changes affect the manager's perception that the value of his human capital changes more than his wealth changes. The general phenomenon of the wage revision process is at least one of the survival substances of modern large enterprises.

Purpose of the pay scheme. What is the organization trying to achieve from the award scheme? The following are among the most important goals are to support organizational goals by aligning employee goals with these, to ensure that the organization is able to recruit and retain a sufficient number of employees with the right skills, to motivate employees, to align the risk preferences of managers and employees with the preferences of the organization, to comply with legal regulations, to be ethical, to be affordable and easy to manage. In this article we will explain how companies approach executive compensation and how some have used it to improve performance, sharing insights from our research.

2. LITERATURE REVIEW

Fama (1980) conduct research of Agency Problems and the Theory of the Firm. The research show that separation of security ownership and control, especially in large corporations, is an efficient form for organization economically. There are certain situations that anticipated future wage changes affected manager perception that his human capital value changes more than his wealth

changes. The general phenomenon regarding wage revision process is at least one of the survival substances of modern big corporation. It is characterized by diffuse security ownership and separation between security ownership and control, as a viable form of economic organization.

Jensen and Meckling (1976) define the concept of agency costs, show its relationship to the 'separation and control' issue. They also investigate the nature of the agency costs generated by the existence of debt and outside equity, demonstrate who bears these costs and why, and investigate the Pareto optimality of their existence. They define that agency relationship is a contract under which one or more persons (the **principal(s)**) engage another person (the **agent**) to perform some service on their behalf which involves delegating some decision-making authority to the agent.

Jensen and Meckling (1976) argue that if the relationship objective are for utility maximizers, there is a chance that the agent will not always act in a best way according to principal's interest. The gap between those interest of principal and act done by agent can be reduced by two ways. The first one is by establishing appropriate incentives for the agents. The latter is by incurring monitoring costs designed to limit the aberrant activities of the agents. Both cost arouse from those two activity is called as agency cost. In some situations, additional payment called bonding costs might occurred with purpose to guarantee that agents will not take certain actions that would give any harmful situation to the principal. For example, there would be compensation to principal if agent does take such actions.

3. METHODS

This research is a qualitative method and we conducted study on literatures related to equity-based compensation. This study provides a theoretical overview regarding Market-Based Bonus Schemes to Remunerate Managers in Terms of Market Value. This paper aims to review Market-Based Bonus Schemes used to give compensation for Managers and consider the relationship between the market-based compensation with firm's value, performance, and managers' behaviour. Methodology used in this research is literature study and we conducted analysis of positive and negative side of Market-Based Bonus Schemes in the prior literatures.

4. RESULT AND DISCUSSION

4.1. Result

Cunningham (2001) explain that according to Warren Buffet, the best managers have the owner way of thinking in making business decisions, or it can be said that managers have shareholder interests at heart. However, managers sometimes have conflict of interest with shareholders. There are several ways to ease those conflict, namely communication between managers and shareholder, managers selection process and controlling managers' process.

Warren Buffet also explained in the Cunningham (2001) that it is possible to use stock options to build managerial culture by which it will encourage owner-like thinking to managers. However, the alignment would not be perfect. Buffett also argue that performance would be better used as a basis to decide executive payment. Executive performance should be measured by profitability, net-of capital employed relevant business or earnings retained by it. In case executive payment using stock options, they should be related to individual performance, rather than corporate performance, and priced based on business value (Elisabet et al., 2018). Moreover, stock options should not simply be considered as compensation schemes, since managers can purchase the stock if they were given cash bonus. If they do, then the manager is truly walk on owner's shoe.

In accordance to above arguments, research regarding market-based bonus schemes has been widely conducted. There are researches that support market-based bonus or compensation system. Several research is conducted to test relationship between the market-based bonus with firms' performance. However, some research also show problem regarding the down side of market-based compensation schemes.

Kumar (1997) conduct research of factors associated with the use of long-term earnings and market-based compensation plans. Based on that research, it is found that firms using long-term plans has tend to be larger, have diffuse ownership and more long-term growth compared to firms that solely using market-based plans. The research evidence is consistent with long-term plans serving as incentive alignment mechanisms.

Bahaji (2011) study behavioral approach regarding incentives from stock option grants. The models in Bahaji (2011) research show that when the probability-weighting feature applies, the subjective value can overstate option which has risk-neutral value. Assuming that company and employee efficiently bargain over compensation components, incentives would be maximized since the strike prices was set around the stock price at the inception date. Loss-averse employees who were not get probability weighting, or with low degrees of probability weighting, if they get options at high exercise price would rather accept compensation reduction than accept deep discount options or restricted shares. It is also explained that loss-averse executives who are facing the same probabilities of options may not prefer an increase in the variance of company stock price return. Executives who is subject to probability weighting, compared to risk-neutral executive, would be more prompted to act in order to increase the firm's assets volatility.

Deschenes, et. Al. (2014) research show that total remuneration of top management is directly related with board-member remuneration and the board average number of director-tenure periods (years). The research found that stock-based ratio of total top-management remuneration is positively affected by independent director's percentage, board directors' remuneration, the ratio of stock-based remuneration of directors to their total remuneration and the average tenure years of the board of directors.

Kwon (2012) is showing sensitivity of executive bonus compensation to earnings and returns in High-Tech Firms. It is shown that the sensitivity of executive bonus compensation to market-adjusted returns is weaker and more symmetric for High-Tech firms than for Non-High-Tech Firms. Moreover, sensitivity of executive equity-based compensation to market-adjusted returns is significantly negative for High-Tech Firms when it is compared to Non-High-Tech Firms when bad earnings news is announced.

Dorata, et. al. (2008) found that for merging firms CEO compensation is positively related with firm size. Result for non-merging firms is that there is indication that CEO compensation is positively associated with firm size and firm performance.

Douka and Zhang (2013) conducted study of equity pricing and compensation in bank merger. The study found that high valued bidders prefer stock than cash in mergers and acquisition and use target market price as the relative pricing of mergers and acquisitions. Other than that, high valued bidders also tend to reward their top managers of with high increase of compensation after mergers done.

Guo, et.al. (2006) study the stock compensation and firm performance in Taiwan. The study found evidences of the research located in Taiwan that there are positive associations between amount of

stock bonuses and firms' operating performance. They also found that larger Taiwanese firm or high growth opportunity firms in Taiwan tend to adopt stock bonus.

Fabrizi (2013) is investigate the economic determinants and the effects of the executives' equity compensation on firm value. The investigation also shows that when there is increment in firm's marketing intensity, the equity incentives also significantly increase. The equity incentives are also positively related to shareholder value and firm value. The equity incentives also have positive effect on firm value and it is partially mediated by marketing investments.

D'Mello and Miranda (2014) investigate impact of introducing compensation structure of CEO, which is equity-based compensation, as a means of top executives' payments on policy decisions. The research compared firm's stock and operating performance in the period of equity-based compensation the reversal period, and conclude that awarding stock options and restricted shares to executives is not associated with firm performance incremental. However, the firms compensate CEOs with equity-based bonus after superior prior performance. Firms that tend to have higher unsystematic and risk in the equity-based compensation period argue that equity-based compensation has influence CEOs' risk-taking behavior and also reduces agency costs that come from managerial risk aversion. Lastly, the research show that leverage and payout ratios are similar in both periods implying that CEOs' compensation schemes have no effect to firms' financing policy.

Enache and Kim (2019) investigate managers' stock-based compensation and the relation to disclosures of high proprietary cost information. The research shows there is no significant relationship between those variables. It is also found that managers who has equity-based compensation (in the total pay) give less disclosures of high proprietary cost information when they have a stronger interest to keep such information. The situation especially occurred when their firms' product development is in early stage, when most of the firms' board consists of directors with limited technology knowledge, and when firms lead the industry's market share.

Daily (2002) gives arguments regarding problem with equity compensation. The study was conducted with more than five decades periods and included 229 studies, also include nearly 1,000,000 equity/performance relationships. The result is there is no evidence of a systematic relationship between equity and firm performance. In contrast, option-based compensation should be eliminated from and such existing practices need a serious reexamination. There are three recommendations in the research to replace stock options for compensating executive or directors. Firstly, index executive options which is indexing option strike prices to the overall market. When the stock price significantly decreased, the options are recalled and new options with lower strike prices are granted. And options also granted when the stock price is increased, with a consideration that the rewards are for their performance, not the stock price performance. Secondly, repricing options which is a valid option under conditions that it is sensible awards for a replacement managers or new team, and the options are indexed to the overall market. Lastly, discontinue equity-based director pay because directors compensated with equity has not yielded anticipated firm performance results.

Henry (2010) supports the research by stated that equity compensation for executives is not the answer to maximize firm value. On the other hand, it appears to be executive's way to maximize their personal wealth. With the financial crisis that affected firms' shareholders, compensation committees need to consider inherent problems of executive compensation as a crucial issue (Silalahi et al., 2018). It may be solved by creating an helpful environment in which not only the executives but all stakeholders are considered that may help to alleviate some of the ill will that has permeated the market.

4.2. DISCUSSION

Based on literature research as presented above, we can see how managers or CEO act as agent and how shareholder as owner of firms has consider compensation as a solution to agency problem. This is inline with Theory of Firms by Jensen and Meckling (1976) that managers of large public firms seem to behave in a risk averse way, and it is opposite of the equity holder's interest. One solution that Jensen and Meckling suggest to this condition is to establish incentive compensation systems for the manager or give stock options compensation.

Several research show pro and contra subject to the stock options compensation. Some show positive sign that market-based bonus is a good consideration to decrease agency conflict. However, in contrary, some researches also show negative sign that compensating managers with market-based bonus is not a best option. Those prior research is briefly concluded as follows:

Table 1. Several research the stock options compensation

Research Topics	Findings	Conclusions
Kumar (1997): Factors associated with the use of long-term earnings and market-based compensation plans.	Firms using long-term plans, compared to firms that solely using market-based plans, tend to be larger, have diffuse ownership and more long-term growth.	Negative
Bahaji (2011): Behavioral approach regarding incentives from stock option grants.	If loss-averse executives get options at high exercise price of options, they may not prefer an increase in the variance of company stock price return. Executives who is subject to probability weighting, compared to risk-neutral executive, would be more prompted to act in order to increase the firm's assets volatility.	Negative Positive
Kwon (2012): sensitivity of executive bonus compensation to earnings and returns in High-Tech Firms.	Sensitivity of executive bonus compensation to market-adjusted returns is weaker and more symmetric for High-Tech firms than for Non-High-Tech Firms. Sensitivity of executive equity-based compensation to market-adjusted returns is significantly negative for High-Tech Firms when it is compared to Non-High-Tech Firms when bad earnings news is announced.	Negative Negative
Dorata, et. al. (2008): CEO duality and compensation in the market for corporate control.	CEO compensation is positively related with firm size and firm performance.	Positive
Douka and Zhang (2013): equity pricing and compensation in bank merger.	High valued bidders prefer stock than cash in mergers and acquisition and use target market price as the relative pricing of mergers and acquisitions. Other than that, high valued bidders	Positive

	also tend to reward their top managers of with high increase of compensation after mergers done.	
Guo, et.al. (2006): stock compensation and firm performance in Taiwan.	Amount of stock bonuses positively related with firms' operating performance. They also found that larger Taiwanese firm or high growth opportunity firms in Taiwan tend to adopt stock bonus.	Positive Positive
Fabrizi (2013): Economic determinants and the effects of the executives' equity compensation on firm value.	The equity incentives positively related to shareholder value and firm value.	Positive
D'Mello and Miranda (2014) Introduction of Equity-Based Compensation and Impact on Firm Policies	Equity-based compensation which is stock options and restricted shares to executives is not associated with increase of firm performance. Equity-based compensation has influence CEOs' risk-taking behavior and also reduces agency costs that come from managerial risk aversion. CEOs' compensation schemes have no effect to firms' financing policy.	Negative Positive Negative
Enache and Kim (2019): managers' stock-based compensation and the relation to disclosures of high proprietary cost information	No significant relationship between stock-based compensation and disclosures of high proprietary cost information. Managers who have equity-based compensation (in the total pay) give less disclosures of high proprietary cost information when they have a stronger interest to keep such information.	Negative Negative
Henry (2010): Does equity compensation induce executives to maximize firm value or their own personal wealth?	Equity compensation for executives is not the answer to maximize firm value but it is their way to maximize personal wealth.	Negative

5. CONCLUSION

Initially, the compensation is one of the answers to solve agency problem, which can be used by owner to influence managers fulfill owner's objective in the firms, such as increasing firms' performance. Research literatures shows positive and negative side of the managers equity-based schemes. Thus, we conclude that prior to the application of equity-based schemes, it is needed to review certain consideration. Referring explanation of Warren Buffet in the Cunningham (2001), it is possible to use stock options to encourage managers having owner way of thinking. However, individual performance would be better used as consideration of the compensation basis instead of

corporate performance. Moreover, stock options should not simply be considered as compensation schemes, because managers can actually purchase the stock from their cash bonus.

REFERENCE

- Abraham, E., & Singh, G. (2016). Does CEO duality give more influence over executive pay to the majority or minority shareholder? (A survey of Brazil). *Corporate Governance: The International Journal of Business in Society*, 16(1), 96–115.
- Arbaugh, J. B., Cox, L. W., & Camp, S. M. (2004). Employee equity, incentive compensation, and growth in entrepreneurial firms. *New England Journal of Entrepreneurship*, 7(1), 15–25.
- Bahaji, H. (2011). Incentives from stock option grants: a behavioral approach. *Review of Accounting and Finance*, 10(3), 200–227.
- Canarella, G., & Gasparyan, A. (2008). New insights into executive compensation and firm performance. *Managerial Finance*, 34(8), 537–554.
- D’Mello, R., & Miranda, M. (2014). Introduction of Equity-Based Compensation and Impact on Firm Policies. *Corporate Governance in the US and Global Settings*, 153–192.
- Daily, C. M., & Dalton, D. R. (2002). The Problem With Equity Compensation. *Journal of Business Strategy*, 23(4), 28–30.
- Deschenes, S., Boubacar, H., Rojas, M., & Morris, T. (2015). Is top-management remuneration influenced by board characteristics? *International Journal of Accounting & Information Management*, 23(1), 60–79.
- Dey’-Tortella, B., Gomez-Mejía, L. R., de Castro, J. O., & Wiseman, R. M. (2005). Incentive Alignment or Perverse Incentives? A Behavioral View of Stock Options. *Management Research: Journal of the Iberoamerican Academy of Management*, 3(2), 109–120.
- Dorata, N. T., & Petra, S. T. (2008). CEO duality and compensation in the market for corporate control. *Managerial Finance*, 34(5), 342–353.
- Doukas, J. A., & Zhang, W. (2015). Do equity mispricing and management compensation incentives drive bank mergers? *Review of Behavioural Finance*, 7(1), 2–41.
- Elisabeth, D.; Simanjuntak, A.; and Ginting, S. (2018). Corporate Social Responsibility, Auditor Opinion, Financial Distress Impact to Auditor Switching for Banking Companies in Indonesia Stock Exchange for Period of 2014 to 2017. In *Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES*, ISBN 978-989-758-432-9, pages 991-994. DOI: 10.5220/0009499909910994. <https://www.scitepress.org/PublicationsDetail.aspx?ID=/ZQ4uUFFTPQ=&t=1>
- Elsayed, N., & Elbardan, H. (2018). Investigating the associations between executive compensation and firm performance. *Journal of Applied Accounting Research*, 19(2), 245–270.
- Enache, L., & Kim, J. B. (2019). Managers’ stock-based compensation and disclosures of high proprietary cost information. *Pacific Accounting Review*, 32(1), 96–124. doi:10.1108/par-10-2018-0078
- Eugene F. Fama (1980). Agency Problems and the Theory of the Firm. *Journal of Political Economy*, 88(2), 288–307. doi:10.2307/1837292
- Fabrizi, M. (2014). Chief marketing officer’s equity incentives: economic determinants and effects on shareholder value. *European Journal of Marketing*, 48(9/10), 1757–1781.
- Fosberg, R. H., & James, J. F. (1995). Bond Rating Changes and CEO Compensation. *Managerial Finance*, 21(2), 12–23.
- Guo, W., & Shiah-Hou, S. (2006). Stock bonus compensation and firm performance in Taiwan. *Managerial Finance*, 32(11), 862–885.
- Hanum, Z., & Muda, I. (2020). Effect of Tax Planning on Profit Management in Registered Food and Beverage Sub Sector Manufacturing Companies On the Indonesia Stock Exchange. *Junior Scientific Researcher*, 6(1), 48-57.

- https://www.jsrpublishing.com/userfiles/files/archive_pages/97/Article._Zulia_Hanum_Vol.V_I_No.1_2020.pdf
- Henry, T. F. (2010). Does equity compensation induce executives to maximize firm value or their own personal wealth? *Ethics, Equity, and Regulation*, 111–139.
- Hoi, C., & Robin, A. (2004). The design of incentive compensation for directors. *Corporate Governance: The International Journal of Business in Society*, 4(3), 47–53.
- Jensen, M.C. and Meckling, W.H. (1976), “Theory of the firm”, *Journal of Financial Economics*, Vol. 3 No. 4, pp. 305-360.
- Jouber, H., & Fakhfakh, H. (2012). Pay for luck: new evidences from the institutional determinants of CEOs’ compensation. *International Journal of Law and Management*, 54(6), 485–507.
- Kumar, Krishna R. (1997). Factors Associated with the Use of Long-Term Earnings and Market-Based Compensation Plans. *Managerial Finance*, 23(5), 40–55.
- Kwon, S. S. (2012). Symmetry in the Sensitivity of Executive Bonus Compensation to Earnings and Returns in High-technology Firms. *International Finance Review*, 127–172.
- Li, H., & Qian, Y. (2011). Outside CEO directors on compensation committees: whose side are they on? *Review of Accounting and Finance*, 10(2), 110–133.
- Li, H., Henry, D., & Wu, X. (2019). The effects of accounting conservatism on executive compensation. *International Journal of Managerial Finance*, 16(3), 393–411.
- Lord, R. A., Saito, Y., Nicholson, J. R., & Dugan, M. T. (2019). CEO compensation, portfolio holdings and strategic investments. *Journal of Financial Economic Policy*, 12(1), 137–160.
- Lubis, P.; Muda, I. and Erlina,. (2018). Analysis of the Factors Affecting the Capital Structure of a Manufacturing Company Listed on the Indonesian Stock Exchange in Moderation by Business Risk. In *Proceedings of the 7th International Conference on Multidisciplinary Research - Volume 1: ICMR*, ISBN 978-989-758-437-4, pages 570-577. DOI: 10.5220/0008890605700577.
- <https://www.scitepress.org/PublicationsDetail.aspx?ID=EX+DchZjbv0=&t=1>
- Murphy, K. J., & Zábojník, J. (2004). CEO Pay and Appointments: A Market-Based Explanation for Recent Trends. *American Economic Review*, 94(2), 192–196.
- Park, S., Song, S., & Lee, S. (2019). The influence of CEOs’ equity-based compensation on restaurant firms’ CSR initiatives. *International Journal of Contemporary Hospitality Management*, 31(9), 3664–3682.
- Petra, S. T., & Dorata, N. T. (2008). Corporate governance and chief executive officer compensation. *Corporate Governance: The International Journal of Business in Society*, 8(2), 141–152.
- Piekkola, H. (2005). Performance-related pay and firm performance in Finland. *International Journal of Manpower*, 26(7/8), 619–635.
- Silalahi, A. D., & Muda, I. (2020). The Effect of Financial Information On Investment Decisions Of Individual Investors In Indonesia Stock Exchange. *Junior Scientific Researcher*, 6(1), 41-47. https://www.jsrpublishing.com/userfiles/files/archive_pages/96/Article._Alistraja._JSR_Journal_Vol.VI_No.2_2020.pdf
- Velte, P., & Obermann, J. (2020). Compensation-related institutional investor activism – a literature review and integrated analysis of sustainability aspects. *Journal of Global Responsibility*, ahead-of-print(ahead-of-print).
- Victoravich, L. M., Xu, P., & Gan, H. (2012). Institutional ownership and executive compensation. *Managerial Finance*, 39(1), 28–46.
- Wang, D., & Wu, D. (2017). Equity incentive and risk taking: evidence from China. *Nankai Business Review International*, 8(1), 80–99.

CHAPTER 10

Two Perspectives (Efficiency Perspective and Opportunistic Perspective) adopted by Positive Accounting Theory Research

Donald J.R. Tobing ¹, Jonni William Panjaitan ², Iskandar Muda ³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹ Email: donaldj.t@gmail.com

ABSTRACT

Since positive accounting theory plays an increasingly important role in the economy. This paper discusses the implications of positive accounting, understanding, accounting theory, efficiency perspective (Ex Ante) and Opportunistic perspective (Ex post); and consistency between the two perspectives on the basis of financial position. This study uses a qualitative approach. The qualitative is an analytical method based on post-positivism philosophy, used to examine the condition of natural objects, where the researcher is the key instrument. The method used in this research is a case study literature research. Case study research is a research conducted intensively and in detail. Expenditures may be consistent with efficiency, as they aim to reflect the firm's value in the most accurate way. But it ignores the benefits that can be obtained from such capitalization. Capitalization can increase managers' opportunism, which means they have a wide range of managers' discretion.

