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Financial Instruments Disclosure: Comparison of Indonesian and UK Banks

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Abstract The purpose of this study is to examine the financial instruments disclosure of banks in Indonesia and UK. Indonesia has started the IFRS convergence since 2008. One of the benefits of IFRS convergence is to increase comparability. However, this benefit of comparability can only be achieved if IFRS is credibly implemented across countries. One of the accounting standards that has adopted the IFRS is PSAK No. 60 *Financial Instruments: Disclosure* which was adopted from IFRS 7 *Financial Instruments: Disclosure*. This standard has significant effect on most Indonesian listed firms, especially banks. On the other hand, UK has fully adopted IFRS since 2005. We have compared the disclosure in noted to the financial statements of 5 Indonesian banks and 5 UK banks. The comparison highlights several differences in disclosure in both countries, where UK banks tend to disclose more comprehensive disclosure in their notes to the financial statements. These differences indicate that the disclosure is not fully comparable between banks in both countries, which in turn may limit the benefit of IFRS convergence.

Keywords IFRS, Convergence, Comparability, Financial instruments

1. Introduction

The process of IFRS (International Financial Reporting Standards) convergence in Indonesia has started since the end of year 2008. The objective of this process is to revise the PSAK (Indonesian-GAAP) to be materially aligned with the IFRS version January 1, 2009 which has been effectively implemented as of 2011/2012. This convergence process is resulted from the agreement of Indonesia government as the member of G20 forum. The G20 meeting which was held in London on April 2, 2009 brought 29 agreements that one of which was discussing the Strengthening Financial Supervision and Regulation:

"To call on the accounting standard setters to work urgently with supervisors and regulators to improve standards on valuation and provisioning and achieve a single set of high-quality global accounting standards"[1].

The first phase of IFRS convergence in Indonesia, to revise the PSAK to be materially aligned with IFRS version January 1, 2009, has been completely accomplished on the beginning of year 2012. Currently, the IFRS convergence in Indonesia is on the second phase. In this phase, DSAK aims to adopt the IFRS with only one year adoption time gap between the effective date of IFRS and PSAK.

According to IFRS implementation profile, it is evident that 130 out of 138 countries have made public commitments to apply IFRS as the single set of global accounting standard. What is more, out of 138 countries, a full amount of 114 countries have imposed the IFRS to either all or most of the large domestic entities that have to perform the public accountability[2]. Indonesia is classified as the country which national standard is substantially, or not fully, converged with IFRS[3].

The IFRS convergence process also includes several parties other than DSAK; the regulators, companies, auditors, and academicians. However, it appears that there has no comprehensive evaluation made on the IFRS convergence process. The IFRS convergence process results on several significant changes on many accounting standards. Specifically, the area of measurement, recognition, and also disclosure are extremely affected by the IFRS convergence process that these leads to significant changes of the principles. Muhammad & Siregar (2013) demonstrates that the average of segment disclosure in year 2010 and 2011 is 65% of the total segment disclosure according to PSAK 5. It indicates that companies' level of compliance to PSAK's

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[1] http://www.iaiglobal.or.id/v02/berita/detail.php?catid=&id=184, Retrieved on February 9, 2015.

[2] The entities with significant public accountability are listed companies, companies that are in the process to be listed, and financial institutions.

[3] http://www.ifrs.org/Use-around-the-world/Pages/Analysis-of-the-IFRS-jurisdictional-profiles.aspx, Retrieved on February 5, 2015.

disclosure stipulation is reasonably low. The evaluation of companies' level of compliance to converged PSAK, therefore, is utterly important to be performed.

This disclosure compliance will serve as one of the indication of how success is the implementation of IFRS convergence in Indonesia. In this study we only focus on PSAK No. 60 and IFRS 7 (Financial Instruments: Disclosure). Financial instrument accounting standards are one of the most complex accounting standards, therefore we only examine the disclosure related to financial instruments. We compare the financial instruments disclosure of Indonesian listed banks compare to UK listed banks. Comparability is one of the characteristics of high quality financial statements. Many literature stress the importance of comparability across financial statements in judging a firm's performance using financial ratios (De Franco et al., 2011).

We only focus on banks because banks are financial institutions that majority of their assets and liabilities are classified as financial instruments. UK was chosen as benchmark due to UK has fully adopt IFRS and considered as a good benchmark to examine whether Indonesian listed banks have fully comply financial instruments disclosure in accordance with IFRS.

According to the abovementioned discussion, it could be considered that the research quesitions from this study is to what extent do the companies comply to disclose their financial statements according to the PSAK converged with IFRS?

2. Literature Review

IFRS is issued by IASB, an International Accounting Standards Board headquartered in London, UK. IASB's objective to issue IFRS is "To develop a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles"[4].

