CHAPTER I
INTRODUCTION

1.1 Background of the Study

Financial statements are fragment of the information that companies shows to the users and contribute with the balance of information between managers and investors. The process of elaboration for financial statements including management carry out a series of calculations and considerations based on deciphering the operation and choosing which accounting regulations to use (Grecco, Geron, Grecco & Lima, 2014). IFRS brought a lot of modification in the way the information contained in the companies' financial statements were declared. For instance, the preface of fair value principle, which is seen as the most significant implication of IFRS. Fair value principle attracts and instigate the researchers and generates several argues on the adoption of the standards (Bello, Abubakar & Adeyemi, 2016).

The IFRS implementation in 2012 is the proof of Indonesia's effort to open the opportunities of capital market in international level. It is also one of Indonesia's obligations as a member of G20 to adopt IFRS (Murtini & Lusiana, 2016). The adoption of IFRS is very important, which can be seen from the high quality of accounting standards of financial statements in the reporting process. The users of financial statements demanded for an honest and fair presentation of information stated about companies from the financial statements. But under the crisis period, it is disputable whether companies shows honest and fair position to all users of financial statements to make economics decisions (Baig & Khan, 2016). It is largely debated that IFRS can raise the accounting information quality due to their needs of accounting measurement and recognition, which are made to better reflect the financial and economic position of the companies. Therefore, the implementation of IFRS can lower the asymmetry in the cost of capital and information, and raise the capital flow across countries (Rathke, Santana, Lourenco & Dalmacio, 2016).

The action of earnings management can be minimized through a monitoring mechanism that aims to maintain a balance in the company called corporate governance. Corporate governance is a set of mechanism used to limit the emergence of agency problems. Corporate governance is the basis for increasing economic efficiency, which includes relationships between companies and stakeholder (Vincent, 2008). The board of directors plays an important role to ensure that the interests of shareholders and managers are balanced. Many parties start to assume that corporate governance is unable to provide oversight to managerial levels in conducting a healthy earnings management. This has caused the published financial statements unable to describe the actual state of the company (Rauf, Johari, Buniamin & Rahman, 2012).

There is one more important factor that lies behind the IFRS adoption, which is the value relevance. The management is expected to provide a high quality financial statements to the stakeholders of the company. The way to accomplish it is by providing a financial statements which is value relevant that will help the users to have a better understanding and accurate information of the company (Temile, Mohammed & Jatmiko, 2018). The value relevance is measured with the model price and is reflected in the stock price. The investors believe in the relevancy of the information when they use the information as a guide for decision making. The value relevance variable is able to measure the increasing quality of financial statements (Murtini & Lusiana, 2016).

However, there are only few studies done about the impact of IFRS adoption on value relevance. The previous study about this topic focused more on the developed countries. We will compare the value relevance pre and post convergence time to show the impact of IFRS adoption on value relevance. (Chebaane & Othman, 2014). It is important for investors to know which part of financial statements are values relevant to calculate the value of a company. Value relevance is the ability of the financial statements to help investors on their decisions. The results of this research will provide an evidence on whether the IFRS adoption has increased the quality of accounting (Umoren & Enang, 2015). From the background above, the author is interested in making a research with the topic **"The Impact of IFRS Implementation and Board Characteristics on Earnings Management and Value Relevance in Indonesia".**

1.2 Problem Statement

The growth of economic and globalization required the existence of an accounting standard that is internationally accepted and recognized by the world. IFRS convergence to Indonesia was first introduced by IAI on December 2008. It was set that starting from 1st January 2012, the companies which are registered in Indonesian Stock Exchange have to fully adopt IFRS. This regulation is implemented in order to increase the quality of the financial information (Mahesh, Yapa & Kraal, 2016).