Keywords : Opportunistic Perspective, Efficiency Perspective, Post-Positivism Philosophy

. Introduction

Accounting theory plays a very important role in any accounting approach. In general, there are three main approaches to applying accounting theory: a) the normative approach tells people what to do and what to do based on logical arguments; b) descriptive approach provides explanations and predictions based on empirical evidence or observations and c) critical approach evaluates accounting theory critically. Among all, positive accounting theory which is widely understood as agency theory is one of the most important accounting theories (Nurmadi et al., 2018). There are two perspectives for positive accounting theory, namely the efficiency perspective (Ex Ante) and the opportunistic perspective (Ex Post). On the one hand, the efficiency perspective interprets ways to reduce agency costs (Simanjuntak et al., 2018). On the other hand, the opportunistic perspective interprets ways to maximize agency benefits. This assignment focuses on explaining what positive accounting theory and other related theories are, and how to apply these theories in conceptual practice.

2. Literature Review

2.1. Definition and nature of Accounting Theory

Theory is the result of the crystallization of empirical phenomena, drawn from various studies, and at a conclusion that is universal, logical, consistent, predictive and objective. Theory will be useful if the formulation of the theory can be used as a tool to predict something that might happen in the future. Accounting theory can be formulated as an arrangement of concepts, definitions, and propositions that present a systematic picture of accounting phenomena, as well as explain the relationship between variables in the accounting structure, to be able to predict emerging phenomena. According to Vernon Kam (1936), theory is a comprehensive system, which includes basic assumptions, definitions, objectives, principles or standards, and procedures or methods. Therefore, theories are explanations, but not all explanations can be categorized as theories.

2.2. Positive Accounting Theory

Positive accounting emerged with the accounting studies produced in the late 1960s. This concept was organized as a school of thought by Ross Watts and Jerold Zimmerman. Positive Accounting Theory tries to make good predictions about real events and make their interpretations of accounting transactions. While normative theory will, in general, suggest what should be done, Positive Theory tries to clarify and predict activities, for example, which accounting transactions a company will choose how companies will respond to recently proposed accounting standards. The general aim is to understand and forecast accounting policy decisions across different companies. He sensed that the financial results were there. Under this theory, three hypotheses have been revealed:

1. Keeping everything else constant, managers of companies with reward plans are bound to choose accounting procedures that shift reported earnings from future periods to current time frames.
2. Keeping all other things constant, the greater the firm's debt/equity ratio, the more likely the firm's managers are to choose accounting procedures that shift reported earnings from future periods to the current time frame.
3. Keeping everything else constant, the larger the company, the more certain managers will choose accounting procedures that defer reported earnings from the current period to future periods.

In this regard, politicians have the power to influence the redistribution of organizational income through corporate tax methods, guidelines, benefits and so on. In addition, certain groups of voters have the driving force to allow “nationalization, confiscation, segregation or regulation of industry or companies”, which is thus believed to provide an incentive to politicians to propose such activities (Stigler, 1971).

Under PAT, companies need to strengthen their prospects for survival, so that they manage themselves effectively. Companies are seen as an aggregation of the deals they have made. With

respect to PAT, arguing that there must be proficiency, the company needs to minimize the costs associated with the contract. In the case of an unregulated economy, the promoter and the original shareholders have an incentive to contract to supply audited financial statements. This agreement is included in the articles of association and in the contract between the organization and its creditors (Watts, 1977). This leads to a decrease in agency costs. Continuing the discussion above, agency costs exist because of conflicts of interest between shareholders and managers, shareholders and bondholders. Managers have incentives to transfer wealth to themselves at the expense of shareholders and bondholders (Watts & Zimmerman, 1979). Bondholders and investors anticipate the behavior of managers and appropriately discount the cost of bonds or shares at issue. As a result, the manager of another company earns less for the stocks and bonds he sells than he earns if he can guarantee that he will continue to run as he did when he owned the company (that is, when there were no outside investors or bondholders). . .). Thus, in an unregulated economy, accounting procedures are constructed in such a way as to reduce contract agency costs. But because they vary between companies, accounting procedures also vary between companies, giving rise to diversity. There is a demand for the expected impact of accounting procedures on the well-being of managers and auditors through disclosure of claims. The auditor contracts with investors (and creditors) to screen the executives, and he can legally accept if he fails to report breaches of agreements in the company's articles of association or by-laws.

For this purpose, accounting theory was built. An accounting text (and theory) detailing how managers look to manipulate profits and the subsequent impact of such manipulation on investors and bondholders not only enhances managers' capacity to monitor those actions, but also provides auditors with ready-made opinions to use against the method in consulting with management (Watts & Zimmerman, 1979). In a regulated economy, citizens, civil servants, and legislators are motivated to harness the power of the state to improve themselves and to blend in for that reason. Financial accounting reports play a major role in this movement of wealth and are influenced both directly and by implication by political procedures. Government commissions often use the substance of financial statements in administrative procedures (tariff regulation, antitrust, and so on). This, thus, motivates boards to choose accounting procedures that either reduce the costs they incur or increase the profits they get due to the activities of controllers and government officials. Since public utilities have the motivating power to propose accounting procedures for the purpose of setting rates that increase the market value of firms, their opinion is helped if accounting standard-setting bodies order similar accounting procedures for financial reporting. The guidelines and regulations that resulted from government oversight of business increased the professional demands and demands of education for accounting theory. The justification demands for theory also extend to regulation. Continuing the discussion above, supporters and opponents of the extraordinary machinations law (or candidates before the administrative and regulatory councils) should provide their opinion for the positions they advocate. In this position incorporating changes in accounting procedures, accounting theory fills in as a valuable rationale (ie, justification) (LH, 1972). Controllers (politicians and administrators) are wise. However, they consider that theoretical validation has costs and advantages. The validity of an accounting theory will not be resolved if the costs to evaluate the validity of a hypothesis outweigh the benefits. Since the interest is in theories that have the direction of open intrigue, once such a basis has been given, the gain to the controller associated with discerning erroneous ideas in accounting theory may be very little. In fact, regardless of whether the theory is known to have legitimate fallacies, there may be a motivation for not understanding the ambiguity. That is, the current theory may have an incentive as a reason regardless of its plausible status. Market failure theory is essential for politicians to legitimize accounting regulatory procedures over private markets for accounting data. Politicians should not be “guilted” by “theoretic illusions” and may not be interested or reluctant (because of disincentives) to understand coherent ambiguity (Watts, RL, & Zimmerman, JL, 1986).

In an economic context, market failure is said to occur when the quantity or nature of goods shipped in an unregulated market conflict with what is indicated as the social optimal. Social ideals

are characterized as products that increase total social welfare and are achieved only if the costs of inputs and outputs equal their marginal social costs. In private markets, makers and buyers pursue each other's interests. In this way, it is argued, private market output varies from the social ideal at whatever point social costs and benefits differ from private expenditures and benefits (Leftwich, 1980). Thus, positive accounting theory will only help if it can provide rich expectations for certain significant phenomena. We argue that although some of the work in the zone of positive accounting theory did help anticipate the development of accounting regulations (Benston, 1969). This theory is mostly concerned about the three shared indicators of lobbying behavior as well, the choice of accounting method depends on the suspicion of self-serving managers' wealth maximization. Managers of firms making large profits and may mishandle monopoly power, presumably, may use a pile of accounting strategy decisions to reduce reported earnings. Their own reference to the disclosure of social responsibility and its relation to their underlying conflict is dark. None of the examinations used each of the three (shared) behavioral hypotheses. Most, in fact, only use political cost measures or hypotheses, and therefore they have to think about shaky testing of the original argument. Second, neither test takes the opportunity to look at management practices other than the selected disclosure variables that might be expected to exist if the self-serving income reduction methodology was accepted as theorized, in this way further weakening the test (Milne, 2002).

Now, consider three behavioral hypotheses. The intellectual precursor of positive accounting theory is the income smoothing hypothesis (Becker, G. M, DeGroot, M. H, 1964). According to this hypothesis, income smoothing is viewed as a function of rational human behavior with several assumptions: - a) organizational managers are utility maximizers b) the main reasons for market risk are variations in earnings and earnings uncertainty c) the main stimulus for stock value is the dividend payout ratio d) The value of a firm's stock is a major determinant of managers' utility (Beidleman, 1973; Watts, RL, & Zimmerman, JL, 1986). It basically assumes that the market is inefficient i.e. the market reacts based on the reported accounting numbers without considering the transparency of the procedures for generating these numbers. However, stock market price formation does not need to consider functional fixation to create smoothing incentives. It is enough for managers to believe that the market takes accounting numbers into account. A study conducted showed that 83 percent of Fortune 500 controllers disagreed with the notion of market efficiency (Mayer-Sommer , 1979). Managers, however , can turn their beliefs and predictions over to the standard setters, if they have the incentive to do so. With the help of this approach to control , it was found that managers do not consider market efficiency (O'Keefe, TB, & Soloman, S. Y, 1985).

In most of the cases other things held constant, the higher the uncertainty in the firm, the higher the incentive for managers to smooth earnings (Vivien Biette, Stephen Brown, David Ewers, Brian John, Stewart Manson, Dylan Thomas, Michael Turner, 1994) . On the other hand, positive accounting theory is based on the concept of market efficiency. Thus, the market captures an observable smoothing incentive. There are three underlying accounting approaches: - a) opportunistic behavior b) efficient contracting and information perspective (Holthausen & Verrecchia, 1990). According to opportunistic behavior, managers are wealth maximizers and try to maximize their own wealth which is directly proportional to their performance, the risk that arises for managers in case of company failure. So, managers have the option to choose the option that maximizes the firm's cash flow and firm value so that they get the maximum amount of incentives. When accounting choices have no direct effect, managers' incentives also emerge. So, other things being held constant, managers will choose the income-reducing accounting method if the political costs are high, and they will choose the income-increasing accounting method if the agency costs of debt and equity are high.

Most of the empirical studies are conducted on the basis of the opportunistic behavior hypothesis. The second in efficient contracts. According to efficient contracts, all contracts that lower agency costs strengthen earnings management. However, all contracts are considered efficient because they result in an increase in firm value. Empirically, it is difficult to distinguish between efficient contracting and the opportunistic behavior hypothesis. The last concept, namely

the information perspective, has emerged as a new concept. It considers income smoothing as an earnings management strategy. Since there is always an information asymmetry between managers and claim holders, this explains how the existence of policies to smooth out earnings can act in the best interests of shareholders (Dye RA, 1988). For example, it can increase a firm's potential shareholders' perception of firm value or by lowering their perception of bankruptcy risk (Trueman & Titman, 1988). The accounting method chosen reflects the manager's expectations regarding future cash flows. Several studies have also shown that the separation of ownership and control increases the likelihood of smooth behavior. Even though the owners control outside, they have direct access to the information. So, they do not rely on published information. Managers of companies with dispersed ownership will be more involved in the smoothing process to reduce information asymmetry. They will also be more involved to reduce systematic work risk and increase company value. The existence of incentive schemes with high and low limits creates conflicts between managers and shareholders. Thus, by leveling income, it helps managers in transferring wealth from shareholders to themselves (Kamin, 1975). Thus, it is empirically proven that income smoothing is directly proportional to management-controlled firms (Amihud & Mendelson, 1983; Kamin, 1975). However, some companies have not been able to correctly identify the relevance of the accounting structure (Hunt III, HG, & Hogler, RL, 1990).

In an examination of positive accounting theory, the authors examine the work of "marginalism" in accounting theory. Likewise, with the aid of the rule of law, the philosophies associated with free economic agreements came into focus in the accounting field at a recent date due to the push to isolate "facts" from "reality" as well as "positive" to "normative". " theory. Indeed, the notion of significant value in accounting is borrowed one of two from the origin of labor-based or utility-based. The latter, as the authors point out, decide on general estimates of product and work in maintenance "by their relative commitment to utility. buyer. In labour-based theory, interestingly, selective sourcing of significant value is advantageous. labor force". Following "value theory" to its current manifestation in marginalism. It is concluded that there are two main characteristics of the replicating theory in accounting thought (Tinker, Merino, & Neimark, 1982). They show differences in the initial aspects and subsequent changes in accounting. The early [aspect] was the emphasis on individualism (regardless of even if the sole proprietor or company became a legitimate "individual") which had offered to capture the question of merging classes of "people" and the role accountants played in class clashes. Subsequent accentuations in accounting it has always been an attempt to protect objectivity and freedom by avoiding "abstract" questions of significant value and limiting bookkeeping information to "objective" (factual & gift) market prices.

The final accent, in which accountants are exhibited as "unbiased and harmless historians," begins with the profession's desire "to deny accountants the obligation to form subjective expectations which, in so doing, influence choices about allotment of capital and disbursement of earnings between and within social class. Moreover, in the general sense, nations for equality have philosophical and mechanical consequences. Standard research in accounting "is dictated by a belief in apparent authenticity - the case that there exists a target universe of realism that continues to be independent of people and which will have the nature or substance of certain things that can be understood (Chua, 2005). From that presumption, he pursues so that people can be described in a targeted way free from social settings. Therefore, the appropriate learning model for standard scholars is the "hypothetical-deductive" or "logical" model, with its emphasis on innovative, all-encompassing associations.

2.3. Positive Accounting Theory and Agency Costs

Agency theory is one example of the failure of positive accounting theory. It stems from its reliance on preconceived notions of level-headed behavior that are in one sense narrow and in another broad and contradictory. Agency relationship can be defined as an agreement in which at least one person (principal) is connected with another person (agent) to run some administration for

their benefit which includes the appointment of some basic leadership positions for the agent. If the two sets in the relationship are utility maximizers, there is valid justification for accepting that the agent will not normally act to the greatest advantage of the principal. Competition in product and factor markets.

Will generally push costs toward less than the average cost of an action. Managers must then persuade their organizations to build effectiveness in order to increase their chances of survival. However, the disciplinary forces of product and factor markets are often more fragile in new activities and activities that involve large economic rents or semi-rents. In this case, the observations by the firm's insider control framework and the market for corporate control are increasingly significant (Jensen & Posner, 1996). Principals can limit *divergences* from their interests by setting appropriate incentives for agents and by incurring monitoring fees designed to limit agent activities (Jensen & Meckling, 1976).

Since the relationship between investors and managers of an organization is perfect for the meaning of a pure agency relationship, it should not be a nuisance to find that the problems associated with the "separation of ownership and control" in modern diffuse ownership of firms are personally connected with general agency problems. The issue of moving the "agent" to act as if he or she is enhancing the welfare of the "principal" is extensive. It exists in all associations and in every congenial deployment—at every level of the board in corporations, in colleges, in joint ventures, in cooperatives, in governmental organizations and authorities, in associations, and in relationships classified as agency relationships, for example, those who are normal in the performing arts and real estate market.

However, the amount of agency costs depends, among other things, on laws and customary law and human creativity in contracting. Borrower bankruptcy is otherwise identified by the agency costs of making the physical investment. Both legislation and deal progress that is critical to competition are the result of past processes in which there were strong incentives for people to limit agency costs. In addition, there is an accessible elective organizational structure, and opportunities to develop new ones. Agency fees also plague public companies, most likely limiting their capacity to issue outside equity. For example, equity issuance can weaken managerial incentives (by lowering the equity-debt proportion) or send a bad signal to outside investors (Bernanke & Gertler, 1986). The development of theories to clarify the structure that agency costs take on in each of these circumstances (where authoritative relationships contrast at all), and how and why they were conceived will encourage rich theories of organization that are currently lacking in the economics and social sciences (Jensen & Meckling, 1976). The manager's choices will include not only the benefits he gets from a refund, in addition, the utility generated by the various non-monetary parts of his pioneering practice, for example, the physical setting of the workplace, the attractive qualities of the workplace. staff, level of representative control, type and size of altruistic commitment, individual relationships ("fellowship", "respect, etc.)) of the different financial and non-financial gains are achieved when the small utility derived from one additional dollar of use (the net estimate of each beneficial effect) is equivalent to each non-monetary and equivalent to the negligible utility gained from the extra dollar after the cost of gaining influence (wealth).

The strength of "agency theory" as an accounting clarification and authoritative development is the ongoing and highly persuasive association of standard suspicion. Nowhere is the parallel between accounting and legal orders clearer than in market theory in determining the many legitimate ideas and offices of significant ideas so unavoidable in significant accounting standards research. All such affinity is crucial in two of them - the work that creates contracts and market play in agency-based accounting research, and more so on the fundamentals of neoclassical monetary economics for this area of examination and theory enhancement (Hunt III, HG, & Hogler, RL). , 1990). The agency connection will include the relevant agency costs if it is expected (as is generally seen) that both parties i.e. the agent and the principal seek to maximize their utility and the operator will not subsequently operate to the greatest advantage of the principal. Indeed, it is generally

inconceivable for either the principal or the agent at zero cost to guarantee that the agent will make ideal choices from the principal's perspective.

In most office relationships, principal and agent will incur positive oversight and custody costs (non-monetary as well as financial), and moreover there will be some difference between the agent's choice and choices that will enhance the principal's welfare. What is comparable to the decline in well-being experienced by principals due to these differences is also an office relationship burden, and we refer to this latter cost as "residual loss" (Jensen & Meckling, 1976).

When associated with an environment of authority, for example, a company, agency theory dispels the idea that association is an important element. On the other hand, most of the associations are just legitimate fiction that fills in as a liaison for many contractual relationships between people. Companies or private companies are basically one of a kind legal fiction that fills in as a liaison for connection contracts. Seen that way, it seems bad to try to identify what is "inside" the company from what is "outside." Undeniably there are only a large number of complex connections (eg contracts) between legitimate fiction (companies) and owners of employment, material and capital sources of information and output consumers. (Jensen & Meckling, 1976).

2.4. Efficiency and Opportunistic Perspectives based on Positive Accounting Theory

2.4.1. Definition and Meaning of Opportunism and Efficiency under Positive Accounting Theory

Sinha (2008) claims that the main goal of positive accounting theory is to focus on predicting and explaining the practice of companies that have high consensus in the accounting community. PAT is considered an important part of the development of accounting because it has contributed to financial accounting techniques, accounting methods (Demski J 1988). That is, it serves as a guide for decision makers in the company (managers, accountants, investors and so on). PAT has a close relationship with various costs related to internal management and external management including agency costs, compensation contracts, contract costs related to political costs and so on. These costs form the basis of an important hypothesis in PAT. In their paper, they use the term 'contract costs' to cover the various types of costs that result in the transaction form of an entity (Zimmerman & Ross 1990). The main objective from an efficiency perspective in PAT is to minimize agency costs produced by all parties associated with the company, which will contribute to the maximum profit for these stakeholders. These parties also include managers and employees except for external parties, cooperation partners (Holthausen R, 1990). Zimmerman and Ross have a more advanced view of this explanation. In all markets, each party seeks to limit the wealth that flows out of their own side and to get more wealth from the other. However, the opportunistic perspective states that managers tend to maximize their individual wealth by choosing certain accounting numbers that can be used to calculate their compensation and increase their wealth (Holthausen R, 1990). Apparently, the opportunistic perspective does not aim to increase the stakeholders and profits of the company, but the managers themselves. However, the reason why managers tend to operate opportunistically stems from three hypotheses concluded by Zimmerman and Ross (Zimmerman & Ross, 1990). They are the bonus plan hypothesis, the debt/equity hypothesis and the political hypothesis.

2.4.2. Arguments and Consistency between the two perspectives on the basis of financial position

Zimmerman and Ross (1989) demonstrate the assumption of Positive Accounting Theory (PAT) that accounting numbers are used to investigate the relationship between accounting numbers and stock prices. One article pointed out that accounting numbers are considered an integral part of contracts in companies. When managers choose accounting methods to be applied in a company, they will use efficiency or opportunism from their main goal (Chirstine and Zimmerman, 1994). While all accounting choices in the empirical view are based on various costs. Also, when investigating effective contracts, Emanuel W, Wong J and Wong N (2003) presented in the article which entities typically use accounting numbers and whether they follow accounting technology is seen as efficiency. On the other hand, the opportunistic perspective shows us several variables,

these variables are selected based on the opportunistic perspective. In other words, Zimmerman & Ross (1990) further explains that if managers are given complete discretion and facilities, then we can say it is inconsistent with the efficiency and interests of all shareholders and other stakeholders. When Zimmerman and Ross conducted their research, they used two sample groups, one of which was a group of surviving firms and the other a so-called non-random sample, in which it was clear that the surviving firms had a low rate of adopting an opportunistic perspective. From this view, it is clear that at the face level, efficiency and opportunistic perspectives are on the opposite side and efficiency leads to a successful way and opportunistic methods can not be considered as a viable way of accounting.

(1) Efficiency and Opportunistic Perspectives Are Inevitable

However, these two perspectives cannot be completely separated. Except for the earliest studies, most researchers agree that they have a positive relationship with each other and the influence between them cannot be easily removed. Zimmerman & Ross (1990) use Figures and Figures to explain where the boundaries of these two perspectives are, they use the concatenation of the two circles to explain that in fact, Ex Ant and Ex Post can be separated completely, leading to a rewrite of the contract. The company aims to eliminate the risk of manager opportunism. We can also see the opinion of Holthaus R (1989), it is difficult to distinguish the efficiency behavior of managers following accounting technology to strengthen the perspective of monitoring and opportunistic behavior of managers.

