Incentives versus standards:
properties of accounting income in four East Asian countries

Ray Ball\textsuperscript{a}, Ashok Robin\textsuperscript{b}, Joanna Shuang Wu\textsuperscript{c,}\textsuperscript{*}

\textsuperscript{a}Graduate School of Business, University of Chicago, Chicago, IL 60637, USA
\textsuperscript{b}College of Business, Rochester Institute of Technology, Rochester, NY 14623, USA
\textsuperscript{c}William E. Simon Graduate School of Business Administration, University of Rochester, Rochester, NY 14627, USA

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Abstract

The East Asian countries Hong Kong, Malaysia, Singapore and Thailand provide rare insight into the interaction between accounting standards and the incentives of managers and auditors. Their standards derive from common law sources (UK, US, and IAS) that are widely viewed as higher quality than code law standards. However, their preparers' incentives imply low quality. We show their financial reporting quality is no higher than under code law, with quality operationalized as timely recognition of economic income (particularly losses). It is

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\textsuperscript{*}Corresponding author. Tel.: +1-585-275-5468; fax: +1-585-273-1140.

E-mail address: wjou@ssb.rochester.edu (J.S. Wu).

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misleading to classify countries by standards, ignoring incentives, as is common in international accounting texts, transparency indexes, and IAS advocacy.

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1. Introduction

Much attention is given in the academic and professional accounting literatures to accounting standards, how they vary across countries, and political and economic pressures to reduce variation. We view the focus on standards as substantially and misleadingly incomplete, because financial reporting practice under a given set of standards is sensitive to the incentives of the managers and auditors responsible for financial statement preparation. Preparer incentives depend on the interplay between market and political forces in the reporting jurisdiction. Market forces include the extent of demand for high-quality financial reporting (influenced, for example, by the amount of publicly traded equity, the size of the market for public debt, and the extent of private versus public contracting in the economy). Political forces include the extent of involvement of governments in codifying and enforcing accounting standards, taxes, and political incentives to reduce the volatility of reported income (i.e. to avoid large profits and large losses). These economic and political variables profoundly affect financial reporting practice.

The East Asian countries of Hong Kong, Malaysia, Singapore and Thailand provide a useful setting for testing the importance of preparer incentives.1 These countries have accounting standards that are generally viewed as high-quality, but (with the possible exception of Hong Kong) they have institutional structures that give preparers incentives to issue low-quality financial reports. We show that accounting standards and preparer incentives in these countries interact to produce generally low-quality financial reporting, consistent with the hypothesis that reporting quality ultimately is determined by the underlying economic and political factors influencing managers’ and auditors’ incentives, and not by accounting standards per se.

“Financial reporting quality” is an elusive concept, particularly in view of the multiplicity of uses of financial statement information. We operationalize the concept in terms of the timeliness with which economic income is recognized in accounting income. Economic income here is defined as change in the market value of equity, adjusted for dividends and capital transactions with shareholders. Timely accounting recognition of gains and losses in income implies timely revision of the book values of stockholders’ equity and of asset and liability amounts reported on

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1 We refer to Hong Kong as a country for simplicity. A more appropriate term might be “region,” due to its status as a British colony during our sample period and subsequent reversion to the People’s Republic of China.
balancesheets. Given the transitory nature of economic income (see below), the less timely that accounting recognition of economic income is, the more noise that is incorporated in individual income statement and balance sheet amounts, thereby reducing overall financial statement quality.2

Following Basu (1997) and Ball et al. (2000), we give particular attention to timely recognition of economic losses. There are several reasons for this asymmetry. First, managers generally possess private information about economic gains and losses (changes in expected future cash flows) that is unobservable to auditors. Their incentive to disclose gain and loss information is not symmetric, so auditors generally give greater credence to information about losses, and financial reporting tends to specialize in timely loss recognition. Second, managers can book economic gains and losses by selling assets and, without accounting recognition of unrealized gains and losses, they would have an asymmetric incentive to exercise the option to realize gains, not losses. Timely recognition of unrealized losses reduces that asymmetry. Third, timely loss recognition decreases the likelihood of managers making ex ante negative-NPV decisions, such as “trophy” investments or acquisitions, whose cash flow consequences extend beyond their tenure. Fourth, pricing of debt at its issuance is unlikely to be influenced substantially by timely incorporation of known gains and losses, but the post-issuance enforcement of coverage and leverage covenants is. Timely loss recognition transfers decision rights from loss-making managers to lenders more quickly, by earlier triggering of covenant violations based on financial-statement ratios. Economic gains do not trigger covenant violations, so debt contracts generate no demand for timely gain recognition. Thus, timely loss recognition increases the economic efficiency of firms’ contracting with both debt holders and management. We hypothesize that loss recognition is less timely in East Asian countries generally, where debt and managerial contracting is conducted more extensively through family or other “insider” networks, and due to political effects on financial reporting.