Back then, many financial fraud has occurred due to the weak structures of the company. Some companies included in the financial fraud cases are large companies, such as Worldcom and Enron. This has caused a big chaos back then, and make the society lose trust on the companies (Kamran & Shah, 2014). Earnings management is the method carried out by management to achieve the desired target for personal interest. This practice is done by setting policies or methods of accounting records in determining the size of income (Francis & Schipper, 1999).

It is important to analyse how the managers realize their financial statements and if any differences between the accounting standards and the IFRS can be discovered when earnings management elements are taken into consideration. The adoption of IFRS is based on the fact that important improvement to financial reporting can be obtained by considering transparency and accounting quality. Moreover, the implementation of the new accounting requirements upon individual financial statements can both influence the profitability of the entity and the confidence that shareholders have in the result reported by manager (Brad, Dobre, Turlea & Brasoveanu, 2014).

The study about value relevance is conducted to measure the improvement of the quality and transparency of financial information. The reason to add value relevance is due to a change from rule based to principle based, which can enhance the relevance of financial information (Murtini & Lusiana, 2016). Investors only rely on the information in the financial statements in deciding whether to invest or not. Value relevance is important because it is seen as a way to measure earnings quality. The research regarding value relevance will be an important aspect for standard setters, policy-makers, internal and external users (Umoren & Enang, 2015).

1.3 Research Question

From the background study of this research, we can see that the questions in this research are as follows:

1. Is there a significant influence between IFRS adoption and earnings management?
2. Is there a significant influence between board size and earnings management?
3. Is there a significant influence between board independent and earnings management?
4. Is there a significant influence between earnings per share and value relevance?
5. Is there a significant influence between book value per share and value relevance?

1.4 Research Objective

Based on the background study of this research, the purposes of this research are as follows:

1. To know is there a significant influence between IFRS adoption and earnings management.
2. To know is there a significant influence between board size and earnings management.
3. To know is there a significant influence between board independent and earnings management.
4. To know is there a significant influence between earnings per share and value relevance.
5. To know is there a significant influence between book value per share and value relevance.

1.5 Research Contribution

Based on the background study of this research, the benefits of this research are as follows:

1. For Companies

   This research provides information on the impact of International Financial Reporting Standards (IFRS) adoption on earning management and provides an understanding of the factors that affect earning management after the implementation of International Financial Reporting Standards (IFRS).

2. For Investors

   This research is expected to provide an overview of the factors that affect earning management as reflected in the financial statements and assist investors in conducting information analysis in order to make the right economic decisions.

3. For Academics

This research is expected to enrich the knowledge and insight of accounting, especially on the factors that affect earning management. The result of this research complements the empirical findings in the field of accounting and can be used as references for further research development.

1.6 Systematic of Writing

The purpose of this systematic discussion is to present a general description of the content and discussion of every chapter included in the preparation of this thesis. The systematic discussion used in this thesis is presented as follows:

CHAPTER I INTRODUCTION

In this chapter, we talk about the background of the study, problem statement, research question, research objective, research contribution, and systematic of writing,

CHAPTER II THEORETICAL FRAMEWORK AND HYPOTHESIS

This chapter consists of two parts, which are the explanation of previous research and the definition of dependent variable and the model that underlies the research up to the formulation of the hypothesis.

CHAPTER III RESEARCH METHODOLOGY

This chapter contains the approaches and research methods used, which consists of: research characteristics, research objects, operational definitions of variables and measurement, data collection techniques, and data analysis methods. Data analysis methods include descriptive statistics, outlier test, panel regression with best model selection based on Chow test, Hausman test, F test, t test, and Goodness of Fit Model

CHAPTER IV ANALYSIS AND DISCUSSION

In this chapter, we discuss about test results of collected data, descriptive statistical analysis, outlier test results, regression test result along with an explanation on the results of the hypothesis tested.

CHAPTER V CONCLUSION, LIMITATION, AND RECOMMENDATION

This chapter is a concluding part of the research which summarizes the whole research, the findings obtained from the analysis and discussion of previous chapters, the limitations found in the research, and recommendations suggested to benefit researchers in future research.