(2) Efficiency and Opportunism Can Affect Each Other

Another part of the efficiency argument and the opportunistic perspective is that the two perspectives under PAT can be presented to each other. Zimmerman and Ross explain that because of asymmetric information and expensive monitoring, all contracting parties think that expected managerial opportunism is rational (1990). This means that this kind of loss of value in the contract is acceptable. However, they also mention that all parties, especially their external parties, use price protection to reduce managerial opportunism. Under these circumstances, managers have incentives to reduce opportunism in their performance, As a result, opportunism is expected to be efficient. Then we can say they are consistent. Christine & Zimmerman, 1994). They say that it is important to decide that how to combine ex ant and ex post can bring a bright future in the accounting community (Zimmerman & Ross, 1990).

2.4.3. Efficiency and Opportunistic Perspectives Based on Other Theories

According to the research of Matinez R and Dacin M (1999), transaction cost theory aims to guide organizations to pursue efficient results. However, it is clear that TCE is not reliably reliable universal, when the decision maker makes the company's final decision. In contrast, institutional theory is concerned with how firms remain consistent with the institutional environment. Usually it is considered under a normative context. It supplies more organizational behavior and presents the phenomenon that many companies in the same area. Tend to use the same accounting method and this is called imperative legitimacy. However, this is considered an inefficient way of accounting. The author goes on to illustrate that companies that operate opportunistically stem from human nature, but the market will ultimately choose those who behave in this perspective. So if the company uses TCE completely on the basis of efficiency. In the end, the author's opinion is that the best way for all companies is to integrate TEC and institutional theory. (Martinez R and Dacin M, 1999).

2.4.4. Efficiency and Opportunistic Perspectives in Accounting Methods

Form previous literature reviews of positive accounting theory and other theories. It is clear that the stakeholder's goal is to maximize the profits of the company as a whole. As a result they can provide discretion to managers and contract with managers to achieve profit goals. However, when aligning the interests of the company with the personal interests of managers, all stakeholders, even debt holders will bear the risk of this policy. This manager may be playing with accounting numbers, we can get evidence from financial statements and methods manager-chosen accounting.

2.4.5. Overview (Empirical Research on Accounting Choices)

Fields T, Lys T and Vicent L (2001) organized their research and review based on three accounting choices, which were the main topics of previous research. The three types of accounting choices are agency costs, information asymmetry and externalities affecting non-contracting parties. How to increase profits and avoid agency costs is a matter of balance. When a company chooses agency costs as an accounting method, it means they choose an efficient accounting contract perspective. It also includes executive compensation agreements and debt agreements. However, for example, LIFO can reduce taxes by reducing the amount of revenue, whereas FIFO tends to increase reported earnings. The second method, information asymmetry, because of the lack of company information, all managers are more likely to use the self-interest method. Third, managers want to influence external parties.

3. Methods

This study uses a qualitative approach. The qualitative is an analytical method based on post-positivism philosophy, used to examine the condition of natural objects, where the researcher is the key instrument. The method used in this research is a case study literature research. Case study research is a research conducted intensively and in detail.

4. Analysis

4.1 Analysis of Accounting Methods

To be consistent with the literature review, Zimmerman and Christine (1994) explain that in most companies, the efficiency perspective is more important than the opportunistic perspective. However, they assume that the method of increasing income is used to satisfy managers' self-interest, because this method can increase the present value of their compensation. However, when stakeholders control for the effects and extent of managers' opportunism, they may have problems evaluating and estimating opportunism. Malmquist and David (1989) claim that the success . method. Cost is more opportunistic because using this method can show high income figures in financial statements. The full cost method tends to be more efficient. The author also explains the reason why most companies tend to provide higher compensation is because the costs of renegotiation and changing new managers are more expensive. The choice and procedure of accounting methods is very complex. They may also relate to consolidation companies and their parent and subsidiary companies. How to present their financial statements using appropriate accounting methods. We need to consider more, such as size, area, company's unique environment. Apart from these points, we also need to balance efficiency and opportunism under the many costs associated with the company. This is not a simple problem (Holthaysen R, 1989).

4.2 Focus on Intangible Assets

As mentioned earlier, several accounting methods are used by accountants. However, which method is determined by the manager. An increasing number of accounting method problems arise, especially, in intangible assets. As a new asset , the challenge of the problem is not only to focus on how to measure intangible assets, but how to satisfy shareholders and debt holders. In the management process, measurement of many intangible assets has an existing opportunistic behavior (David H. 1989). Landry and Callimaci (2003) study that treating intangible assets as capital or expense is a problem in the accounting field. In fact, intangible assets are capital in the information age, but some companies never mention it on their balance sheets. Intangible assets must include information and computer data, innovative properties, economic competence. Our group analyzes one of the intangible assets: research and development. In the innovative property section, there are several accounting methods for measuring research and development (R&D).

First, there are two assumptions for R&D, then study in depth especially which one is better for the company, and all stakeholders. Moreover, it is still confused whether there is an opposing relationship between managers and shareholders, or there is opportunism in agency costs.

Hypothesis 1 R&D cost capitalization effect on firms.

Hypothesis 2 R&D costs have an effect on the company.

H1:

Therefore, Markarian (2008) believes that among the firm's decision to capitalize on R&D costs. Recently, Aswath (2014) described the process of transforming R&D spending into capitalization at MICROSOFT CORPORATION on YouTube. At the same time, borrowing the annual report of APPLE INC. 2014&2013, and estimates the company's performance when capitalizing R&D.

Sheet 1 output: all financial data about R&D at apple Inc.

Sheet 2 amortization and comparison

As a result, from the two tables found a large difference in the company's capital between capitalizing R&D costs and maintaining R&D as a cost item. First, after-tax operating income increased by \$2612.66. However, R&D costs are added to after-tax operating income directly. It can be used to obtain tax benefits. In the future, maybe the law will change the rules, and enact tax regulations, if we want to take advantage of R&D. Second, the return on investment has not changed too much. Third, the return on capital fell to 27.47%. Free cash flow never changes. Actually we only capitalize R&D costs and then add them to the company's capital, then the total value of the company becomes large. The company will show better performance compared to spending all R&D costs.

Table 1. Spending all R&D costs

Tahun	Beban Litbang	Bagian yang belum diamortisasi	Amortisasi tahun ini
Saat Ini(2014)	6041.00	1.00 6041.00	2998.25 \$ 0.00
2013 2012	4475.00	0,67	1 115.73 \$ 0.00 1,491.67
2011	3381.00	0,33	\$ \$ 0.00 1,127.00
	2429.00	0,00	\$10.154,98 \$ 809,67
	0.00	0.00	-
Nilai Aset Penelitian =			3,428,33
Investasi pada aset sebagai kapitalis pada tahun berjalan =		6041.00	
Amortisasi aset untuk tahun berjalan =		\$3,428,33	
	Tanpa kapitalisasi	Dengan kapitalisasi	
Pendapatan operasional	\$52,503.00	\$55,115,67	
Pendapatan operasional setelah pajak	\$38,786.04	\$41,398.70	
Pendapatan bersih	\$39,510,00	\$42,122,67	
Nilai buku modal	\$140,534.00	\$150,688,98	
Pengembalian modal	27,60%	27,47%	
Belanja modal	\$9,813,00	\$15,854,00	
Depresiasi & Amortisasi	\$7,946,00	\$11,374,33	
Pengeluaran Modal Bersih	\$1,867,00	\$4,479,67	

R&D. Guida and Boujelbene (2014) claim that managers may intentionally achieve profit targets which may have a close relationship with their compensation. Similarly, Ahmed and Falk (2006) confirm the reason why US accounting standards do not use capitalization when dealing with R&D is that they aim to avoid the risk of managers' excessive discretion. Furthermore, Ahmed and Falk (2006) also claim that they think R&D capitalization does not contribute to increasing firm value. Then, let 's look at the function of cost. According to Kothari S's research, Laguerre T & Leone A claims that The main function of capitalization is to increase the price of securities through increasing the value of the company. If a firm actually charges all R&D, the security's price may not be reflected in its true value. There is no denying that R&D can bring future value to a company. If R&D can generate true cash inflows for a company, we must maintain consistency with accounting principles. As a result R&D costs can be capitalized but must be in a reasonable manner. Guida R & Boujelbene (2014) compare different hypotheses when choosing the type of R&D cost which should be capitalized.

4. Conclusion

This research conclude all the considerations ourselves. Expenditures may be consistent with efficiency, as they aim to reflect the firm's value in the most accurate way. But it ignores the

benefits that can be obtained from such capitalization. Capitalization can increase managers' opportunism, which means they have a wide range of managers' discretion. From our point of view, we think that record keeping should separate out R&D expenses, such as salary costs, material costs and expenses paid out and so on. These costs are related to R&D. We must measure the likelihood of bringing about future benefits from costs. If the level of relevance is lower, then it is excluded. Also, if some expenses are incurred in one accounting period and are not related to profit, we need to charge them as well (accrual principle). The remaining costs, which can bring benefits in the future, we can take advantage of.

Reference

- Ahmed K, Falk H (2006). Value relevance of management research and development reporting options : Evidence from Australia. *Journal Accounting and Public Policy*. 25(3). 231-264
- Christie, Andrew A, Zimmerman, Jerold L (1994). Efficient and opportunistic choice of accounting procedures: a contest for corporate control. *Accounting Review*. 69(4). 539-556.
- Emanuel W, Wong J, Wong N (2003). Efficient contracts and accounting. *Accounting & Finance*. 43(2).149-166.
- Field T, Lys T, Vicent L (2001). Empirical research on accounting choice. *Journal of Accounting and Economics*. 31(1-3). 255-307.
- Guidara R, Boujelbene Y (2014). Profit Management Based on R&D and Performance Motivation Accountancy. *International Journal of Academic Research in Accounting, Finance and Management Sciences*. 4(2). 81-93
- Holthausen, Robert W (1990). Choice of accounting method: opportunistic behavior, efficient contracting, and information perspective. *Journal of Accounting and Economics*, 12(1-3). .207.
- Landry S, Callimaci A (2003). Effect of management incentives and cross-listing status on the accounting treatment of R&D expenditure. *Journal of International Accounting, Auditing and Taxation*. 12(2). 131-152.
- Malmquist DH (1989). Efficient contracting and choice of accounting methods in the oil and gas industry. *Journal of Accounting & Economics*. 12(1-3). 173-205.
- Martinez, Richard J, Dacin, M, Tina (1999). Motives of efficiency and normative power: combining Transaction Fees and Institutional Logic. *Journal of Management*. 25(1). 75-96.
- Nurmadi, R.; Adiman, S.; and Ginting, S. (2018). Measuring and Valuation of Asset: Accounting Theory Perspective. In Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES, p.1208-1212. DOI: 10.5220/0009510912081212.
<https://www.scitepress.org/PublicationsDetail.aspx?ID=0LjRMTSE2nE=&t=1>.
- Simanjuntak, A.; Purba, D.; and Ginting, S. (2018). Regulatory Approach to Formulate Accounting Theory: Literature Study of Developed Countries. Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES, ISBN 978-989-758-432-9, pages 1179-1184. DOI: 10.5220/0009508811791184.
<https://www.scitepress.org/PublicationsDetail.aspx?ID=elt85ocahjw=&t=1>

CHAPTER 11

Three Key Hypotheses Often Used in the Positive Accounting Theory (PAT) Literature to Explain and Predict Support or Disapproval of Accounting Methods

Dilla Nurhidayah ¹, Silvia Handayani ², Iskandar Muda ³

^{1,2,3} Universitas Sumatra Utara, Medan, Indonesia

¹ Email: dillanurhidayah9@gmail.com

ABSTRACT

This study aims to explain positive accounting theory and how the three key hypotheses are often used to explain and predict the support or rejection of accounting methods. In this study, the inductive method is used to draw conclusions about things or events from data that has been collected through observation, and documentation, which can be generalized (drawn towards general conclusions). so it is clear that this inductive method is to assess empirical facts. Found then matched with existing theories. This paper finds that the three main hypotheses that are often used in the positive accounting theory literature are the bonus plan hypothesis, the debt hypothesis, and the political cost hypothesis.

Keywords : Positive Accounting Theory, Bonus Plan Hypothesis, Debt Hypothesis, Political Cost Hypothesis

1. INTRODUCTION

Accounting research is an effort made to find the truth in the field of accounting. In 1977, the actual statement of accounting theory and acceptance of theory issued by the AAA had identified three areas for discussing accounting theory: the classical or income/inductive approach, the decision usefulness approach and the information/economics approach. (Steele, Katie, & H, 2015)

On the basis of its objectives, accounting theory can be divided into two types, namely normative accounting theory which provides a formula for accounting practice and positive accounting theory which seeks to explain and predict accounting-related phenomena (Ghozali and Anis, 2007) in (Herlin, 2012)

(Shabrina, Rizqi, Iskandar, & Syafruddin, 2018) Positive accounting theory has been the subject of intense debate. Zimmerman (2001) says that a unifying theory must emerge, but as a matter of course it must be based on economics. Positive research in accounting began to gain prominence around the mid-1960s and has become a vector for the paradigm shift in financial accounting research in the 1970s and 1980s. Positive accounting theory was developed by Watts and Zimmerman and is based on work done in economics and relies heavily on the efficient market hypothesis, capital asset pricing models, and agency theory.

Jensen expects the development of an accounting theory positive that would explain why accounting is the way it is, why accountants do what they do, and what influence the phenomena have on use of people and resources. (Herlin, 2012)

Watt and Zimmerman (1986) in (Indira, 2004) revealing that there are three basic reasons there is a shift in the normative to positive approach, namely:

- 1) The inability of the normative approach to test the theory empirically, because it is based on the premise or assumptions that are wrong so that their validity cannot be tested empirically.
- 2) The normative approach focuses more on the prosperity of individual investors than on the prosperity of the wider community.
- 3) The normative approach does not encourage or enable the optimal allocation of economic resources in the capital market.

To cover weaknesses of normative theory, Watt and Zimmerman developed a positive approach applicable in the *specific scientific period* 1970-present. (DP, 2008) Positive Accounting Theory (PAT) begins with a study based on normative accounting assumptions in the 180s.

This is indicated by the two groups of studies conducted based on positive accounting theory. First, research conducted by Ball and Brown (1968), Beaver (1963), Foster \$97n, Beaver, Clarke and Wright (1979), Tleaver, Lambert and Morse (1980), Grant (1980), McNichols and Mangotd (1930). by testing the relationship between accounting earnings and stock prices. The results obtained indicate that accounting earnings are relevant in measuring changes in share value. Second, research conducted by Kaplan and Roll (1972), Sunder (1973, 1975), Ricks (1982), etc. Yang attempted to distinguish between two competing hypotheses, such as the "no effect hypothesis" and the "mechanistic hypothesis", where the results proved to be mixed.

The previous research was based on the efficient market hypothesis (EMH) and the capital asset pricing model (CAPM). Such research tends to be doubtful as a result of the existence of assumptions attached to the model used that are normative, such as zero transaction costs and there is only one source of information in making decisions. Where it can not be obtained in the real world. Due to this, the opportunity to explain and predict variations in accounting practices between companies is becoming more open. This is indicated by the practice of choosing an equivalent

accounting method that can potentially affect the cash flow in the company. Based on this idea, the initial study concerned the choice of accounting methods related to bonuses for management, debt, and the political processes that affect firms.

2. LITERATURE REVIEW

In (Shabrina, Rizqi, Iskandar, & Syafruddin, 2018) positive accounting theory, in principle, it assumes that the purpose of accounting theory is to explain and predict accounting practices. Positive accounting theory seeks to explain a process, which uses the ability, understanding and knowledge of accounting and the use of accounting policies that are most appropriate to deal with certain conditions in the future.

The presence of positive accounting theory has made a significant contribution to the development of accounting. The contribution of positive accounting theory to the development of accounting is to produce systematic patterns in accounting choices and provide specific explanations for these patterns, provide a clear framework for understanding accounting, show the main role of contracting costs in accounting theory, explain why accounting is used and provide a framework for predicting choices. -accounting choice, encourage relevant research where accounting emphasizes the prediction and explanation of accounting phenomena. (Herlin, 2012)

The development of positive theory cannot be separated from dissatisfaction with normative theory (Watts and Zimmerman, 1986). Furthermore, it is stated that the reason for analyzing accounting theory with a normative approach is too simple and does not provide a strong theoretical basis.

Given that in an economic system based on market mechanisms, accounting information can be a controlling tool for the community in allocating economic resources efficiently. Positive accounting theory is based on the work done in economics and greatly To reduce the gap in the normative approach, Watts and Zimmerman developed a positive approach that is more oriented towards empirical research and justifies the various accounting techniques or methods currently used or looks for new models for the development of accounting theory. in the future.

Watts and Zimmerman in (Kaya, 2016) reviewing the theory and methodology of the economics-based literature in accounting in their leading book dated 1986. In this book written and used for the second year MBA and Ph.D. Ladies and gentlemen, the authors point out the important role of the efficient market hypothesis in accounting research; they use the CAPM as a valuation method. They explain the methodology of empirical studies in the development of the literature.

(Herlin, 2012) In Januari's paper (2004) described research that supports positive accounting theory, including research conducted by Lev (1979), Healy (1985), Jones (1991), and Sweeney (1994). Lev (1979) research related to the *bonus- debt covenant*, where there is a tendency for managers to be opportunistic by saving bonuses and ignoring changes in *debt covenants* when the expected market efficiency reacts negatively. Subsequent research was conducted to try to examine the effects of management bonus compensation plans (*bonus plans*). This research was conducted by Healy (1985: 85-107) and was followed by Holthausen, Larker, and Sloan (1995: 29-74).

The research wants to prove that managers who base their bonuses on *net income* prefer to use *accrual accounting policies* for reporting their income so that they can maximize bonuses. The results of the study found strong evidence that management's decision to choose or adopt an accounting regulation is closely related to how sensitive the bonus is associated with achieving profit targets. These results reflect the importance of understanding the behavior of managers towards the existence of a compensation plan that can affect their current and future prosperity. Jones (1991) examines firm changes to reduce reported *net income* for import relief.

Granting import relief to companies is unfair because it is influenced by foreign competition, which is partly a political decision.

The research that criticizes positive accounting theory . The positive approach looks at "why accounting practice and/or accounting theory develops as it is with the aim of explaining (*to explain*) and predict (*to predict*) accounting events. Therefore, the positive approach seeks to determine the various factors that might influence rational factors in the accounting field. Basically the positive approach seeks to determine a theory that explains the observed phenomena. The positive approach seems to have generated considerable optimism among its supporters. But this sense of optimism is not shared naturally by everyone.

The critique of positive accounting theory that was conveyed before Wattz and Zimmerman wrote the article in 1990, was first expressed by Christenson (1983: 5) who stated that positive research is more related to the sociology of accounting. This is because the content is in the form of descriptions and predictions about the behavior of individuals, both accountants and managers, in choosing accounting methods.

According to Christenson, in (Herlin, 2012) terms of accounting theory development, the behavior that is explained and predicted should be the behavior of accounting entities. This is in line with Godfrey et al (2010) which states that positive accounting theory is more of a sociology of accounting, because it focuses on human behavior rather than the behavior or measurement of accounting entities. Furthermore, Christenson (1983) says that looking at science does not have to be viewed from the difference between normative and positive, but can be seen as a product, namely a systematic set of knowledge or viewed as a process, namely human activity in producing knowledge.

The second criticism is conveyed by Sterling (1990) which is divided into three parts, namely 1) two main pillars related to the study of phenomena and *value free*, 2) basic economic assumptions rooted in positive economic theory, 3) *science* rooted in logical positivists and achievements actual and potential.

The first pillar of Sterling's critique consists of the study of phenomena related to research into accounting practice, accounting practice, and *utility maximization*. The study of the phenomenon of accounting practice reveals that theory is considered scientific if it is based on practice because then theory can be used to predict and explain individual behavior, both accountants and managers, regarding the selection of accounting methods. This implicitly states that what is considered scientific is a positive theory. Meanwhile, theories that are not put into practice, namely normative theories are considered unscientific.

3. METHOD

Basically, qualitative research data analysis has been carried out from the beginning of the research activity to the end of the research. In this way, it is hoped that there will be consistency in the overall data analysis (Simanjuntak et al., 2018). Considering that this research is descriptive in nature, a philosophical or logical data analysis is used, namely inductive analysis.

The inductive method is a method of thinking by drawing conclusions from certain data. Inductive thinking departs from specific facts, concrete events, then from certain facts or events, generalizations are drawn (Nurmadi et al., 2018). In this study, the inductive method is used to draw conclusions about things or events from data that has been collected through observation and documentation, which can be generalized (drawn towards general conclusions), so it is clear that this inductive method is to assess empirical facts. Found then matched with existing theories.

4. RESULTS AND DISCUSSION

a. Result

The (Indira, 2004) positive approach has made a significant contribution to the development of accounting according to Watt Zimmerman (1986).