According to IASB's website, there are 130 out of 138 countries in the world that have made public commitment to implement IFRS as the single set of global accounting standards. Amongst these countries, 114 countries have imposed the implementation of IFRS either for all or most of the large-scale domestic entities that have to perform public accountability[5].

Many countries around the world have implemented the full adoption of IFRS. For instance, the European Union has imposed the large-sized listed companies in EU stock exchange to implement the IFRS as adopted by the EU for their consolidated financial statements as of 2005[6].

On the other hand, some other countries implement the IFRS adoption gradually, this process thus allows to the notion of IFRS convergence. Indonesia is one of the countries that opt to implement the IFRS gradual adoption. IFRS convergence in Indonesia was initially planned at the end of year 2008 with the implementation target on year 2012.

One of the goal of IFRS convergence is the improvement in cross-firm comparability, with a general view that same accounting standards will lead to higher comparability (Lang et al., 2010). Nowadays, globalization has significantly increased the interaction among countries worldwide. This economic interaction has created an increased demand for more comparable accounting information. There are several benefits associated with enhanced comparability, including enabling global markets to operate with less friction as well as facilitates international transactions and reduces exchange costs (Yip & Young, 2012).

Comparability is one of the qualitative characteristics of financial statements which will increase financial statements usefulness to its users (IASB, 2010). Information comparability is ''the quality of information that enables users to identify similarities in and differences between two sets of economic phenomena'' (Financial Accounting Standards Board/FASB 1980; International Accounting Standards Board/IASB 2010).

Advocates of IFRS adoption claims that IFRS will increase financial statement comparability. However, IFRS will only increase comparability if it is credibly implemented (DeFond et al., 2011).

Several studies have been carried out to examine the appropriateness of IFRS convergence. Studies within this vein are primarily concentrates on the potential benefit of presenting financial statement accurately and comprehensively in a timely manner to reduce the differences of accounting standards within countries (Ball, 2006).

Barth (2008) identifies the challenges and opportunities arise from IFRS adoption in terms of education and research activities conducted by American academicians. It is demonstrated that there are several challenges exist: (1) a consistent interpretation and application of IFRS between countries; (2) the appropriateness of IFRS adoption by multinational companies in general and other companies in specific; (3) educate the market participants regarding the differences between IFRS and local GAAP; and (4) the changes from the local standard to IFRS for the purpose of reporting to regulator and auditing.

IFRS convergence presents both challenges and opportunities for investors, capital market, companies, regulators, and auditors. Saudagaran (2001) explains several advantages from the harmonization progress including: increases accounting information comparability, allows international investment inflow, and facilitates the preparation of consolidation financial statements.

Investors around the world consider that IFRS convergence is the mechanism that allows them to compare companies' financial statement from different countries. The

4 http://www.ifrs.org/The-organisation/Documents/2015/Who-We-Are-January-2015.pdf, retrieved on February 11, 2015.

5http://www.ifrs.org/Use-around-the-world/Pages/Analysis-of-the-IFRS-jurisdictional-profiles.aspx, retrieved on February 11, 2015

6http://www.iasplus.com/en/resources/ifrs-topics/europe, Retrieved on February 11, 2015.

implementation of IFRS will increase as long as the investors' demand of IFRS application grows. The IFRS convergence also acquiesce the cross-border investment and capital inflow. The significant benefit of the convergence for the companies throughout the world is the highly standardized accounting standard that it reduces the complexity, diversity, and probability of mistakes in preparing the financial statements. Moreover, for auditor, the IFRS convergence allows them to give audit opinion for financial statements based on one single accepted accounting standard (Rezaee, Smith, & Szendi, 2010).

On the other hand, the challenges in IFRS convergence is related with culture, legal and politic system, and also education, and implementation of IFRS. The regulator and standard setter encounter the challenges in reconciling the existing cultural, politic, and legal differences to be effectively implementing the IFRS (Rezaee, Smith, & Szendi, 2010).

Companies and auditors also find the constraint in implementing the principles-based IFRS insofar as it requires more professional judgement in its implementation. The companies and auditor also need to provide sufficient training and education for their employees that it requires a reasonably high cost. Another challenge appears is the difference between accounting standard with tax standard. Moreover, there is also the tendency of change resistance as the academicians and the practitioners are already accustomed with the local GAAP. On one hand, many of accounting study programs experiences the lack of educators with high qualification to teach IFRS curriculum. What is more, not every public accounting firm's employees obtain sufficient training to conduct financial audit process based on IFRS.

Several researches in accounting and financial vein denote that it is reasonably difficult to translate a language into another language (Doupnik & Richter, 2003). The IFRS which is originally drafted on English language based on certain concepts could not be directly translated to another language. As the standard setters in non-English speaking countries translate the English version of IFRS to local languages, it might be possible that there are misinterpretation during the translation process that it leads to the differences on accounting standard (Huerta, Petrides, & Braun, 2013). Apparently, the common mistake on translation process, often, is on the general terminologies rather than on accounting specific terminologies.