Our chief proxy for economic income is fiscal-year change in market value of equity. Researchers undoubtedly have differing views of the validity of this proxy, so we also perform a time-series analysis that does not utilize stock returns. This research design identifies transitory components in accounting income to identify incorporation of economic gains and losses (Basu, 1997; Ball and Robin, 1999). Consistent results are obtained from the two designs.

The notion that auditor and manager incentives influence choice among accounting standards is due to the seminal work of Watts and Zimmerman (1986). Our contribution is to study the case where standards and incentives conflict, to better understand the interaction between them. In essence, we study the effect of regulating accounting standards on the market for financial reporting, and conclude that market effects predominate.3

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2“Quality” here addresses the extent to which accounting information reflects the underlying economic situation of the firm. It is related to the concept of “transparency,” defined as the ability of users to “see through” the financial statements to comprehend the underlying accounting events and transactions in the firm.

3Subsequent to (and partly stimulated by) prior versions of this paper, several studies investigate the effects of various institutional factors on accounting earnings properties across different countries (for
The paper proceeds as follows. Section 2 describes the formal accounting standards and standard-setting institutions in the four East Asian countries. Section 3 describes preparers’ incentives in the region. Section 4 describes the sample and provides summary statistics, and results are presented in Sections 5 and 6. Section 7 outlines our conclusions, and implications of our results in several areas where it is important to consider incentives as well as standards.

2. Accounting standards and standard-setting institutions

A useful starting point is to classify countries into whether accounting standards predominantly originate in markets (i.e. common-law countries such as Australia, Canada, UK, and US) or in governments (i.e. code-law countries such as France, Germany, and Japan). Historically, there has been a strong common-law influence on accounting standards in the four East Asian countries, from the early British colonial influence to the more recent influence of IAS. In this section, we summarize the salient influences on the accounting standards of each country. The following section addresses the incentives facing managers and auditors in the region, which exhibit substantial code-law properties.

2.1. Hong Kong

Appendix A summarizes the chronological development of Hong Kong’s accounting system. Having been a British colony for over 100 years, Hong Kong is heavily influenced by UK standards and practices. The main accounting professional body is the Hong Kong Society of Accountants (HKSA), established in 1973. Before 1982, there was no formal standard setting in Hong Kong; the non-mandatory accounting standards issued in this period essentially were reissues of UK standards. In addition, most students took the UK Chartered Association of Certified Accountants (CACA) exams to satisfy the HKSA membership requirement. Formal standard setting structure was introduced in 1982. According to the

(footnote continued)
example, Ali and Hwang, 2002; Hung, 2001; Fan and Wong, 2002; Leuz et al., 2002) Their results generally are consistent with ours. In their investigation of earnings management activities around the world, Leuz et al. (2002) conduct cluster analysis, which classifies three of our four sample countries (Singapore, Hong Kong, and Malaysia) as “outsider economies” similar to the UK and US, due to historical common-law influence. In contrast, we classify them under the Asian version of the “insider” model, due to the prevalence of family control and networks in the region. Leuz et al. find that these countries have by far the worst earnings management ratings, which as they point out in the paper, is consistent with our arguments and our classification of the countries.

Hong Kong Accountant (1992), Hong Kong Statements of Standard Accounting Practice (SSAPs) issued before 1992 “were almost identical to the UK SSAPS”. Similar views were also expressed by Ernst & Young (1993) (reproduced in Appendix B). From 1992, the HKSA switched to IAS as the model for accounting standards. According to Price Waterhouse (1991 and 1995), the Hong Kong “SSAPs comply in all material respects with the applicable IASC statements” (see Appendix B).5

Another major source of authority in Hong Kong accounting comes from the Company Ordinance, which was first issued in 1932 and was based on the 1929 UK Company Act. Subsequent amendments to the Company Ordinance incorporated provisions from later UK Company Acts. Consistent with common-law concepts, the Company Ordinance requires that accounting information give a “true and fair” view.

2.2. Malaysia

Before its independence in 1957, Malaysia was under British rule for over 80 years, thus its accounting standards and reporting practices also originated in the UK. After IAS came into existence in the 1970s, they have taken over as the major force shaping Malaysian formal accounting standards. The professional accounting bodies, the Malaysian Association of Certified Public Accountants (MACPA) and the Malaysian Institute of Accountants (MIA), endorsed IAS as early as 1977. They review standards when issued by the IASC and adapt them to local needs. The time lag between the issuance of the IAS standards and their corresponding adoption in Malaysia usually is less than 5 years, and in many cases it is 2–3 years. By 1996, most IAS standards either had been adopted or were under consideration in Malaysia, with only a few exceptions (Appendix C).6

The Companies Act 1965 represents another source of authority in Malaysian accounting. It prescribes disclosure requirements and, following the British model, it requires published financial statements to reflect a “true and fair” view.