- 1) Generate systematic patterns in accounting choices and provide specific explanations.
- 2) Provide a clear framework in understanding accounting
- 3) Shows the main role of *contracting costs* in accounting theory.
- 4) Explain why accounting is used and provide a framework for predicting accounting choices.
- 5) Encouraging research relevant to accounting and emphasizing the prediction and explanation of phenomena,

Theory is needed because the theory can be used to predict *certain* social phenomena that are expected to occur. This means that the requirements or assumptions that support a theory can be met, so there is a great hope (possibility) that certain social phenomena will occur, but this does not mean that the theory causes the predicted phenomena to occur. Based on this understanding, it can be concluded that the theory consists of descriptive hypotheses as a result of research using certain scientific methods.

Positive accounting theory has reduced by not recognizing the theory normative as something scientific. Whereas the reality of accounting itself is not value-free. even loaded with value. So the reality of accounting is not free from normative aspects. This matter This was emphasized when in 1986 Watts and Zimmerman defined accounting theory positive as a textbook, according to Sterling since then positive accounting theory has to be normative and Wattz and Zimmerman have included the value that the correct is an empirical process. In this case, the reality of accounting is actually also practice normative aspects of accounting, which are then tested statistically which is a construct mathematical theory (positive theory) for further confirmation of the theory. So can concluded that *science* has a chain of activity relationships, where researchers seek and find more advanced techniques (positive theory), academics then teach these techniques (normative theory), and practitioners implement these techniques better.

The hypothesis will be a reference source for explaining and predicting the symptoms or events in accounting. The hypothesis in positive accounting theory formulated by Watt & Zimmerman (1986) in the form of "*opportunistic*" which is often interpreted, namely:

- 1) The bonus plan hypothesis (*Plan Bonus Hypothesis*), in *ceteris paribus*, the managers of companies with bonus plans will be more likely to choose accounting procedures that can replace *earnings reports* for future periods to the current period or known as *income smoothing*. With this hypothesis, if the manager in his salary system is very dependent on bonuses, he will tend to choose an accounting method that can maximize his salary, for example the *accrual method*.
- 2) *Debt Covenant Hypothesis*, in *ceteris paribus* managers of companies that have a large leverage ratio (*debt/equity*) will prefer to choose accounting procedures that can replace *earnings reports* for the future period to the current period. By choosing an accounting method that can transfer profit recognition for future periods to the current period, the company will have a small *leverage ratio*, thereby reducing the possibility of *technical default*. As it is known that many debt agreements require the borrower to comply with or maintain debt to equity ratios, working capital, shareholder equity etc. during the term of the agreement, if the agreement is violated the debt agreement may provide penalties, such as constraints on dividends or additional loans.
- 3) The political *process hypothesis*, in *ceteris paribus*, the greater the company's political costs, the more likely company managers are to choose accounting procedures that defer current *earnings reports* to future periods.

Many researchers have proven the three hypotheses put forward by Watt & Zimmerman, while the researchers are Scott (2000):

- 1) Healy, 1985 with the bonus planning hypothesis, which produces evidence that managers who base their bonuses on *net income* are reported systematically using *accrual accounting policies* for reporting earnings so that they can maximize bonuses.
- 2) Sweeney, 1994 with the debt covenant hypothesis, produced evidence that companies often violate debt covenants in the form of maintaining working capital and shareholder equity.
- 3) Jones, 1991 examines firm changes to reduce reported *net income* for import relief. Giving import concessions to companies is unfair because it is influenced by foreign competition, partly a political decision.
- 4) Lev (1979) in the bonus - *debt covenant hypothesis*, there is a tendency for managers to be opportunistic by saving bonuses and ignoring changes in *debt covenants* when the expected market efficiency reacts negatively.

PAT has led to a large number of empirical studies. Positive researchers empirically test their predictions around the bonus plan hypothesis, the debt covenant hypothesis, and the political cost hypothesis.

b. Discussion

The presence of positive accounting theory has made a significant contribution to the development of accounting, namely generating systematic patterns in accounting choices and providing specific explanations for these patterns, providing a clear framework for understanding accounting, showing the main role of *contracting costs* in accounting theory, explaining why accounting is used and providing a framework. in predicting accounting choices, encourage relevant research where accounting emphasizes the prediction and explanation of accounting phenomena.

The rejection of positive accounting theory is a discourse that can actually contribute to accounting science. Criticism arises because Watts and Zimmerman's framework is more motivated by the *pragmatism utility of knowledge of accounting research*, where the size used is determined according to the contribution it makes, namely positive accounting theory can provide direct

benefits in the form of the ability to explain and predict accounting practices associated with individual behavior. in maximizing its utility. Critics expect more roles, namely entering into accounting science and not only in accounting practice

c. CONCLUSION

The hypothesis in positive accounting theory formulated by Watt & Zimmerman (1986) in the form of "*opportunistic*" which is often interpreted, namely:

- 1) The bonus plan hypothesis (*Plan Bonus Hypothesis*), in *ceteris paribus*, the managers of companies with bonus plans will be more likely to choose accounting procedures that can replace *earnings reports* for future periods to the current period or known as *income smoothing*.
With this hypothesis, if the manager in his salary system is very dependent on bonuses, he will tend to choose an accounting method that can maximize his salary, for example the *accrual method*.
- 2) *Debt Convenat Hypothesis*, in *ceteris paribus* managers of companies that have a large leverage ratio (*debt/equity*) will prefer to choose accounting procedures that can replace *earnings reports* for the future period to the current period. By choosing an accounting method that can transfer profit recognition for future periods to the current period, the company will have a small *leverage ratio*, thereby reducing the possibility of *technical default*. As it is known that many debt agreements require the borrower to comply with or maintain the ratio of debt to equity, working capital, shareholder equity etc. during the term of the agreement, if the agreement is violated the debt agreement may provide penalties, such as constraints in dividends or additional loans.
- 3) The political *process hypothesis*, in *ceteris paribus*, the greater the company's political costs, the more likely company managers are to choose accounting procedures that defer current *earnings reports* to future periods.

The three hypotheses above show that positive accounting theory recognizes three agency relationships, namely between management and owners, between management and creditors, and between management and government.

REFERENCE

- DP, EN (2008). Positive Accounting Theory is viewed from three philosophies (Lakatos, Kuhn, and Poer). *ISSN 0854-8986* .
- Herlin, TS (2012). Positive Accounting Theory and Economic Consequences. *Journal of Accounting* , 427-438 .
- Indira, J. (2004). Approaches and Criticisms of Positive Accounting Theory. *Journal of Accounting & Auditing* .
- Kaya, D. (2016). Accounting Options in corporate financial reporting: A literature review of positive accounting theory. *Intechopen* .
- Nur, E. (2008). Positive Accounting Theory is viewed from three main streams of philosophy (Lakatos, Kuhn, and Popper). *ISSN 0854-8986* .
- Nurmadi, R.; Adiman, S.; Muda, I. and Ginting, S. (2018). Measuring and Valuation of Asset: Accounting Theory Perspective. In Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES, p.1208-1212. DOI: 10.5220/0009510912081212.
<https://www.scitepress.org/PublicationsDetail.aspx?ID=0LjRMTSE2nE=&t=1>
- Shabrina, TA, Rizqi, FP, Iskandar, M., & Syafruddin, G. (2018). Positive Accounting Theory: Theoretical Perspectives on Accounting Policy Choices. *Science and Technology Publications* .

- Steele, Katie, & H, OS (2015). *Decision Theory* . *Stanford Encyclopedia of philosophy* .
- Scott, (2000). *Financial Accounting Theory* , Prentice Hall Inc
- Simanjuntak, A.; Purba, D.; Muda, I. and Ginting, S. (2018). Regulatory Approach to Formulate Accounting Theory: Literature Study of Developed Countries. Proceedings of the 1st Unimed International Conference on Economics Education and Social Science - Volume 1: UNICEES, ISBN 978-989-758-432-9, pages 1179-1184. DOI: 10.5220/0009508811791184. <https://www.scitepress.org/PublicationsDetail.aspx?ID=elt85ocahjw=&t=1>
- Watts and Zimmeman, (1986). *Positive Accounting Theory* , Prentice Hall
- .

Accounting Inquiries with New Approaches in the Post-Pandemic Era
Volume I

CHAPTER 12

Behavioral Implications of Airline Depreciation Accounting Policy Choice

Abdurahman Hakim¹, Nanda Dwi Kartika², Iskandar Muda³

^{1,2,3}Universitas Sumatera Utara, Medan, Indonesia

¹ Email: abd.rahman@student.usu.ac.id

ABSTRACT

Fixed assets are a very important component for the company for its operational activities and as a support to achieve the objectives of the company's establishment. Depreciation is also known as depreciation, namely the allocation of fixed assets due to a decrease in the value of these fixed assets. The research method used in this research is descriptive research. The research instrument used is financial statement data in the form of a balance sheet. The population used is data on the financial statements of airlines. The data collection technique used is a literature study. The four airlines use the straight-line depreciation method. The financial performance of the four companies is different. The result of this research is that Delta Airlines wants to reduce its depreciation expense from 6% per year to 4.75% per year. AMR Corporation's new policy is to change the depreciation rate from 4.75% to 3.60% per year. Meanwhile, Singapore Airlines has made three policy changes. Initially the company used a depreciation rate of 11.25% but in 1989-2001 the rate changed to 8.00%. The latest change is 6.00% per year from the beginning of 2001.

Keywords : Operational Activities, The Allocation Of Fixed Assets, Behavioral Implications

1. INTRODUCTION

The goal of a profit-oriented organization is to maximize shareholder profits and maximize the value of the company in the short term. With ideal results will reward employees for their contributions to the company (Cavaliere, et al., 2021). Therefore, companies must look for measurements that represent the ultimate goal and take alternative paths in obtaining control results

Performance measurement can be divided into three categories. Two of these categories are summary financial measures, which are intended both in market (share prices) and in financial terms, and the third category is a combination of measures (Rahmi et al., 2022). The measurement summary reflects a collection of various performance areas. The first category contains market measurements, which describe changes in stock prices. The second category contains accounting measures, which can be defined in terms of either residuals (such as net income after tax, operating profit, residual income, or additional economic value) or ratios (such as Return on Investment (ROI), Return on Equity (ROE), or Return on Net Operating Assets (RNOA)). The third category is a combination of measurements involving market measurements and financial measurements.

To support the achievement of that goal, each company has certain assets to facilitate the activities carried out by the company (Cavaliere et al., 2021). Fixed assets are a very important component for the company for its operational activities. These fixed assets are one of the components in the balance sheet, so that the accuracy in processing fixed assets greatly affects the fairness of their valuation in the financial statements. The fairness of the valuation of a company's fixed assets can be adjusted to the Statement of Financial Accounting Standards (PSAK) No. 16 (2009). In this PSAK it is stated that fixed assets are tangible assets that are held for use in the production or supply of goods or services, for rental to other parties, or for administrative purposes and are expected to be used for more than one period.

Behavioral problems on the selection of accounting policies on depreciation costs are an important problem, because they affect the profits generated by a company. If using the depreciation method that is not in accordance with the applicable principles or conditions of the company, it will affect the income reported for each accounting period. In addition, it also affects the value of these fixed assets. In calculating the depreciation of fixed assets there are several methods that can be used, among others: the straight line method, the declining balance method, the number of years method, the unit input method and the unit output method.

Managers of some companies choose a relatively “conservative” set of policies, while others choose a relatively “liberal” set of policies. To determine whether airlines tend to be conservative or liberal in choosing accounting policies, one of the areas that can be reviewed is the area of fixed asset accounting (Property, Plant, and Equipment – PP&E). Fixed assets generally account for more than 50% of the total assets of an airline. , the fixed asset accounting policies of airlines vary widely.

The airlines that are the object of this research are four airlines which include Delta Airlines, AMR Corporation, Singapore Airlines and Lufthansa. The airline in this company has aircraft that can fly indefinitely assuming the aircraft is properly maintained, has aircraft maintenance costs that tend to increase over time, has a limited economic useful life, but is difficult to estimate, the price of new aircraft tends to increase overtime.

2. LITERATURE REVIEW

2.1. Agency Theory

Agency theory describes the company as a meeting point between the owner of the company (principal) and management (agent). Rahmawati, et al (2006) stated that the agency relationship is a contract that occurs between the manager (agent) and the owner of the company (principal). The powers and responsibilities of both the agent and the principal are regulated in a work contract by mutual agreement. The concept of agency theory according to Anthony and Govindarajan (2005) is

the relationship between principal and agent. Principals employ agents to perform tasks in the interests of the principal, including delegating decision-making authorization from the principal to the agent. In companies whose capital consists of shares, shareholders act as principals, and the CEO (Chief Executive Officer) as their agent. Shareholders employ the CEO to act in the interests of the principal (Santoso, 2020).

According to Ujijanto and Bambang (2007), agency theory uses three assumptions of human nature, namely: (1) humans are generally self-interested (self-interested), (2) humans have limited thinking power regarding future perceptions (bounded rationality) , and (3) humans always avoid risk (risk averse). Based on the assumption of human nature, managers as humans will act opportunistically, namely prioritizing their personal interests. Agents are motivated to maximize the fulfillment of their economic and psychological needs, among others in terms of obtaining investments, loans, and compensation contracts. Conflicts of interest are increasing mainly because the principal cannot monitor the day-to-day activities of the CEO to ensure that the CEO is working in accordance with the wishes of the shareholders. The principal does not have sufficient information about the agent's performance. Agents have more information about the company as a whole. This has resulted in an imbalance of information held by the principal and agent (Nasution and Doddy, 2007).

2.2. Accounting Policy

2.2.1. Conservative Accounting

Watts (2003) defines conservatism as a precautionary principle in financial reporting where companies are not in a hurry to recognize and measure assets and profits and immediately recognize losses and debts that may occur. The application of this principle in the choice of accounting method at the method that reported lower income or assets and reported higher debt. Thus, lenders will receive protection against downside risk from a balance sheet that presents net assets and financial statements that report bad news in a timely manner (Haniati and Fitriany, 2010). GIVoly and Hayn (2000) define conservatism as early recognition of expenses and losses and deferred recognition of revenues and gains.

The official definition of conservatism is contained in the Glossary of Concept Statements No. 2 FASB (Financial Accounting Statement Board) which defines conservatism as a prudent reaction in the face of uncertainty inherent in the company to try to ensure that the uncertainties and risks in the business environment already considered enough

The principle of conservatism is a concept that recognizes expenses and liabilities as soon as possible even though there is uncertainty about the outcome, but only recognizes income and assets when it is certain that they will be received.

2.2.2. Liberal Accounting

Companies that are optimistic in recording their transactions are referred to as aggressive accounting or liberal accounting. Liberal accounting is an accounting process to recognize and record a transaction or event in an expolative manner. Based on this process, liberal accounting will state that the value of assets is too high or the value of debt is too low on the balance sheet.

Liberal accounting is also a selection criterion among accounting principles obtained by accelerating revenue recognition, slowing expense recognition, valuing assets higher and valuing debt lower.

2.3. Depreciation

According to PSAK No. 16 (2011:13 paragraph 06) Depreciation is "the systematic allocation of the depreciable amount of an asset over its useful life". According to Putra et al (2020)

depreciation is the allocation of the acquisition price of fixed assets as an expense into the accounting period that enjoys the benefits of these fixed assets.

2.4. Fixed Asset Depreciation Accounting Method

PSAK No. 17 definition of depreciation as the allocation of the amount of an asset that can be depreciated over its estimated useful life. Depreciation for the accounting period is charged to revenue either directly or indirectly. There are several methods of accounting for allowable depreciation. This research focuses on the use of the straight-line method of depreciation, the sum of the years digits and the declining balance.

Profit or profit is one of the company's goals in carrying out its activities. The profit earned by the company will be used for various purposes, the profit will be used to improve the welfare of the company for the services it obtains. Hanum (2020) explains that profit is a measure of the company's overall performance, which is defined as follows: Profit = sales – costs. Meanwhile, the Financial Accounting Standards (2004) describe that profit is the definition of income which includes both revenue and gains. Revenues arise in the course of the ordinary activities of the company and are known by different names such as sales, service fees, interests, royalties and rent. Gains reflect other items that meet the definition of income and may or may not arise in the course of the ordinary activities of the enterprise. Gains reflect increases in economic benefits and are thus not substantially different from income. Therefore, they are not considered as separate items in the framework this base.

Setiadi (2020) in his research explains that the straight-line depreciation method applied by the company to its fixed assets is very appropriate. This can be seen from the relationship between the decline in asset value with use and time, the effect of obsolescence, the pattern of repair and maintenance costs, as well as the level of operating efficiency.

3. METHOD

3.1. Types of research

This type of research is descriptive research. Descriptive research is a method used to describe or analyze a research result but is not used to make broader conclusions (Sugiyono, 2005:21)

3.2. Population and Sample

The population in this study are airlines that use the straight-line depreciation method, have different residual values and useful lives of aircraft due to time differences. The sample used in this study is the balance sheet in the financial statements of Delta Airlines, AMR Corporation, Singapore Airlines and Lufthansa from 1989 to 2001.

3.3. Research Instruments and Data Collection Techniques

The instrument used in this research is data on the financial statements of Delta Airlines, AMR Corporation, Singapore Airlines and Lufthansa, in the form of a balance sheet containing fixed assets, total assets and accumulated depreciation of the company's fixed assets. The data collection technique used is a literature study related to the object of research by obtaining library materials

4. Results and Discussion

4.1. Result

The accounting policies for fixed assets of airlines vary widely. Behavioral Implications of Airline Depreciation Accounting Policy Choices describe the selection of accounting policies made by managers. Managers of some companies choose a relatively “conservative” set of

policies, while others choose a relatively “liberal” set of policies. Conservatism causes delays in the recognition of certain receipts or gains and/or accelerates the recognition of certain expenses or losses. The effect of conservatism is that earnings will be reported at a later date and longer than the use of more liberal accounting policies.

To determine whether airlines tend to be conservative or liberal in choosing accounting policies, one area that can be reviewed is the area of fixed asset accounting (Property, Plant, and Equipment – PP and E). Fixed assets generally account for more than 50% of the total assets of an airline. The following is a breakdown of the depreciation policies of the four major airlines:

Table 1. The Depreciation Policies

	Delta Airlines			AMR Corporation	
	< 1986	1986-1993	>1993	< 1999	>1999
Estimated Useful Life (Year)	10	15	20	20	25
Residual Value (% of cost)	10%	10%	5%	5%	10%
Depreciation Expense per year (% cost)	9.00%	6.00	4.75%	4.75%	3.60%
Annual Depreciation Expense for \$100 gross value of Aircraft (in Dollars)	\$9.00	\$6.00	\$4.75	\$4.75	\$3.60
	Singapore Airlines			Luthansa	
	< 1989	1989-2001	>2001		
Estimated Useful Life (Year)	8	10	15	12	
Residual Value (% of cost)	10%	20%	10%	15%	
Depreciation Expense per year (% cost)	11.25%	8.00	6.00%	7.08%	
Annual Depreciation Expense for \$100 gross value of Aircraft (in Dollars)	\$11.25	\$8.00	\$6.00	\$7.08	

The details of the facts from this case are that an airplane can fly indefinitely if properly maintained, maintenance costs tend to increase every year, the economic useful life of aircraft is limited, but difficult to estimate, aircraft prices tend to increase over time (some aircraft flying values have been maintained at 90% or more despite decades of use, although it is rare for an aircraft in operation to fall below 50%).

The four airlines use the straight-line depreciation method. The salvage value and useful life of the aircraft from the four companies are different due to the time difference. It should be noted that the choice of measurement method is one of the reasons why accounting profit measurement fails to reflect economic income perfectly. An example in this case is how AMR Corporation was able to reduce depreciation expense of approximately \$158 million after changing the useful life and residual value of its property, plant and equipment so that the company's accounting profit was higher. In fact, the increase in accounting profit is not necessarily followed by an increase in actual economic income. Although each company has its own reasons for calculating depreciation based on the thinking and rationalization of the company's management, the choice or change in depreciation accounting needs to be observed by looking at some of the reasons stated above.

Given that the economic useful life of an aircraft is limited but difficult to estimate, changes in the useful life and residual value may not be appropriate because some types of aircraft are no longer competitive for use in the passenger market in the future. An example in this case is the use of aircraft that first operated in 1957 or even earlier, namely in 1935, although they are no longer competitive. It is understood that an aircraft that is no longer competitive will have fewer hours of flight than a new aircraft owned by the company but both

will have the same or nearly the same depreciation expense. This of course will not be seen in the short term unless there are new technological breakthroughs and will make the company's short term profits higher than the profits that will be obtained in the future. Another important consideration is that although in many countries tax regulations allow ultra-conservative accounting to ensure that companies do not have to pay taxes before getting cash from customers, in this case the rules are not widely used by companies. Companies tend not to depreciate airplanes as quickly as possible to defer tax obligations because doing so will result in lower profits. Savings on depreciation expense are more profitable for the company than savings on taxes because in the short term the company's profits are higher.