Several researches on financial statements have examined whether the companies oblige the IFRS' stipulation on financial statement measurement and/or disclosure. For instance, Street and Gray (2002) asserts that many companies around the world do not comply with IFRS. Numbers of researches also identify the factors that affect companies' compliance to IFRS. Zarzeski (1996) demonstrates that the disclosure presented by the companies that operate globally have several state-mandated disclosures. Other research suggests that the extent of disclosure is significantly higher for the companies who quote their shares on either American stock exchange or more than one stock exchange (Asbaugh, 2001). Muhammad & Siregar (2013) empirically demonstrate that the average of segment disclosure on year 2010 and 2011 is only 65% from the total of segment disclosure based on PSAK 5. This evident indicates that the compliance of public companies regarding the disclosure requirement on PSAK is considerably low.

3. Research Method

In order to conduct an analysis about the level of compliance of public companies to PSAK, the thorough examination of companies' financial statement will be implemented through content analysis method. This research will focus on the PSAK which has significant impact to companies: PSAK relating to financial instrument (PSAK 60 Financial Instrument: Disclosure) which is based on IFRS 7 Financial Instrument: Disclosure. For each disclosure item obliged on the aforementioned PSAK and IFRS will be compared to Indonesian and UK banks' 2014 financial statements.

4. Results

In order to compare financial instruments disclosure of listed banks in Indonesia and UK, we have selected 5 banks in each country. We choose large banks to conduct the analysis because larger banks tend to have more complex financial instruments. Below are the banks as a sample in our study:

Indonesia

1. Bank Mandiri (Persero) Tbk
2. Bank Rakyat Indonesia (Persero) Tbk
3. Bank Negara Indonesia (Persero) Tbk
4. Bank Central Asia Tbk
5. Bank Danamon Indonesia Tbk

UK

1. HSCB Holdings
2. Barclays PLC
3. Royal Bank of Scotland Group
4. Llyods Banking Group
5. Standar Chartered PLC

Based on our comparison, we notice that there are several differences in how banks in both countries disclosed the financial instruments in notes to the financial statements. UK banks tend to disclose additional quantitative information compare to Indonesian banks. For example:

Information disclosure on collateral asset: for Indonesian banks the disclosure is limited to the qualitative aspect through "Summary of Accounting Policy". In UK banks, there are detail disclosures on collateral assets (qualitative and quantitative).

Reclassification: Indonesian banks disclosed reclassification qualitatively on notes to the financial statement, whereas UK Banks the reclassification is disclosed qualitatively and the calculation is presented quantitatively.

For several disclosure items required in the standard, UK banks also tend to disclose more information. For example, the standard stipulate the special disclosures about financial assets and financial liabilities designated to be measured at FVTPL. Indonesian banks disclosure is limited to the qualitative aspect through "Summary of Accounting Policy" for quantitative information, it is required to consult to each note of financial assets and liabilities. On the other hand, UK banks' he disclosure is separated as stand-alone account in statement of financial position with the relatively extensive disclosure, including: basic valuation, adjustment, risk related adjustment, model/method of measurement, the disclosure and measurement is conducted based on the 3 level of input (including the reconciliation for the movement that includes the provision of credit risk effect), sensitivity analysis of the effect of changes in significant unobservable assumptions to reasonably possible alternatives (including the favourable and unfavourable effect of market risk), quantitative information about significant unobservable inputs in Level 3 valuations.

These differences in disclosure maybe due to institutional characteristics in both countries. Daske et al. (2008) and Li (2010) find that benefits of IFRS are more pronounced in countries with stricter enforcement regimes and therefore better IFRS implementation; stronger reporting incentives and therefore higher quality financial reporting.

5. Conclusions

Indonesia has started the IFRS convergence since 2008. One of the benefits of IFRS convergence is to increase comparability. However, this benefit of comparability can only be achieved if IFRS is credibly implemented across countries. One of the accounting standard that has adopted the IFRS is PSAK No. 60 Financial Instruments: Disclosure which was adopted from IFRS 7 Financial Instruments: Disclosure. This standard has significant effect on most Indonesian listed firms, especially banks. On the other hand, UK has fully adopted IFRS since 2005.

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The result has implications for regulators and standard setters. Regulators need to examine whether listed firms have fully comply with disclosure requirements in accounting financial standards. Standard setters and regulators should examine whether non compliance or limited disclosure may indicates that preparers may have obstacles in disclosing several required disclosure.

There are several limitations of our research. We only observe disclosure of 5 banks in each country. This may not represent the disclosure practices of all listed banks. We do not examine the usefulness of those disclosure for usefule of financial statements. More comprehensive disclosure does not necessarily means higher financial reporting quality nor useful for financial statements' users.

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