4.2. Discussion

The financial performance of the four companies is different. Delta Airlines wants to reduce its depreciation expense from 6% per annum to 4.75% per annum. AMR Corporation's new policy is to change the depreciation rate from 4.75% to 3.60% per year. Meanwhile, Singapore Airlines has made three policy changes. Initially the company used a depreciation rate of 11.25% but in 1989-2001 the rate changed to 8.00%. The latest change is 6.00% per year from the beginning of 2001. Singapore Airlines' depreciation assumptions are very different from those of Delta's and AMR Corporation. This relates to the company's overall strategy: If the amount of depreciation of a company is high, this will have an effect on low net income. The company will pay taxes based on a low net income so that the savings in tax payments can be felt by the company by changing the depreciation assumption. The company targets the sale of aircraft at a fair market value, where the value of the aircraft is 20% higher than the residual cost after 10 years.

5. Conclusion

Conclusions from the description of the case analysis that has been presented above, several conclusions can be drawn as follows:

1. Performance measurement that is often used is market measurement and accounting measurement.
2. Company managers have a tendency to be oriented towards achieving short-term profits, which is often known as corporate myopia. Myopia is the tendency to make managers focus too much on the short term so that the company's long term orientation is often overlooked.
3. One of the ways that company managers do to increase company profits in the short term is to change accounting policies related to depreciation of fixed assets. The method commonly used as in the example above is to extend the estimated useful life of property, plant and equipment and increase the salvage value. The goal is to reduce the cost of depreciation of fixed assets so that the company's net income increases. With high net income, managers expect to get high incentives from the company.

Reference

- Anthony, R., Vijay Govindarajan (2005). *Management Control System*, Volumes I and II, Translation of Kurniawan Tjakrawala and Krista, Salemba Empat Publishers, Jakarta.
- Cavaliere, L. P. L., Rakesh, D. S. K., Polisetty, A., Swadia, B. U., Rajest, S. S., & Regin, R. (2021). The Determinants of Audit Quality and Impact on Overall Audit Performance. *Nveo-Natural Volatiles & Essential Oils Journal/ NVEO*, 8(5). 12963-12984. <https://www.nveo.org/index.php/journal/article/view/4139>
- Cavaliere, L. P. L., Ruby Khan, D. S. C., Vijayalakshmi, N. S., Chakravarthi, M. K., Rajest, S. S., & Regin, R. (2021). The Impact of the monetary policy on the performance of deposit money

- banks in MENA Region. *Nveo-Natural Volatiles & Essential Oils Journal/ NVEO*, 10805-10826. <https://www.nveo.org/index.php/journal/article/view/3026>
- Hanum, Z., (2020). Effect of Tax Planning on Profit Management in Registered Food and Beverage Sub Sector Manufacturing Companies On the Indonesia Stock Exchange. *Junior Scientific Researcher*, 6(1), 48-57. https://www.jsrpublishing.com/userfiles/files/archive_pages/97/Article._Zulia_Hanum_Vol.V_I_No.1_2020.pdf
- Indonesian Accounting Association. (2011). *Financial Accounting Standards*. Jakarta: Salemba Empat Publishers.
- Nasution, Marihot and Doddy Setiawan (2007). *Effect of Corporate Governance on Earnings Management in the Indonesian Banking Industry*. SNA X Makassar.
- Putra, K.B, Tarigan, M.F, (2020). A Set of Fixed Tangible Assets Long Term to Used for Operating Activities in the Company. *Turkish Online Journal of Qualitative Inquiry*. 11(4). 1060-1066. <https://tojqi.net/index.php/journal/article/view/8224>
- Rahmawati, et al (2006). *Effect of Information Asymmetry on Earnings Management Practices Public Banking Company listed on the Jakarta Stock Exchange*, Symposium National Accounting IX.
- Rahmi, N.U, Susanto, A, (2022). Implications of Corporate Social Responsibility (CSR) on the Financial Performance of Companies Receiving the Sustainability Reporting Award (SRA). *Journal of Positive School Psychology*. 6(3). 2443–2450. <https://journalppw.com/index.php/jpsp/article/view/1976/1157>.
- Ratnadi, Ni Made Dwi. (2016). *Conservatism Accounting Theory and Measurement Models*. Denpasar: Private Publisher Nulus
- Santoso, M. R. (2020). Shareholders and Firm Value for Manufacturing Companies Listed in Indonesia Stock Exchange. *Journal of Economics, Business, & Accountancy Ventura*, 23(1). 138-147. <https://journal.perbanas.ac.id/index.php/jebav/article/view/2171>
- Savitri, Enni (2016). *Accounting Conservatism Method of Measurement, Empirical Review and Factors Influencing It*. Edition 1. Yogyakarta: Pustaka Sahila Publisher
- Setiadi (2020). Application of Fixed Assets Depreciation Method (Case Study at PT Chandra Sakti Main Leasing Jakarta). *Journal of Business and Accounting Elements*.5(2). 89-103.
- Sugiyono. (2017). *Research Methods Quantitative, Qualitative and R and D*. Bandung: Alfabeta
- Ujiyantho, Muh. Arief and Scouts, Bambang Agus (2007). *Corporate Mechanism Governance, Earnings Management and Financial Performance (Study on Go . Companies Public Manufacturing Sector)*. National Accounting Symposium X. Makassar.
- Utama, Adhika (2015). *Behavioral Implications of Airline Depreciation. Case Analysis Accounting Policy Choices*. Jakarta: State College of Accountancy.

Accounting Inquiries with New Approaches in the Post-Pandemic Era
Volume I

CHAPTER 13

Cultural Dimension Model and The Effect of Culture On Accounting Systems

Ricky Martin Sitorus¹, Floren Asteria Giawa², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹Correspondence email : rickymartin@student.usu.ac.id

ABSTRACT

This study uses a descriptive approach through the collection of literature and the purpose of this journal is to assist the reader in understanding the basic concepts of the influence of culture on the accounting system. Based on the results of the analysis of financial reporting in force in a country, it is determined through government regulations, or other private entities that are authorized. The rules in a country's financial reporting are regulated in its accounting standards. It is the same with Indonesia where the accounting standards are regulated in the Financial Accounting Standards (SAK) set by the Indonesian Institute of Accountants (IAI). From several observations made by researchers, it appears that there are differences in accounting standards that apply in each country. And this difference, there must be harmonization in accounting standards. Where, if a company will sell its shares in another country through the capital market. Then it will be able to determine the accounting standards used in financial reporting.

Keywords : Accounting Systems, accounting system culture, Cultural Characteristics

1. Introduction

Accounting is used in terms of accountability and the provision of information used in decision making by users of that information. Redebaugh and Gray (1997) Accounting is an environmental product that is influenced and reflects its environment. The accounting system itself is defined as a set of accounting methods, procedures and controls that are made in an organized manner that is used to collect, record, classify, analyze, summarize, interpret, and present accurate and timely financial data which will be used in decision making by management (Nasution et al., 2021 and Yulisfan and Nedelea, 2021). Where this system is often based on transactions during the company's business operations. (Manullang, 2008) The accounting system is a collection of standards, rules, policies in the field of accounting set by the government, professional organizations or other institutions, which arise because of the interaction between these institutions and other institutions in order to carry out social functions. The development of the accounting system is influenced by several factors including the political system, economy, tax system, capital market development, and culture (Redebaugh and Gray, 2006). Culture is the most important social factor (Perbawasari et al., 2019). Culture is the overall attitude and pattern of behavior and knowledge which is a habit that is inherited and owned by a member of a particular society which affects aspects of life such as religion, customs, politics and so on. Culture has become a social phenomenon that shapes human existence and various aspects of life related to humans (Lubis et al., 2021).

The importance of culture and history is now increasingly recognized in today's accounting developments. Although less attention has been paid in the past to this dimension in the classification of the international literature. Culture is considered an important element in the framework for understanding how social systems change due to the influence of culture and values, norms and group behavior within and across systems. Gray (1988) suggests that a theoretical framework that incorporates culture can be used to explain and predict differences in accounting systems and to identify patterns of accounting development. Gray also argues that culture, or social values, can be expected to permeate organizational and work subcultures, albeit with varying degrees of integration. Because accounting systems and practices can influence and strengthen social values. This study examines the influence caused by culture on the accounting system in financial reporting reports and the factors that affect the accounting system along with the harmonization and standardization of accounting.

2. Literature Review

Hofstede (1980) suggests about cultural framework which has four components, namely external influences, ecological factors, cultural dimensions, and institutional consequences. Where, external influences (such as natural forces, trade and investment) affect ecological factors (geography, economy, history, demography, genetics, and technology). And these ecological factors also affect cultural dimensions (individualism, power distance, uncertainty avoidance, and masculinity), which also affect institutions (education, religion, political system, and legal system). In turn, ecological factors and cultural dimensions are reinforced by institutions.

Gray (1988) also extends the cultural framework developed by Hofstede (1980) into the financial accounting system. Which treats financial accounting as a subculture, adding a cultural framework to the elements of accounting values (professionalism, uniformity, conservatism, and confidentiality) and accounting systems (authority, enforcement, measurement, and disclosure) and the relationship of cultural and institutional dimensions. Gray (1988) also claims that accounting values originate from and are associated with cultural dimensions. Furthermore, the accounting system will be influenced by accounting values and will also be influenced by institutions.

Redebaugh and Gray (2006) suggest several factors that affect the accounting system. These factors will affect the business world in its accounting practices and the disclosure of company financial information. The factors referred to include the nature of company ownership, business activities, sources of funding, and the capital market, the taxation system, the existence and

importance of the accounting profession, accounting education and research, political system, social climate, economic growth and development level, level of inflation, the statutory system, and accounting accounts. Meanwhile (Christopher Nobes and Robert Parker, 1995, Wardhani et al., 2022)) explain the existence of seven factors that affect the accounting system and accounting practices. These factors include the legal system, sources of funds, taxation system, accounting profession, inflation.

3. Method

This study uses a descriptive approach through the collection of literature and the purpose of this journal is to assist the reader in understanding the basic concepts of the influence of culture on the accounting system.

4. Results and Discussion

4.1. Results

4.1.1. Cultural Dimension

Culture contains patterns, explicit or implicit, of required behavior and embodied in symbols, which indicate different human groups, including human creations, the main core of culture is traditional ideas which are hereditary and selected and the values inherent in culture.

- Cultural Characteristics
 - a. Learning: In learning, observation and experience where culture is required and manifested.
 - b. Sharing: Individuals in groups, families and communities share cultures.
 - c. Transgeneration: It is cumulative and passes from one generation to another.
 - d. Caregiver perceptions: Shape the behavior and structure of how a person perceives the world.
 - e. Adaptation: Culture is based on a person's capacity to change or adapt.
- Organizational culture
 - a. Globally oriented corporate organizational culture will influence and be influenced by the national culture in which the company operates.
 - b. The organizational culture of a company may differ from country to country.
 - c. Organizational Culture, contains values, beliefs, assumptions, perceptions, norms, peculiarities and behavior patterns.
 - d. Culture in an organization helps workers respond to the inevitable uncertainty and complexity of getting a job done.

Culture organization in simple terms "Personality" or "Feeling". Culture affects the way humans act in organizations, namely in working, looking at work, working with colleagues, and looking at the future which is largely determined by cultural norms.

- National Culture
 - a. National Culture, is a collection of values, attitudes, beliefs and norms that are mingled by the majority of the population of a country.
 - b. Being important traits in the laws and regulations of the community, also become norms that are generally accepted in the social system of the country.
 - c. And people in society learn what to obey and what not, how they get along with one another, and how they handle responsibility, success and failure.
 - d. Often not aware of how culture actually has influenced values, attitudes, beliefs and norms.
 - e. In general, the country has a dominant national culture. However, it is different from Japan and the United States which have strong sub-cultures.
 - f. A strong national culture creates a lot of conflict with subcultures that disrupt society and subgroups

4.1.2. The Influence of National Culture on Accounting Sub-culture

- The Influence of Culture on the Accounting System

Harrison and McKinnon (1986) proposed a methodological framework incorporating culture for analyzing changes in country-specific corporate financial reporting regulations. Culture is considered an important element in the framework for understanding how social systems change due to the influence of culture and values, norms and group behavior within and across systems. Complementing this approach, Gray (1988) suggests that a theoretical framework that incorporates culture can be used to explain and predict international differences in accounting systems and to identify patterns of international accounting development.

- **Culture, Social Values and Accounting**

(Hofstede, 1980) Structural Elements of Culture that affect business detects the structural elements of culture that most strongly influence behavior in organizational and institutional work situations. Hofstede's statistical analysis reveals four underlying social value dimensions, namely Individualism, Power Distance, Uncertainty Avoidance, and Masculinity.

- **Structure of Cultural Elements**

Affecting Business Statistical analysis proposed by Hofstede (1980) produces four basic dimensions of social value, namely individualistic vs. collectivity, large vs. small power gap, strong vs. weak uncertainty avoidance, masculine vs. feminism.

- **Accounting Value**

Gray (1988) identified 4 accounting values for the accounting profession and accounting practice, namely professionalism vs legislation, uniformity vs flexibility, conservatism vs optimism, confidentiality vs transparency.

- **International Accounting Value and Classification**

Having linked social values to international accounting values it is necessary to distinguish between the power of the accounting system, i.e. the extent to which the system is influenced by statutory controls or professionalism, and the measurement and disclosure of accounting system characteristics. In this way, accounting values can be linked to the characteristics of the accounting system. Gray (1988) a model for examining the accounting change process. Where to identify several important factors regarding international pressures that affect accounting changes such as international economic and political developments, new trends in foreign direct investment, changes in multinational corporate strategies, the influence of new technologies, developments in international financial markets,

4.1.3. Factors Affecting Accounting Practices and Systems

There are 8 (eight) factors that influence accounting practices and systems:

- a. **Funding system**

In strong equity markets, such as the United States and the United Kingdom, accounting has a focus on how well management runs the company (profitability) and is designed to help investors analyze future cash flows and the associated risks. In a credit-based system where banks are the main source of funding, accounting has a focus on protecting creditors through conservative accounting measures in minimizing dividend payments and maintaining adequate funding in order to protect borrowers.

- b. **Legal System**

The legal system determines how individuals and institutions interact. The western world has two basic orientations, namely the codification of law (civil) and general law (case). The legal codifications are mainly drawn from Roman law and the Napoleonic code. In countries that follow the Latin-Roman legal codification system, law is a complete group that includes provisions and procedures.

- c. **Taxation**

In most countries, tax regulations effectively define accounting standards because companies must record revenues and expenses in their accounts to claim them for tax purposes.

- d. **Political and Economic Ties**

Accounting ideas and technologies were transferred through conquest, trade and similar powers. The double-entry system that began in Italy in the 1400s gradually spread in Europe along with other rannaissance ideas.

e. Inflation

Inflation obscures historical accounting costs through excessive decreases in asset values and related expenses, while on the other hand, excessive increases in income.

f. Economic Development Level

These factors affect the types of business transactions carried out in an economy and determine which ones are the most important. In turn, the type of transaction determines the accounting problem at hand.

g. Level of education

Sophisticated accounting standards and practices are useless if they are misinterpreted and misused. For example, complex technical reporting on variance in cost behavior is meaningless unless the reader understands cost accounting. Disclosure regarding the risk of derivative securities will not be informative unless it is read by a competent party. Professional accounting education is difficult to achieve if the level of education in a country in general is also low.

h. Culture

Here culture means the values and behaviors shared by a society. Cultural variables underlie the institutional arrangements in a country (such as the legal system). Hofstede underlies four dimensions of national culture (social values) namely individualism, power distance, uncertainty avoidance, and masculinity.

4.1.4. The Influence of Culture on the Accounting System in Financial Reporting

The applicable financial reporting in a country is determined through government regulations, or other authorized private bodies (Nasution et al., 2021). The rules in a country's financial reporting are regulated in its accounting standards (Yulisfan et al., 2021). Similar to Indonesia, where accounting standards are regulated in Financial Accounting Standards (SAK) set by the Indonesian Institute of Accountants (IAI). From several observations made by researchers, it appears that there are differences in accounting standards that apply in each country. And this difference, there must be harmonization in accounting standards. Where, if a company will sell its shares in another country through the capital market. Then it will be able to determine the accounting standards used in financial reporting.

- Research Development

The following is a description of research that examines the influence of culture on the accounting system in financial reporting.

- a. Hofstede's Models (1980, 1987)

Hosfede conducted research by studying the relationship between 4 dimensions of culture, namely external factors, ecological factors, social values and institutional impacts. And described as follows.

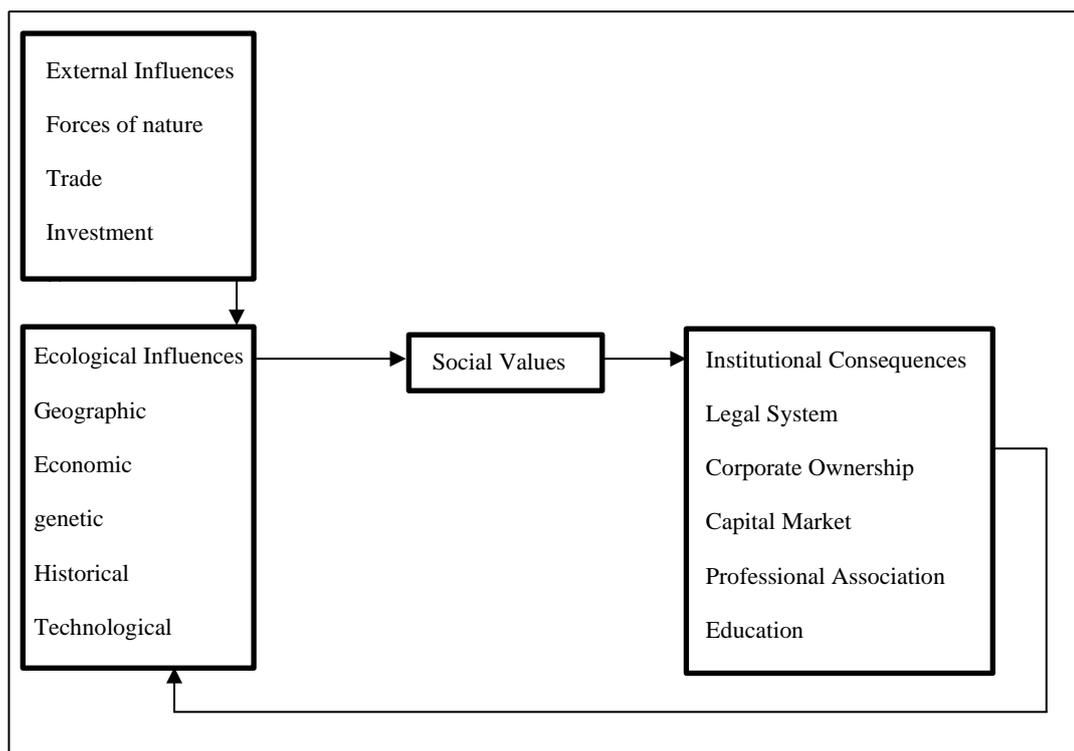


Figure 1. Hofstede's (1980) model

Hofstede set 4 indexes in his research that describe the cultural characteristics of each country. The four indexes are as follows:

1. Uncertainty Avoidance Index (UAI), which is the degree of discomfort/rejection of certain community members towards things that are uncertain or ambiguous.
2. Masculinity Index (MAS) This index describes the degree of "femininity" of a society, namely the preference for relationships with one another, modesty, helping the weak, and quality of life.
3. Power distance Index (PDI), which is the tendency of the community to accept the power gap in the company.
4. Individualism Index (IDV), which is the degree of people's behavior to be more concerned with themselves and their closest family than others.

Hofstede (1987) confirmed that accountants are the result of the world of society (social world) and not a mere technical system. And accounting is also an area where rules occur because of conventions in society (not natural laws like exact science). Thus it is not surprising that the accounting system will vary in each country, because each country has a different culture.

b. Gray Models (1988)

Gray (1988) the relationship between culture on accounting systems and accounting practices, especially in terms of financial reporting in his research. In Gray's model, several constructs and their relationships are examined, namely:

1. The accounting system is influenced by accounting values and the impact on institutions.
2. Institutions and Accounting values are influenced by social values
3. Social values are influenced by external and ecological influences.

Gray Model examines the relationship between common values in a country's culture and the professional values held by accountants in that country. Gray added 2 constructs which were developed from Hofstede's (1980) model, namely accounting value as part of the value accepted by society, and accounting system as part of institutional impact.

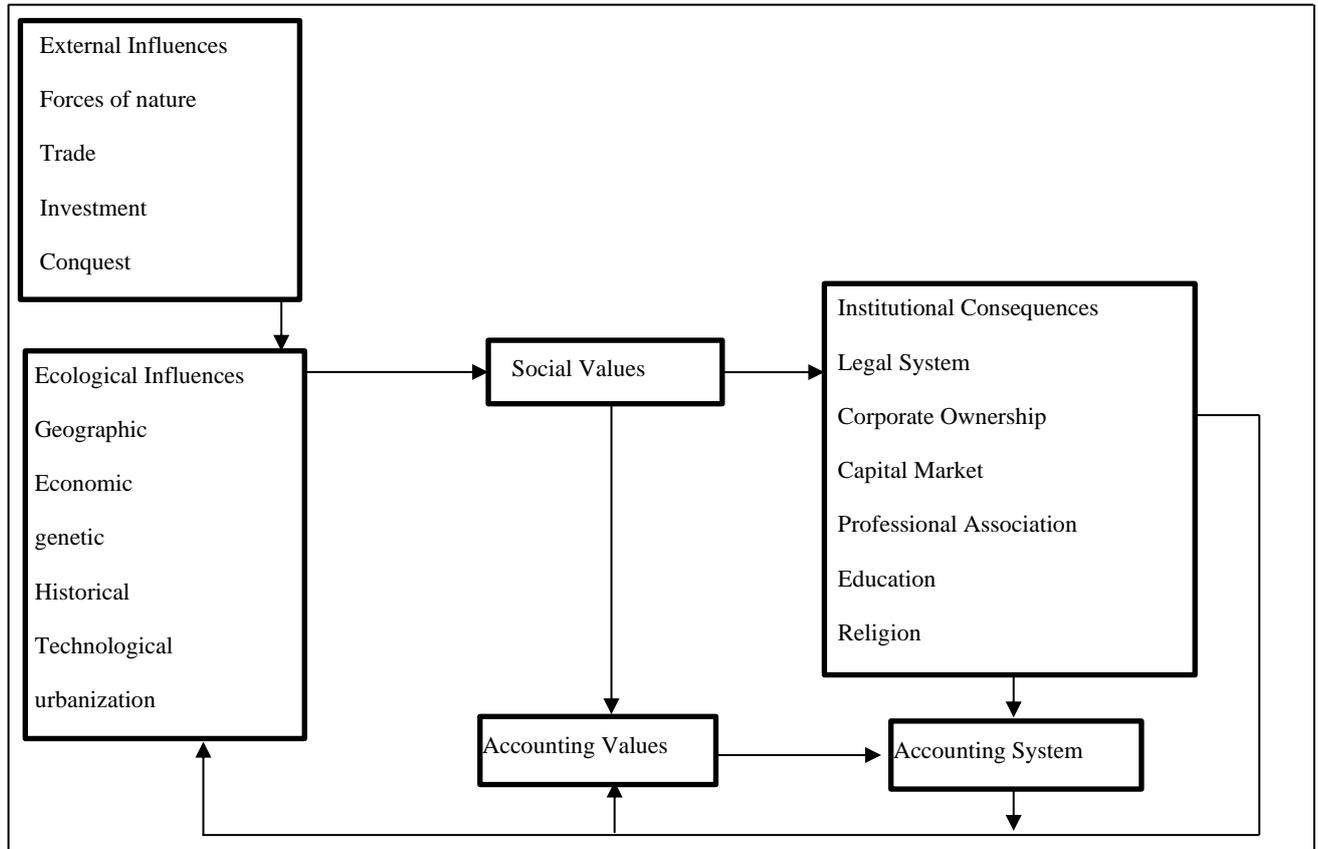


Figure 2. Gray Model (1988)

Gray's model reveals several things, namely as follows:

1. Accounting value is directly influenced by social values, and affects the accounting system. Accounting values are values that are embraced by practitioners (accountants) in carrying out their profession.
2. The accounting system is influenced by institutional consequences. The accounting system in this model is the accounting standards set by the government and professional organizations.

c. Verma-Gray (2006) Model

Verma-Gray (2006) proposes a model that describes the influence of culture on the accounting system and is an amalgamation of the model of Gray and McKinnon (1986) whose model reveals that financial reporting is seen as a social system whose functions are carried out by social institutions such as government, professional organizations and so on. The accounting system is seen as a link of authority between these social institutions. The model is described as follows.

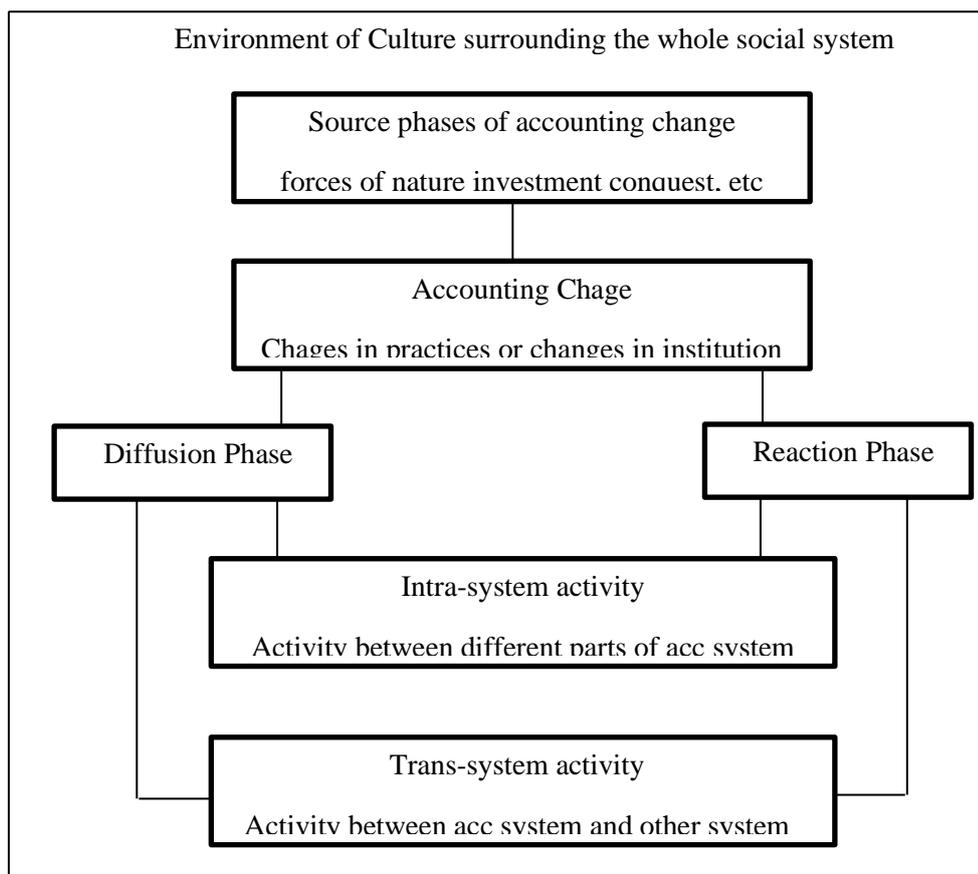


Figure 3. Verma-Grey (1997)

This model is mostly based on the McKinnon model which is characterized by the terms source phase, diffusion phase, reaction phase. Gray model is also applied to this model by incorporating external factors into the source phase. This model can be used to study the development of accounting in a country. The Verma-Grey model examines the development of accounting in the 1990s when India underwent significant political and economic changes.

4.1.5. Harmonization and Accounting Standards

Since 2005, the accounting standards issued by the IASB have been effectively applied. Where in recent years many countries have adopted this accounting standard. And the reason why adopting the accounting standards issued by the IASB is the consideration that different countries' accounting rules can generate significant advantages and disadvantages.

Accounting harmonization is one of the most important issues faced by accounting standard makers, capital market regulatory agencies, stock exchanges, and preparing or using financial reports. Harmonization is a process to improve the compatibility of accounting practices by setting limits on how much these practices can vary. Nobes and Parker (2004) distinguish between harmonization and accounting standardization. Harmonization is the process of increasing the suitability of accounting practices by setting limits on the degree of difference. While accounting standardization is the application of a more stringent set of rules and a narrower scope of harmonization. These two terms are often interpreted in international accounting although harmonization is more flexible than standardization.

Nobes (2008) in understanding financial statements globally and having an adequate basis for comparing financial accounting numbers is the rationale for the international standardization of

financial accounting. And the interpretation of financial accounting information is more effective because all estimates are prepared using the same underlying assumptions and accounting rules.

4.2. Discussion

Many different countries along with the accounting standards used are also different, with different mechanisms, different capital markets, different cultures and so on which will also lead to standardization of accounting practices. And this is the main assumption of the IASB. There are various reasons why international differences will persist after the introduction of IFRS which are as follows:

- a. Differences in the tax system.
- b. Differences in economic and political influence on financial reporting.
- c. Modification of IFRS at the national level.
- d. Differences in the implementation, supervision and enforcement of the law.

There are many reasons that cause differences in accounting methods from different countries. Mueller (1968) revealed that differences are caused by differences in the laws that underlie the country, the political system and or the level of economic development of a country. And other factors such as the tax system, education level, level of economic development and other factors also explain the differences in the history of accounting practice (Lubis et al., 2021).

Culture is a general concept that is expected to have an impact on the legal system, so that in the tax system, the way businesses are formed and financed and so on. Culture has been used in the psychological, anthropological and sociological literature as a basis for explaining differences in social systems. The accounting value system originates and is related to social values (Bakar et al., 2021). Where this social value also has an impact on the development of the accounting system on a national scale.

Harmonization and Standardization in improving the compatibility of accounting practices and the application of standards or rules in financial statements has several reasons why these two things are needed, namely as follows:

- a. Investors will be more efficient and effective in making investment decisions.
- b. Simplified accounting procedures.
- c. It is more flexible to use an accountant or auditor (Warae Et Al., 2021).

Besides the reasons it is needed, there are also some challenges in this harmonization and standardization as follows:

- a. Cultural and institutional differences.
- b. Lack of professional accountants in some countries.
- c. Accounting regulations have economic consequences.

5. Conclusion

Financial reporting has an important role in the accounting process. To maintain the objectivity of the contents of financial reports, each country sets financial reporting standards, either through government regulations, professional organizations or other institutions authorized by the government. Culture is considered as one of the main factors that cause the diversity of these standards. In addition to the culture that affects the reporting system is the occurrence of changes in the company's operating activities. Some of these changes can be reported directly in the financial statements, but some cannot be reported because the standards are not yet clear. This requires complete disclosure (disclosure).

REFERENCE

- Bakar, E. A., Nedelea, A., & Wardhani, M. M. (2021). The Influence of Using SAP CRM On Increasing Customer Satisfaction Index at Pt. Bank X In Medan, Indonesia. *The USV Annals of Economics and Public Administration*, 21(1).33-44.
<http://annals.seap.usv.ro/index.php/annals/index>

- Gray, S. J. (1988). Towards a theory of cultural influence on the development of accounting systems internationally. *Abacus*, 24(1), 1-15.
- Harrison, G. L., & McKinnon, J. L. (1986). Culture and accounting change: A new perspective on corporate reporting regulation and accounting policy formulation. *Accounting, Organizations and Society*, 11(3), 233-252.
- Hofstede, G. (1980). Culture and organizations. *International studies of management & organization*, 10(4), 15-41.
- Lubis, P. D. K., Lubis & Nedelea, A. M. (2021). Management Process Administration In Enterprise Resources Planning (ERP) Systems Applications and Products In Data Processing (Sap) In Ptpn Iii Sei Dadap. *Ecoforum Journal*, 10(1). <http://www.ecoforumjournal.ro/index.php/eco/article/view/1203/761>
- Lubis, P. D. K., Lubis, I., & Nedelea, A. M. (2021). Management Process Administration in Enterprise Resources Planning (ERP) Systems Applications and Products In Data Processing (Sap) In Ptpn III Sei Dadap. *Ecoforum Journal*, 10(1).1-6.
- Manullang, Poltak. (2008, March). The Influence of Culture on the Accounting System in Financial Reporting. *Journal of Economics and Business*. 2(1), 1-13
- Nasution, A. P., Muda, I., Iskandar, R., & Abubakar, E. (2021). Identification of Success Strategies for E-Government Services in Medan City. In *BICED 2020: Proceedings of the 2nd EAI Bukittinggi International Conference on Education, BICED 2020*, 14 September, 2020, Bukittinggi, West Sumatera, Indonesia (p. 230). European Alliance for Innovation. <http://dx.doi.org/10.4108/eai.14-9-2020.2305668>.
- Nasution, D. A. D., Muda, I., Sumekar, A., & Abubakar, E. (2021, March). Analysis of The Economic Behavior of Society E-Commerce as An Impact on The Development of The 4.0 Industrial Revolution and Society 5.0. *BICED 2020: Proceedings of the 2nd EAI Bukittinggi International Conference on Education, BICED 2020*, 14 September, 2020, Bukittinggi, West Sumatera, Indonesia (p. 217). European Alliance for Innovation. <http://dx.doi.org/10.4108/eai.14-9-2020.2305669>
- Nobes, C. (2008). Accounting classification in the IFRS era. *Australian Accounting Review*, 18(3), 191-198.
- Perbawasari, S., Dida, S., Nugraha, A. R., Sjachro, D. W., & Muda, I. (2019). Indung/Parent Management Communication Model to Establishment of Tourism Identity Based On Sundanese Cultural Values. *GeoJournal of Tourism and Geosites*, 27 (4), 1201–1211.
- Radebaugh, L. H., Gray, S. J., & Black, E. L. (2006). *International accounting and multinational enterprises*. John Wiley & Sons.
- Verma, S., & Gray, S. J. (2006). The creation of the Institute of Chartered Accountants of India: the first steps in the development of an indigenous accounting profession post-independence. *Accounting Historians Journal*, 33(2), 131-156.
- Warae, Y., Sigalingging, E. D., Abubakar, E., & Nedelea, A. M. (2021). Revealing Auditor and Auditee Satisfaction In The Evolution Of Accounting Software (Phenomenology Study In The Regional Government Of South Nias District). *Ecoforum Journal*, 10(2). <Http://www.Ecoforumjournal.Ro/Index.Php/Eco/Article/View/1210/744>
- Wardhani, M. M., Padang, N.N & Nedelea, A. M. (2022). Indicators of Giving Interest Rates to Customers and Debtors at PT. Bank X in Medan, Indonesia. *Ecoforum Journal*, 11(1). 1-6. <http://www.ecoforumjournal.ro/index.php/eco/article/view/1284/789>
- Yulisfan, Y., & Nedelea, A. M. (2021). The Evolution of Payroll Software That Can Replace The Manual Method In Indonesia. *Ecoforum Journal*, 10(2).1-6.
- Yulisfan, Y., Muda, I., & Nedelea, A. M. (2021). Implementation of Digitalization On The Revenue Cycle To Improve The Quality Of Decision Making More Timely In Indonesia. *Ecoforum Journal*, 10(3). <http://www.ecoforumjournal.ro/index.php/eco/article/view/1217/762>

CHAPTER 14

How Challenging Should Financial Performance Targets Be?

Al Wahfi Suhada Sipahutar¹, Ermadayani², Iskandar Muda³

^{1,2,,3}Universitas Sumatera Utara, Medan, Indonesia

¹ Email: alwahfi@student.usu.ac.id

ABSTRACT

To measure financial performance, financial ratios are needed. Financial ratios are one of the methods of financial analysis used as an indicator of the company's development assessment, by taking data from financial statements during the accounting period. So that it can be seen the maximum financial performance of the company. Financial ratios offer a way to evaluate their company's performance and compare it to other similar businesses in their industry. In addition, this ratio is often used by company management for making decisions related to saving company assets so that they do not take wrong steps in making decisions.

Keywords : Measure Financial Performance, Financial Ratios, Accounting Period, Development Assessment

. INTRODUCTION

Financial performance is an evaluation of a company regarding assets, liabilities, equity, costs, revenues, and overall profitability. Financial performance is measured through various formulas and formulas that allow to determine the effectiveness of the company. Internally, financial performance is examined to determine the company's current benchmarks or achievements. For externals, financial performance is analyzed to determine potential investment opportunities and to determine whether a company is feasible for these external parties. Companies and interested groups such as managers, shareholders, creditors, and tax authorities seek to answer important questions.

Financial performance is a description of the economic results that can be achieved by the company at a certain time through the company's activities. These activities are recorded and summarized into information that can be used as a medium to report the condition and position of the company to interested parties, especially creditors, investors, and the company's management itself.

Information that is presented correctly in a financial report will be very useful for companies in making decisions and to determine the company's financial performance. To explore more information contained in financial statements, an analysis of financial statements is needed. Performance measurement can be done using a measuring instrument called a ratio. Financial ratio analysis is the process of determining the important operating and financial characteristics of a company from accounting data and financial statements. Financial statement analysis predicts what may happen in the future, so this is where the financial statements are needed.

Analysis of financial data reflected in financial statements is needed to measure progress in generating profits effectively and efficiently. Ratio analysis allows interested parties to evaluate the financial condition that will indicate the health condition of a company. The ratio analysis used will be the basis for the company in evaluating the performance of the company's management and financial management to obtain the resulting profit. Financial statement analysis uses ratio calculations in order to evaluate the company's financial condition in the past, present, and future. Ratios can be calculated based on the data source consisting of balance sheet ratios, namely ratios compiled from data derived from the balance sheet, profit and loss statement ratios compiled from data derived from profit and loss calculations, and ratios between reports that compiled from balance sheet data and income statement. Financial statements need to be prepared to find out whether the company's performance is increasing or even decreasing and in analyzing financial statements financial analysis tools are needed, one of which is by using financial ratios.

2. LITERATURE REVIEW

One way that can be used to assess the performance of a company is by analyzing and calculating the company's financial ratios. A ratio does not have its own meaning, but must be compared with other ratios so that the ratio becomes more perfect.

According to Kasmir (2015) financial ratios are activities to compare the numbers in the financial statements. Comparisons can be made between one component with components in one financial report or between components that exist between financial statements. Then, the numbers being compared can be in the form of numbers in one period or several periods.

According to Harahap (2015) financial ratios are numbers obtained from the comparison of one financial statement post with other posts that have a relevant and significant relationship.

According to the definition of financial ratios according to Irham Fahmi (2012:107), it is stated as follows: "This financial ratio is very important for analyzing the company's financial condition. Short- and medium-term investors are generally more interested in the short-term financial condition and the company's ability to pay adequate dividends. This information can be known in a simpler way, namely by calculating financial ratios that are as desired.

Financial performance according to Indriyo Gitosudarmo and Basri (2002:275) is a series of financial activities in a certain period that are reported in the financial statements including the

income statement and balance sheet. Financial performance according to Irham Fahmi (2014: 2) is an analysis carried out to see how far a company has implemented using financial implementation rules properly and correctly. Financial performance according to Sucipto (2003) is the determination of certain measures that can measure the success of an organization or company in generating profits. Meanwhile, according to IAI (2007) financial performance is the company's ability to manage and control its resources.

From the above understanding it can be concluded that financial performance is a formal business that has been carried out by a company that can measure the company's success in generating profits, so that it can see the prospects, growth, and potential for good development of the company by relying on existing resources. A company can be said to be successful if it has achieved the standards and goals that have been seen. From the above understanding it can be concluded that financial ratios are a mathematical calculation carried out by comparing certain items or components in financial statements that have a relationship for later which is intended to show changes in the financial condition of a company.

3. METHODS

To measure financial performance, financial ratios are needed. Financial ratios are one of the methods of financial analysis used as an indicator of the company's development assessment, by taking data from financial statements during the accounting period. So that it can be seen the maximum financial performance of the company. Financial ratios offer a way to evaluate their company's performance and compare it to other similar businesses in their industry.

In addition, this ratio is often used by company management for making decisions related to saving company assets so that they do not take wrong steps in making decisions. Financial ratios are made by measuring the relationship between two or more components of financial statements to obtain meaningful information about the company.

Numbers in a company's financial statements, such as balance sheets, income statements, and cash flow statements, are used to perform quantitative analysis and assess a company's liquidity, leverage, growth, margins, profitability, rate of return, valuation, and more.

Financial ratios are most effectively used to compare results over several periods. This makes it possible to track the company's performance from time to time and find if there are signs of problems.

Performing an analysis of financial ratios will provide two main benefits, including:

1. **Track company performance**
Determining financial ratios per period and tracking changes in their value over time is done to see trends that may develop in the company. For example, an increasing debt-to-asset ratio could indicate that the company is burdened with debt and may eventually face the risk of default.
2. **Make a comparative assessment of the company's performance**
Comparing financial ratios with major competitors is done to identify whether a company is performing better or worse than the industry average. For example, comparing returns on assets between companies helps the analyst or investor to determine which company is the most efficient use of its assets.

4. RESULT AND DISCUSSION

4.1. RESULT

The first problem setting financial performance targets is how difficult, or how challenging, setting them will be. For planning purposes, the budget target should be an unbiased best estimate. The budget target should be the same as the expected performance, namely: with a 50% chance of achieving it. The target will be the best decision-making view for managers who plan resource levels without (or less) the risk of over- or under-resourced activities.

Performance targets are related to the results control system. If a target is set incorrectly, or the target is set in the wrong way, the results control system will fail. Two important issues regarding financial performance targets relate to:

1. The amount that is in accordance with the challenges on the target needs to answer the question: is the target made challenging or made to ensure it is achieved? A budget with a high level of achievement has several advantages:
 - a. Increase manager commitment
 - b. Convincing projection protection
 - c. Manager's highest achievement
 - d. Reduction of intervention costs
 - e. Reduce game play
2. The role of subordinates in setting targets Another important issue in designing results control systems when targets are negotiated is the extent to which subordinates' influence is allowed in their target setting. Some organizations set their targets from the bottom-up to the managerial level. Allowing employees to be involved in the process of setting their performance targets can provide several benefits, namely:
 - a. Increase the manager's commitment to the achievement of targets
 - b. sharing information
 - c. Cognitive benefits

The following are some situations where a top-down targeting process can produce good results:

1. Targets can be effectively derived from a top-down process when top management has sufficient knowledge of the operating business and operational prospects to properly set challenging performance targets.
2. A second situation that can lead to top-down target setting is when top-level managers have information to evaluate relative performance. For example, they manage a large number of relatively homogeneous entities operating in a stable environment.
3. Top-down target setting is usually carried out in organizations where lower-level managers have less ability in terms of budgeting.
4. Upper management knows better how to set standards according to learning curve models that have proven accurate in the past or they are better informed about new technologies that can cause structural changes in the way work is done and can change business prospects, making historical performance standards obsolete.
5. Top-down targeting needs to be done to avoid bias, so that targets are not set too high or too low than they should be. Lower-level managers have a tendency to try to lower targets, because it can make it easier for them to achieve them so they can earn bonuses with less effort. There are also some managers who are overly optimistic, so they want high targets to show management their abilities.
6. The biggest top-down risk is, losing commitment from subordinates to achieve targets

4.2. DISCUSSION

Financial ratio analysis is important in the business world, especially for management, investors and potential investors. Through this analysis, investors can determine the amount of investment to be invested. In addition to investors, financial ratio analysis is also useful for the management itself, because it can be used to assess business development. Financial analysis is also included in the balanced scorecard, a tool to measure the company's performance, how effective the strategies that have been used to achieve competitive advantage. This activity is not only addressed to the management, but also to other parties such as investors or creditors. For them, financial ratio analysis becomes an assessment material for how healthy the company deserves to inject investment or loan funds to manage. Basically, financial performance reports are very useful for a company. Information that can be utilized in several ways, namely.

- a. Used as a basis for determining the company's strategy for the future.
- b. Measuring the achievements achieved by the company in a certain period that reflects the level of success of the implementation of its activities.
- c. Assess the contribution of a part in the achievement of company goals as a whole.
- d. The basis for determining investment policies in order to increase company efficiency and productivity.
- e. See the company's overall performance
- f. Provide guidance in making decisions and activities of the company in general and company divisions in particular.
- g. Financial performance can be assessed in several ways such as comparative analysis of financial statements, financial ratios, position tendencies, percentage per component, sources and uses of working capital, breakeven, sources and uses of cash, and analysis of changes in gross profit.

5. CONCLUSION

All company activities from a financial point of view are divided into two main forms of activity, namely; activities of companies that use funds (allocation funds) and activities of companies that seek/generate funds (raising funds) these two activities of companies are often called financial functions. When the company is so eager to carry out activities that use funds (allocation funds) but is hampered in finding/generating funds (raising funds), the company is said to be experiencing financial distress (financial distress). Continuing financial distress has resulted in various problems within the company. Therefore, managers are expected to have a good understanding of good financial performance. In addition, it is also expected that managers have knowledge of good financial performance analysis techniques so that they can overcome the company's financial problems

Apart from being a measuring tool for the health of a company, financial ratio analysis has other benefits, namely;

- a. See the trend of company performance in a certain period.
- b. Materials for evaluating company resources such as suppliers, equipment, production processes and even the employees themselves.
- c. As a reference for investors to choose companies.
- d. For consideration by creditors.
- e. Assess the effectiveness of the company's strategy in building a competitive advantage.
- f. Analysis of the company's internal strengths and competitiveness with competitors.
- g. As reference material for internal audit transactions that occur in companies from the financial, operational, or other sectors.
- h. Determine the fair value of the profits earned by the company.

Based on the points above, the role of financial statement analysis essentially has two roles; as material for consideration and evaluation by both business owners and internal parties such as creditors or investors.

References

Ahamed, W. S., Almsafir, M. K., and Al-Smadi, A. W. (2014). Does corporate social responsibility lead to improve in firm financial performance? Evidence from malaysia. *International Journal of Economics and Finance*, 6(3), 126-138.

Dewi, N. W., dan Candradewi, M. R. (2018). Pengaruh employee stock ownership plan, leverage, dan ukuran perusahaan terhadap kinerja keuangan perusahaan. *E-Jurnal Manajemen*

Unud, 7(9), 4774-4802.

Freeman, R. E., and Reed, D. L. (1983). Stockholders and stakeholders: A new perspective on corporate governance. *California Management Review*, 25(3), 88-106.

Hansen, D. R., and Mowen, M. M. (2007). *Managerial Accounting*. Boston: Cengage Learning.

Kamatra, N., and Kartikaningdyah, E. (2015). Effect corporate social responsibility on financial performance. *International Journal of Economics and Financial Issues*, 2(1), 157-164.

Leon, S. A. (2013). The impact of capital structure on financial performance of the listed manufacturing firms in sri lanka. *Global Journal of Commerce and Management Perspective*, 2(5), 56-62.

Malik, M. S., and Nadeem, M. (2014). Impact of corporate social responsibility on the financial performance of banks in pakistan. *International Letters of Social and Humanistic Sciences*, 21(9), 9-19.

Margaretha, F., dan Letty. (2017). Faktor-faktor yang memengaruhi kinerja keuangan perbankan indonesia. *Manajemen Keuangan*, 6(2), 84-96.

Mule, R. K., and Mukras, M. S. (2015). Financial leverage and performance of listed firms in a frontier market: Panel evidence from kenya. *European Scientific Journal*, 11(7), 534-550

Accounting Inquiries with New Approaches in the Post-Pandemic Era

Volume I

CHAPTER 15

Debt Contracting: Agency Cost of Debt (A Monitoring Actions Between Debtholders Against Managers)

Hasbi Aulia Siregar¹, Henri Wiliam Dhani², Iskandar Muda³

^{1,2,3} Universitas Sumatera Utara, Medan, Indonesia

¹ Email: hasbiauliasiregar@gmail.com

ABSTRACT

The agency relationship is a contract in which one or more people (principal) orders another person (agent) to perform a service on behalf of the principal and authorizes the agent to make the best decision for the principal. Agency costs of debt arise as a result of agency conflicts between shareholders and debtholders of public companies. The agency costs of debt arise when debtholders limit the use of their capital because they believe that management will take actions that are more favorable to shareholders than debtholders. The agency cost of this debt is one element of the cost of debt that will reduce the benefits of using debt. This research is a descriptive qualitative research that tries to discuss important points related to the agency costs of debt. This study will attempt to discuss how debt agency costs can arise and how to handle them.

Keywords : Agency Theory, Agency Conflict, Agency Cost of Debt.

1. INTRODUCTION

The company is seen as a set of contracts between company managers and shareholders. The principal or owner of the company submits the management of the company to the management (Imes & Anderson, 2021). Managers as parties who are given authority over company activities and are obliged to provide financial reports will tend to report something that maximizes its utility and sacrifices the interests of shareholders.

As company managers, managers will know more about internal information and company prospects than owners (shareholders) (Solomon, et al., 2021). So in the view of agency theory, there is no reason to believe that agents will always act in the principal's best interest (Davis, et al., 2021). This is because it is generally impossible for the principal or agent, at a zero cost level, to guarantee that the agent will make optimal decisions from the principal's point of view.

Each company has two sources of funding that come from internal and external companies (Eniola, 2021). The company's internal source of funds comes from retained earnings. The company's external sources of funds come from debt, bonds, stock issuance, and others. To continue the project, the company generally uses debt as the company's external funding if the funding from retained earnings is not sufficient for the company's activities. Behind that, the company has an obligation to repay the loan and pay the interest expense periodically (Wardhani et al., 2022). In addition, the use of debt that is too large will also cause new agency conflicts between shareholders and debtholders, resulting in agency costs of debt (Amstrong, et al., 2021).

Agency costs of debt are conflicts of interest that exist between shareholders and debtholders or creditors of the company as a result of management choices. Agency costs of debt are actions taken by debtholders to limit what management can do with their capital (Renjie, et al., 2021). This is because management has more information than debtholders. Therefore, to overcome this difference, debtholders must carry out monitoring actions against managers. Especially if debtholders think that management prefers activities that benefit shareholders than debtholders (Zhou, et al., 2021). However, as a consequence, monitoring actions will result in high monitoring costs.

Creditors as providers of funds face a large potential risk of information regarding the actual condition of the company before entering into an agreement with the company (Chu, et al., 2022). This causes creditors to be only willing to provide loans to companies if creditors can obtain reliable information through direct control and monitoring to guarantee the repayment of their loans by the company. However, if the loan has been granted and the creditor feels that the company's management is too concerned with the interests of shareholders rather than debtholders, then one of the actions that creditors can take is to limit the loans extended, increase the cost of debt, make debt contract agreements or withdraw all financing required. been done (Bahlous-Boldi, 2021).

Creditors can implement policies that increase the cost of debt or creditors can also make debt agreements because they are worried about agency conflicts. As is known, debtholders (creditors) in the company do not have any authority over the funds they provide (Nurjanah, et al., 2022). Instead, the company's management did it. When debtholders are concerned that management may make riskier decisions that benefit shareholders rather than debtholders. So the debt holder can impose restrictions as mentioned above to avoid potential principal-agent conflicts.

2. LITERATURE REVIEW

2.1 Agency Theory

Jensen and Meckling (1976) define a contract between one or more principals who delegate authority to another person (agent) to make decisions in running the company. The main principle of this theory is the statement that there is a performance relationship between the party giving the authority (principal), namely the owner (shareholder) and the party receiving the authority (agent), namely the company management, in the form of a cooperation contract.

Despite the fact that agency theory is very practical and popular, it has a number of drawbacks, as described by Eisenhardt (1989); Shleifer and Vishny (1997). This theory is based on a contractual agreement between the principal and agent for a finite or indefinite future period, in which the future is unknown. Contracts are supposed to solve agency problems, but have many weaknesses in practice, such as knowledge asymmetry, rationality, fraud, and transaction costs. The main interest of shareholders in the company is to maximize their profits, but their position in the company is limited (Hanum & Muda, 2020). The director's role is limited to monitoring managers and their further role is not clearly defined. So the manager is seen as a "leader" in this theory. Execution of the contract raises costs known as agency costs, namely costs incurred for managers to act in accordance with the owner's goals, such as making contracts or carrying out supervision.

This conflict can be caused by differences between shareholders who prefer high-risk investments with the hope of obtaining high returns, while management prefers investments with lower risks to protect their position (Tran, et al., 2017).

However, with the passage of time, agency problems have expanded to include other parties such as creditors or debtholders (Chu, 2017), majority shareholders, and minority shareholders, apart from principals and agents.

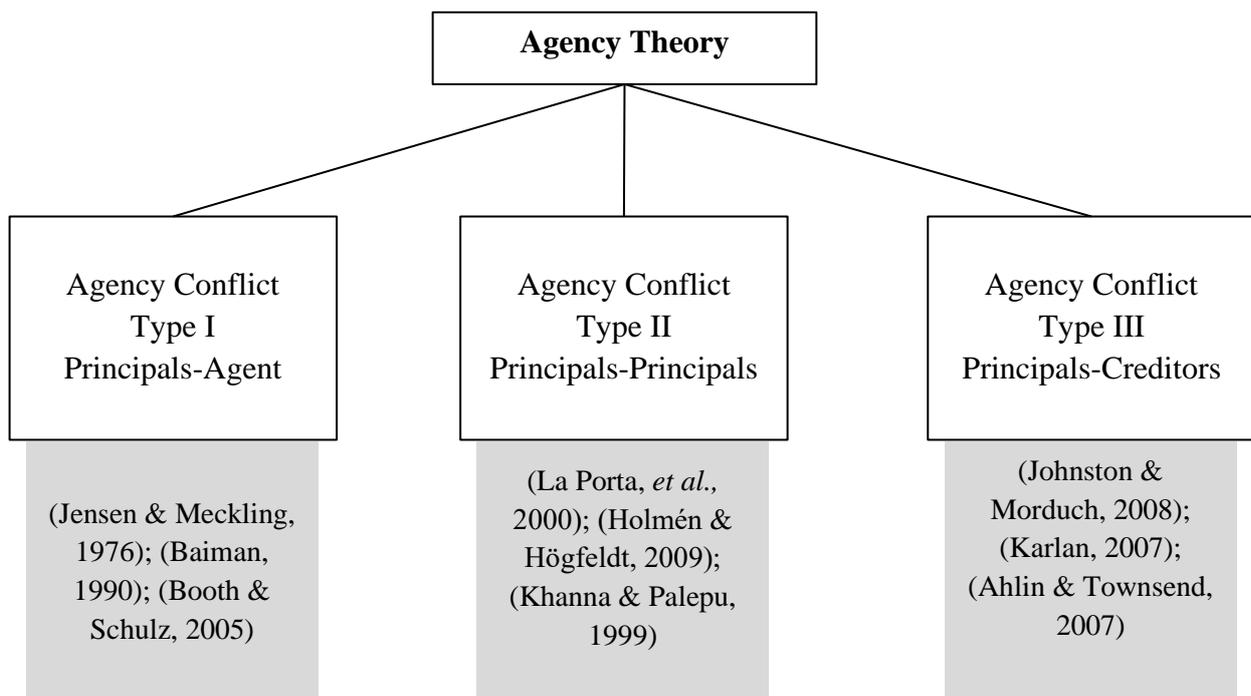


Figure 1. Agency Conflict

Researchers who have studied agency theory (especially agency conflict) have divided agency problems into three categories, as shown in Figure 1 above. Type I arises because of differences in attitudes between principals and agents (Jensen & Meckling, 1976). Type II conflicts arise when majority shareholders make decisions that are more favorable to them at the expense of minority shareholders (Gilson & Gordon, 2003) and it occurs when majority shareholders make decisions in their favor at the expense of minority shareholders. Type III agency problems occur when owners and creditors are at odds. This conflict arises when owners make riskier investment decisions and creditors consider this a threat to their financing.

Public companies are sophisticated machines with a wide variety of players. While all of these players want the company to thrive, certain actions benefit certain players more than others, resulting in a conflict of interest.

Various conflicts of interest in the company, whether between managers and shareholders, managers and creditors or between shareholders, managers and creditors, are caused by an agency relationship. Managers, for example, may wish to engage in harmful activities in the hope of benefiting shareholders seeking high returns (Charles, et al., 2021). While debtholders are usually looking for safer investments, debtholders may try to limit how their money is used to reduce risk. As a result of this conflict of interest, debt agency costs arise which refer to the costs incurred as a result of this conflict (Obeng, et al., 2021).

3. METHODS

This research is a qualitative research conducted with a descriptive approach. Analysis of qualitative research data has been carried out from the beginning of the research activity to the end of the study. In this way, it is hoped that there will be consistency in the overall data analysis. Considering that this research is descriptive in nature, it uses philosophical or logical data analysis, namely inductive analysis.

The inductive method is a method of thinking by drawing conclusions from certain data. Inductive thinking departs from specific facts, concrete events, then from certain facts or events, generalizations are drawn.

In this study, the inductive method is used to draw conclusions about things or events from data that has been collected through observation, and documentation, which can be generalized (drawn towards general conclusions), so it is clear that this inductive method is to assess empirical facts. Found then matched with existing theories.

4. RESULTS DAN DISCUSSION

4.1. Result

A. Cause-Risk Preference

The parties involved in the company certainly have different perceptions of risk and struggle for the decisions they make (Tran, 2021). So that this conflict can arise between shareholders and creditors. Decisions taken within the company will be based on risk. Individual behavior in dealing with risk will be different and can be classified into two categories, namely:

- a. Risk averse, which is the behavior of individuals who are afraid of risk and tend to avoid risk.
- b. Risk taker, which is the behavior of individuals who are willing to take risks.

Generally, shareholders will have a risk preference that is risk taker. So that shareholders will not hesitate to make decisions that have a high risk, while debtholders (creditors) will not like this (Pahi & Yadav, 2021).

Shareholders will try to invest in risky projects, where they expect higher returns. That is the nature of shareholders. While the risks involved in the project can increase financial costs and reduce the value of debt, so that it will affect creditors. If the project is successful, then the owner will enjoy a large profit, while the creditor's interest is limited because they only get a fixed rate of interest. On the other hand, if the project fails, then the creditors will be forced to share some of the losses and generally the problem continues under these circumstances.

B. Cause-Limited Earnings

Both managers and creditors of the company are significant stakeholders of the company, but they only have limited income because managers pay attention to their compensation, while creditors' income comes only from interest generated (Chu, 2017).

Creditors provide their capital to the company with a fixed interest rate for a certain period of time and the company is authorized to use it for a certain period of time in accordance with the agreed terms and conditions. So that shareholders and creditors both have a claim on the assets and income of the company.

Creditors have priority to receive interest and repayment of their principal. However, lenders invest their capital to earn a fixed rate of interest and to get the principal repaid only when it is due. Meanwhile, shareholders invest their capital to maximize the market price of their shares.

It is in the lender's interest to see sufficient income to cover fixed interest payments and timely principal payments. While creditors are not entitled to additional returns from the presence of additional risk, but they must bear the additional risk, which is taken by the company.

C. Cause-Information Asymmetry

Information asymmetry occurs because agents have better, complete and comprehensive information about their business than creditors (debtholders). High asymmetric information will mislead creditors in making credit decisions and even make it difficult for creditors to supervise, on the contrary, the lower the asymmetric information, the credit decisions made by creditors will be of higher quality and it will be easier for creditors to supervise the financing.

In conditions of relatively high asymmetric information, creditors cannot adequately monitor all actions taken by agents (management). Creditors are very difficult to know the activities carried out by the agent as a whole. If the agent's actions cannot be properly observed, then the creditor cannot design a contract based on that action

fairly. This phenomenon of high asymmetric information can occur due to weak financial system regulations, weak loan officers and risk assessment by creditors.

In addition, this information asymmetry can also be caused by the absence of an independent rating agency or the absence of an independent rating agency that can rate credit or loans granted to public companies.

As a consequence of asymmetric information, in addition to disturbing the quality of contracts and monitoring activities, creditors can also make mistakes in making credit decisions because creditors have difficulty distinguishing between good quality prospective debtors and poor quality debtors (prospective debtors).

Foreign creditors are often seen as creditors who have a more distant geographical position so that they have more potential to face high information asymmetry, foreign creditors certainly lack comprehensive knowledge and understanding of the condition of local debtors, so it is not easy to get complete and quality information. However, if foreign creditors are able to reduce asymmetric information by using modern information technology, operate at a more efficient cost, have a better supervisory system, then foreign creditors will certainly be able to overcome this agency conflict better (Mian, 2003).

However, this opinion is not entirely correct, because domestic creditors also face high asymmetric information because the credit business in Indonesia is a non-transparent business (yet), there is no rating agency that works for debtors optimally, obtain comprehensive and complete information.

D. Solution-Proper Budget Planning

Conflicts of interest between shareholders and creditors arise when managers make decisions to maximize shareholder value by ignoring the interests of creditors. Creditors are seen as principals and shareholders as agents in their agency relationship. Creditors, in general, provide their capital to the company at a fixed rate of interest for a certain period of time, and the company is authorized to use it for a certain period of time in accordance with agreed terms and conditions. Creditors have no say in the management and decision-making of the company.

Because shareholders want investments with high returns, managers acting on behalf of shareholders tend to acquire high-risk projects with the aim of generating high returns for shareholders. Meanwhile, creditors see a high risk of this strategy. On the one hand, creditors will only enjoy returns to the extent of the interest rate, while the rest of the investment returns on the project will be enjoyed only by shareholders. On the other hand, if this project investment fails, the company will be unable to pay its debts and interest. Therefore, creditors do not want the company to carry out investment projects like this. One way to overcome this is to implement appropriate budget planning (Kenno. et al., 2018).

D. Solution-Creditor Protection

Creditors can protect themselves by including restrictive terms and conditions in the credit agreement. This condition is set to maintain the company's debt service capacity. Restricting terms and conditions may include restrictions on share repurchases, capital structure restructuring, dividend policy decisions, and so on. In

addition, creditors can enter into agreements requiring mandatory management to maintain a certain level of working capital (Dao, et al., 2022). These terms and conditions will force shareholders through managers to act fairly with creditors.

Creditor protection agreements can be classified into two types, namely negative agreements and positive agreements. Negative agreements limit or prohibit actions a company can take, for example:

- a. Limitation of dividend payments that can be paid by the company.
- b. The company may not pledge its assets to other lenders.
- c. Companies may not merge with other companies.
- d. The company may not sell or lease its primary assets without the approval of the lender.
- e. or the Company may not issue additional long-term debt.

Whereas a positive agreement specifies the actions that the company agrees to take or the conditions the company must comply with. Examples of such agreements are:

- a. The company agrees to maintain its working capital at a predetermined minimum level.
- b. or the Company must provide periodic financial reports to the lender as an evaluation process.

E. Solution-Compensation for High Risk

When managers work for the company, they can be influenced by their own interests so that they prioritize their own interests over the interests of the company, on the contrary, the interests of creditors are to provide credit and get the principal and interest on time (Li et al., 2020). To ensure the return of their credit, lenders always pay attention to whether the company is doing business in the right way or not.

Creditors lend funds at a certain rate based on several factors. Here are some of them:

- a. Depending on the existing risk of the company's assets,
- b. Depending on expectations about the risk of adding assets in the future,
- c. Depends on the existing capital structure of the company (i.e. the amount of debt financing used), and
- d. Depends on expectations regarding future capital structure decisions.

This is a major determinant of a company's cash flow risk and its debt, so lenders will base their required rate of return on these factors.

Creditors have claims on a portion of the company's revenue streams as well as claims on company assets in the event of bankruptcy. However, shareholders have full control through the company's managers over decisions that affect the profitability and risk of the company. Indeed, neither shareholders nor managers have the right to expropriate wealth from creditors, because business is an ethical game (Abatino & Dari-Mattiacci, 2020). So that creditors feel that shareholders are trying to take advantage of them, creditors may refuse to have further dealings with the company. Or the lender may charge a higher interest rate to compensate for the increased risk. So that the problem between shareholders through managers and creditors can be solved by giving a higher risk premium to creditors for a high level of risk (Li, et al., 2020).

E. Alternative Solution – Managerial & Institutional Ownership

As an alternative solution, we offer that companies can use managerial and institutional ownership as a means to ensure that companies will be able to implement higher compliance with business ethics, compliance with applicable accounting principles and companies can also monitor expenses properly (González, 2018).

As is known, management must take the best business decisions to increase shareholder wealth. Where in the view of this theory management can be said to be a "leader". However, shareholders cannot monitor all decisions and activities carried out by managers. A threat to shareholders if managers will act in their own interests, not in the interests of shareholders. This is the basic problem in agency theory, namely the existence of a conflict of interest. A conflict of interest occurs if the manager's decision will only maximize his interests and is not in line with the interests of shareholders and debtholders (creditors). However, the decisions and activities of managers who own company shares will certainly be different from those of managers who are purely managers. Managers who own company shares mean that the manager is also a shareholder (Kao, et al., 2018). Managers who own company shares will of course align their interests with their interests as shareholders (Nugraha, 2021).

Meanwhile, managers who do not own company shares may only be concerned with their own interests (Mahoney & Mahoney, 2021). Ownership of company shares by managers is called managerial ownership. With their involvement as share ownership, managers will act carefully because they share the consequences for the decisions they make. In addition, with the involvement of share ownership, managers will be motivated to improve their performance in managing the company well.

In addition, institutional ownership will also encourage an increase in more optimal supervision of the performance of management. The higher the institutional ownership, the stronger the internal control over the company is expected, which will reduce the agency cost of debt in the company. The existence of this control will make managers use debt at a low level to anticipate the possibility of financial distress and corporate bankruptcy.

4.2. Discussion

Agency conflicts between shareholders, managers and shareholders are very common. However, it is different from the conflicts that occur over shareholders and creditors. There are various sources of conflict between shareholders and creditors. According to Gweyi, et al., (2013), high dividend payouts are the main source of conflict between them. Shareholders always try to maximize their wealth by asking for high dividends (Tran, 2019). While shareholder dividends increase, the interest paid to creditors remains the same. Furthermore, high dividends increase the market value of shares but decrease the market value of bonds. Therefore, maximizing shareholder wealth causes a decrease in creditor wealth. Second, conflicts arise through the choice of projects (Jerzemowska, 2006). Shareholders try to cause the company to implement risky projects with the prospect of high returns. However, lenders prefer low-risk projects/investments where the probability of success and loan repayment is higher. If the risky project is successful, shareholders will benefit from higher dividends as business performance improves while creditors cannot share the profits. They only receive fixed interest. However, if the project is not successful, the creditor must bear the loss. In addition, conflicts arise because shareholders encourage management to borrow more to finance projects/investments and pay dividends (Jerzemowska, 2006).

So that both shareholders, management, and debtholders (creditors) must have harmony so that problems between them can be muted. This study provides several solutions that can be offered to minimize conflicts that occur.

One solution that can be offered relates to determining the right budget planning. Budget is a process of planning and controlling the activities of a company's operations which are expressed in an operating activity of a company, which is expressed in an activity in units of money which aims to project the company's operations in financial projections. This budget planning needs to be made properly because it will have a big impact on the company. It not only threatens creditors, but also threatens the survival of the company so that shareholders must also pay attention to it. By establishing a good budget plan, both shareholders and creditors will both have bonds that can establish mutually beneficial relationships and will minimize debt agency costs that can arise.

Several other solutions that we offer are also related to the issue of creditor protection, providing compensation for high risk consequences that threaten creditors. As well as alternative solutions related to managerial ownership and institutional ownership so that the company can run properly so as to reduce conflicts between principals, agents and creditors.

5. CONCLUSION

We propose that in the contract the agency relationship between shareholders and creditors can actually be minimized, namely by prioritizing the relationship between the two by building a strong bond of trust. The solutions that we present in this study are expected to solve the problems that have existed so far. Problems regarding shareholders and creditors are indeed a frightening specter for the company, but on the other hand, creditors have a greater impact behind this conflict.

The conflict between creditors and shareholders (managers) is the most severe and the most important in the company. Conflicts between shareholders and debtholders (creditors) manifest themselves in the choice of projects to be taken (investment decisions) and in determining how to finance these projects and how much to pay as dividends.

REFERENCE

- Abatino, B., & Dari-Mattiacci, G. (2020). Agency Problems and Organizational. *Roman Law and Economics: Institutions and Organizations Volume I*, 273.
- Ahlin, C., and Townsend, R. M. (2007). Using Repayment Data to Test Across Models of Joint Liability Lending. *Economic Journal*, 117(517), F11-F51.
- Armstrong, C., Kepler, J. D., Kim, C., & Tsui, D. (2021). Creditor Control Rights and Executive Bonus Plans. *Available at SSRN 3975781*.
- Bahlous-Boldi, M. (2021). Agency Costs and Credit Availability: an International Study. *European Journal of Management and Business Economics*.
- Baiman, S. (1990). Agency Theory in Managerial Accounting: A Second Look. *Accounting, Organizations and Society*, 15, 341-371.
- Booth, P. & A. Schulz (2004). The Impact of an Ethical Environment on Managers, Project Evaluation Judgements Under Agency Problem Conditions. *Accounting, Organizations and Society*. 29: 473-488.

- Charles, V., Chi6n, S., & Gherman, T. (2021). Expert decision-making: A Markovian approach to studying the agency problem. *Expert Systems with Applications*, 184, 115451.
- Chu, Y. (2017). Shareholder Litigation, Shareholder–Creditor Conflict, and the Cost of Bank Loans. *Journal of Corporate Finance* 45: 318–332.
- Chu, Y., Lin, L. X., Saffi, P. A., & Sturgess, J. (2022). Shareholder-Creditor Conflicts and Limits to Arbitrage: Evidence From the Equity Lending Market. In *Proceedings of Paris December 2021 Finance Meeting EUROFIDAI-ESSEC*.
- Dao, T. H., Tran, Q. T., Nguyen, T. M., & Nguyen, T. S. (2022). Creditor Protection, Shareholder Protection, and Cost of Debt Financing Around the World. *Australian Journal of Management*,
- Davis, P. E., Bendickson, J. S., Muldoon, J., & McDowell, W. C. (2021). Agency Theory Utility and Social entrepreneurship: Issues of Identity and Role Conflict. *Review of Managerial Science*, 15(8), 2299-2318.
- Eisenhardt, K. M. (1989). Agency Theory: An Assessment and Review. *Academy of Management Review*, 14(1), 57–74.
- Eniola, A. A. (2021). The Entrepreneur Motivation and Financing Sources. *Journal of Open Innovation: Technology, Market, and Complexity*, 7(1), 25.
- Gilson, R. and Gordon, J. N. (2003). Controlling Shareholders. *University of Pennsylvania Law Review*, 152, 785-850.
- Gilson, R., & Gordon, J. (2003). Controlling Controlling Shareholders. *University of Pennsylvania Law Review*, 152(2), 785–843.
- González, F. (2018). Creditor Rights, Financial Health, and Corporate Investment Efficiency. *The North American Journal of Economics and Finance* 51: 100873.
- Gweyi, M. O., Ndwiga, P. M., & Karagu, J. M. (2013). An Investigation of the Impact of Co-Operative Movement in Rural Development in Kenya.
- Hanum, Z., & Muda, I. (2020). Effect of Tax Planning on Profit Management in Registered Food and Beverage Sub Sector Manufacturing Companies On the Indonesia Stock Exchange. *Junior Scientific Researcher*, 6(1), 48-57. https://www.jsrpublishing.com/userfiles/files/archive_pages/97/Article_Zulia_Hanum_Vol.VI_No.1_2020.pdf
- Holmén, M. and Högfeldt, P. (2009). Pyramidal Discounts: Tunneling or Overinvestment?. *International Review of Finance*, (9)1-2: 133-175.
- Imes, M., & Anderson, R. (2021). Executive Risk-Taking and the Agency Cost of Debt. *Journal of Empirical Finance*, 64, 78-94.
- Jensen, M., & Meckling, W. (1976). Theory of The Firm: Managerial Behavior, Agency Costs, and Ownership Structure. *Journal of Financial Economics*, 3(4), 305–360.
- Jerzemowska, M. (2006). The Main Agency Problems and Their Consequences. *Acta Oeconomica Pragensia*, 14(3), 9-17.
- Johnston, D., & Morduch, J. (2008). The Unbanked: Evidence from Indonesia. *World Bank Economic Review*, 22(3): 517-537.
- Kao, M. F., Hodgkinson, L., & Jaafar, A. (2018). Ownership Structure, Board of Directors and Firm Performance: Evidence from Taiwan. *Corporate Governance: The International Journal of Business in Society*.
- Karlan, D. S. (2007). Social Connections and Group Banking. *Economic Journal*, 117(517), F52-F84.
- Kenno, S. A., Lau, M. C., & Sainty, B. J. (2018). In Search of a Theory of Budgeting: A Literature Review. *Accounting perspectives*, 17(4), 507-553.
- Khanna, T. and Palepu, K. (1999). Emerging Market Business Group, Foreign Investor, and Corporate Governance. *NBER Working Paper 6955 (February)*.

- La Porta, R., Lopez-de-Silanes, F., Shleifer, A., and Vishny, R. W. (2000). Investor Protection and Corporate Governance. *Journal of Financial Economics*, 58: 3-27.
- Li, X., Wang, Y., & You, H. (2020). Executive Compensation and Conflict Between Shareholders and Creditors: Evidence from Creditor Litigation. *China Journal of Accounting Research*, 13(4), 405-424.
- Mahoney, P. G., & Mahoney, J. D. (2021). The New Separation of Ownership and Control: Institutional Investors and ESG. *Colum. Bus. L. Rev.*, 840.
- Mian, A. (2003), Foreign, Private Domestic, and Government Banks: New Evidence from Emerging Market, Graduate School of Business, University of Chicago, Chicago
- Nugraha, N. M. (2021). The Influence of Institutional Ownership, Managerial Ownership, and Board of Commissioners on Agency Costs. *Turkish Journal of Computer and Mathematics Education (TURCOMAT)*, 12(8), 1381-1387.
- Nurjanah, S., Ansari, T. S., & Daru, B. (2022). Legal Protection of Creditors in Credit Agreements with Liability Guarantee. *LEGAL BRIEF*, 11(2), 445-453.
- Obeng, V. A., Ahmed, K., & Cahan, S. F. (2021). Integrated Reporting and Agency Costs: International Evidence from Voluntary Adopters. *European Accounting Review*, 30(4), 645-674.
- Pahi, D., & Yadav, I. S. (2021). Product market competition, Agency Cost and Dividend Payouts: New Evidence from Emerging Market. *Journal of Management and Governance*, 1-32.
- Renjie, R. W., Xia, S., & Verwijmeren, P. (2021). Mutual Fund Dual Holdings and Shareholder-Creditor Conflicts. Available at SSRN 3735058.
- Shleifer, A., & Vishny, R. W. (1997). A Survey of Corporate Governance. *Journal of Finance*, 52(2), 737-789.
- Solomon, S. J., Bendickson, J. S., Marvel, M. R., McDowell, W. C., & Mahto, R. (2021). Agency Theory and Entrepreneurship: A Cross-Country Analysis. *Journal of Business Research*, 122, 466-476.
- Tran, Q. T. (2019). Creditors and Dividend Policy: Reputation Building versus Debt Covenant. *European Research on Management and Business Economics*. 25: 114-121.
- Tran, Q. T. (2021). Foreign Ownership and Cost of Debt Financing: Evidence from an Emerging Market. *International Journal of Emerging Markets*.
- Tran, Q. T., Alphonse, P., & Nguyen, X. M. (2017). Dividend Policy: Shareholder Rights and Creditor Rights Under the Impact of the Global Financial Crisis. *Economic Modelling* 64: 502-512.
- Wahyudi, R., Kaban, A.K, (2020). Liability Accounting (State Debt Management Analysis: Government Debt Management and Its Problems). *Turkish Online Journal of Qualitative Inquiry*. 11(4). 1108-1117. <https://tojqi.net/index.php/journal/article/view/8230>
- Wardhani, M. M., Padang, N.N & Nedelea, A. M. (2022). Indicators of Giving Interest Rates to Customers and Debtors at PT. Bank X in Medan, Indonesia. *Ecoforum Journal*, 11(1). 1-6. <http://www.ecoforumjournal.ro/index.php/eco/article/view/1284/789>
- Zhou, D. K., Sun, A. W., & Zhang, J. Y. (2021). Interpreting Agency Theory Through Greiner Growth Model: Regulatory Mechanism Reduces Agency Costs for Modern Chinese Enterprises. In *2021 5th International Seminar on Education, Management and Social Sciences (ISEMSS 2021)*. 819-828. Atlantis Press.

Accounting Inquiries with New Approaches in the Post-Pandemic Era
Volume I

EDITORS' BIOGRAPHIES

Prof. Dr. Iskandar MUDA

Prof. Dr. Iskandar Muda, SE, M.Si, Ak, CA, CPA is an Accounting Lecturer at the Faculty of Economics and Business, University of Sumatera Utara (2002 - Until Now), he is included in the AD Scientific Index (Alper-Doger Scientific Index) 2022 World Scientist Ranking list. Based on the release of AD Scientific Index , Iskandar Muda is ranked 7906 in Asia and ranked 18 in Indonesia.

The list is based on the accumulation of various scientific papers assessed from the H Index, I Index and citations indexed by Google Scholar. The H Index is an index that attempts to measure both the productivity and impact of a scientist's published work. This index is based on the number of scientific papers produced by a scientist and the number of citations received from other publications.

While the I Index is the score of a researcher in a publication that has articles cited by at least 10 other articles. Citation is the number of scientific works that are cited or cited by other people around the world and become a source of reference for scientific works. This list is a form of recognition by world institutions for the achievements of the work given by scientists.

The AD (Alper-Doger) Scientific Index is a study that shows the total and productivity coefficients of publication performance over the last five years of scientists, based on H-Index scores and citations according to Google Scholar. The index provides a ranking and assessment of scientists in a field of study and academic branch from 14,120 universities and 215 countries.

He is also active in professional organizations such as the Indonesian Institute of Certified Public Accountants (IAPI), the Indonesian Institute of Accountants (IAI), the Indonesian Bachelor of Economics Association (ISEI), the Institute of Certified Sustainability Practitioners (ICSP) Netherland and the International Public Sector Accounting Standards (IPSAS), USA. . As for his achievements, he was the winner of the USU No.1 Productive Researcher Award in 2017 and the 2nd most author in the field of Social Science, Humanities and Art in the database at Scimago, Scopus as of September 2021.

In addition to being active as a lecturer in Masters & Doctoral Accounting programs, Uuniversity of Sumatera Utara, he is also active as a regional finance researcher, speaker of Technical Guidance (BIMTEK) and practitioner accountant at City District in North Sumatra. Some of his research has been published in indexed national and international journals and Intellectual Property Rights listed on Google Playstore.

Mr. Luigi Pio Leonardo Cavaliere

Luigi Pio Leonardo Cavaliere is a dedicated and active researcher affiliated with the University of Foggia, Italy. He authored and co-authored numerous research projects and articles indexed on both Scopus and Google Scholar. Luigi joined important international research teams, continuously contributing to successful research projects and publications in Banking, Accounting, Finance, and Management Information Systems. Regardless of his young age, he frequently served as a member of the organisation committees at international conferences, co-editor and reviewer for scholarly blogs and international academic journals. Beyond the scholarly scope, his skills are also extended to the professional field to include the qualification of IT specialist, certified by Microsoft and Certiport. He is about to complete his mandatory professional apprenticeship and yet to achieve his Professional Qualification as a Chartered Accountant in Italy.

Dr. Muhammad Ali TARAR (Ph. D Rural Sociology)

Dr. Muhammad Ali Tarar joined University of Agriculture, Faisalabad- Pakistan as Teaching Assistant in 2005, later as, Lecturer Rural Sociology in November 2007 and presently serving the Department of Sociology, Ghazi University, Dera Ghazi Khan-Pakistan as Associate Professor / Chairman Sociology. Additionally, he is also serving as Director office of Research, Innovation & Commercialization (ORIC) from 2015. As Chief Editor, Kisht-e-Nau (student Magazine, University of Agriculture, Faisalabad) published Centennial Number in 2006 and was awarded UNIVERSITY GOLD MEDAL from Chancellor of University/ Governor of Punjab-Pakistan as well-as UNIVERSITY ROLE OF HONOR, UNIVERSITY COLOUR & UNIVERSITY CERTIFICATE OF EXCELLENCE was awarded from Worthy Vice Chancellor for publishing the Centennial Number of “ Kisht-e-Nau “ as Chief Editor on the eve of centenary celebrations of University of Agriculture, Faisalabad (14th to 16th March 2006). He has vast experience in teaching & research. Being Researcher published more than 40 research articles on different social & behavioral issues in National & International quality indexes/ impact factor journals that are recognized by Higher Education of Pakistan and at postgraduate level supervised more than one hundred research students and completed their research. He is also coauthor of book “Introduction to Sociology”. He is also external examiner of research / paper setter of many universities for postgraduate level as well as examination supervisor of Punjab Public Service Commission, Pakistan. Being Director ORIC made collaboration with sister universities and industries to develop academia to academia & Academia-Industry linkages for better knowledge and research sharing and signed more than 20 MOUs and strengthen the external linkages, developed a Business Incubation Center (Regional Plan9) & Women Development Center at Ghazi University with collaboration of Govt. of Punjab, Pakistan. He is Member selection/ recommendation Committee of Ghazi University to recommend BS-1 to BS-16 candidates to the Vice Chancellor for Approval of Appointment, Terms, and conditions of Services); Member Board of Faculty for a period of three years for faculty of Arts; Member Consultative Committee; Member Convocation Organizing Committee for 1st & 2nd Convocation of the Ghazi University; Convener University Disciplinary Committee ; Convener University Disciplinary Advisory Committee; Member Compliance Implementation Plan Committee (CIPC) to prepare Compliance Implementation Plan (CIP) in coordination with respective offices; Nominated as Focal Person to collaborate with QEC regarding IPE Review visit at Ghazi University; Member Affiliation Committee (to affiliate & Disaffiliate Govt. & Private Educational Institutes / colleges with Ghazi University); Member University Grievance Redress Committee; Member University Monitoring, Evaluation and Learning Committee; Member University Scrutiny Committee for Administration Posts; Member Standing Committee for vetting of non-schedule items with the term of Reference (TORs); Member Surveillance committee of Ghazi University; Member Online Quality Assurance (OQA) Task Force of Ghazi University; Members University General Purchase Committee; Member University Semester Rules Committee; Member Inquire committee about matter/ issue regarding allegations on social & print media against employees, Member University Prospectus Committee to prepare prospectus and Member University Admission Committee year 2019, 2020 & 2021; Focal Person Kamyab Jawan Innovation League; Member Plagiarism Standing Committee (PSC) Ghazi University; Member Self Institutional Performance Evaluation (IPE) Committee and Focal person to conduct quantitative research on Beggary in Punjab with collaboration of Department of Social Welfare, UCDP, D. G. Khan (December 2016 to To-date).

Doğrulama Kodu : f70b63cb-4c05-4132-bec8-804f1f8a5950

**T.C.
KÜLTÜR VE TURİZM BAKANLIĞI**



SERTİFİKA

FİRMA ADI : NCM MİMARLIK MÜHENDİSLİK İNŞ. SAN. TAAH. TİC. LTD. ŞTİ.
ADRESİ : ESENTEPE MAHALLESİ GÜVERCİN(160) SOKAK ŞENOCAK APARTMANI 2A
NİLÜFER/BURSA NİLÜFER / BURSA
VERGİ DAİRESİ : NİLÜFER VERGİ DAİRESİ MÜD.
VERGİ NUMARASI : 6270313993
FAALİYET ALANI : DAĞITIM (KİTAP, MÜZİK VB), İTHALAT, SATIŞ, YAYINEVİ
VERİLİŞ NEDENİ - TARİHİ : Yeni Sertifika Başvurusu - 30.07.2021

İş bu sertifika açık unvan ve adresi yazılı olan işyeri, 5846 sayılı Fikir ve Sanat Eserleri kanunu uyarınca yukarıda belirlenen alan/alanlara ilişkin faaliyet gösterir.

SERTİFİKA NO : 51898
GEÇERLİLİK TARİHİ : 30.07.2021 - 30.07.2025

 e-imzalıdır
Dr. Kamil ÖZER
Vali a.
İl Müdürü