2.3. Singapore

The colonial history of Singapore dictates that its accounting standards and professional training also were under strong British influence. Before 1987, there was no formal standard setting; accounting standards were mainly reissues of UK standards. The Singapore Institute of Certified Public Accountants (ICPAS) was established in 1987, and it turned to the IASC as its main guidance for standard

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5 HK SSAPs generally allow fewer choices than IAS, for example, in the areas of inventory, accounting changes, and taxes. IAS standards that were not relevant for Hong Kong, such as changing prices, were not adopted. Evidence of adapting an IAS standard for local needs can be observed in SSSAP13 for investments, where investment properties are reported at market value without depreciation due to Hong Kong’s historically strong property market. Appendix C provides a comparison of the four East Asian countries’ accounting standards with International Accounting Standards as of 1995.

6 The exceptions are standards of little relevance in Malaysia, for example those dealing with changing prices and hyperinflation. For adopted IAS standards, differences with the original IAS standards are minimal.
setting. All IAS standards are examined for propriety of adoption in the Singapore context, and most had been adopted by the end of 1995 (Appendix C). Some IAS standards have been amended to be more relevant in the Singapore context, but the amendments generally are not significant and the essence of each IAS statement has been retained.

The statute that has a significant influence on accounting practices is the Companies Act of Singapore, which also drew its substance from the UK Companies Acts. It prescribes disclosure requirement for all companies, and in keeping with the British common-law influence, it also requires certification that the financial statements give a “true and fair” view.

2.4. Thailand

Thailand is the only country among the four that escaped British colonization in the 19th century. Nevertheless, the Institute of Certified Accountants and Auditors of Thailand (ICAAT) has turned to UK and US standards, and more recently, to IAS for guidance in standard setting. Gray et al. (1984) suggest that the Thai standards reflect “significant” IASC influence and “moderate” UK influence. For financial reporting issues where no local standards have been established, the Securities Exchange of Thailand requires that listed companies follow IAS or, failing the availability of such a standard, US GAAP (Ernst & Young, 1996; Ma, 1997). The common-law concept of “fair presentation” is emphasized in the Thai auditor’s report. Thai accounting standards therefore also reflect substantial common-law influence.

2.5. Accounting standards in the region as a whole

Appendix A summarizes the evolution of standard-setting in the four East Asian countries, and documents the strong common law influence on standards throughout that evolution. A collection of statements made by the accounting firms of Price Waterhouse and Ernst & Young about accounting standards in the four countries is provided in Appendix B. We offer these statements as indicative of the consensus in the accounting profession generally that accounting standards in the four East Asian countries exhibit greater similarity to UK, US, and IAS accounting standards (all of which are of common law origin) than they do to accounting standards in code law countries. To the best of our knowledge, the accounting professions in these countries have made no substantial attempts to deny this perception, and have actively promoted it.

We hasten to add that we do not conclude that accounting standards in the region are of equivalent quality to the UK, US or IASB standards that subsequently have been issued. Rather, we conclude that the accounting standards governing reporting in the four East Asian countries during our sample time period (1984–1996) were

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7 Some IAS standards that are of little relevance in Singapore, such as those dealing with changing prices and hyperinflation, were not adopted. For the adopted standards, only minimal changes were made to them (Appendix C).
influenced substantially by UK, US and IAS accounting standards and standard-setting institutions at the time, were widely believed to reflect that influence, and were widely believed to be of approximately equivalent quality to contemporary common law standards. Our empirical tests therefore attempt to measure earnings quality in the East Asian countries relative to that in both code law and common law countries during the same period.

3. Institutional factors influencing issuers’ incentives

Preparers’ (i.e. managers’ and auditors’) financial reporting incentives depend on the sources of demand for, and political influence on, financial reporting. This section surveys the salient institutional factors influencing East Asian financial reporting incentives. We conclude that East Asian financial reporting generally takes place within an incentive structure that can be characterized as a variant of the code law model.

3.1. System for determining and enforcing accounting standards

Ball et al. (2000) argue that preparers’ financial reporting incentives depend on the extent of political relative to market influences on their practices. Consequently, as in the case of standards, a useful starting point is to investigate whether preparer incentives originate predominantly in markets (as in common-law countries) or in governments (as in code-law countries). We conclude that preparer incentives in the four countries most closely resemble the code-law model, but also exhibit distinct regional features.

In market-oriented common-law countries, the “shareholder” model typically gives exclusive corporate governance rights to shareholders. There typically is a larger, more diverse base of individual shareholders and bondholders, and information asymmetry is more efficiently resolved through public disclosure. Hence, there is a larger demand for quality, including more timely incorporation of economic income in reported accounting earnings. The asymmetric loss function of debt holders implies a particular demand for earnings conservatism, because timely recognition of economic losses makes existing leverage and coverage covenants binding more quickly. The larger common-law monitoring role played by external shareholders and analysts, rather than by supervisory board members, also implies a larger demand for timely recognition of economic losses. Standard-setting and enforcement primarily are private-sector functions. Accounting standards are determined primarily by an independent accounting profession, whose members market their services to corporations. Auditors in common-law countries certify that financial statements are “fair” in representing the contractual relation between users and the firm, or that they conform to agreed market standards such as “Generally Accepted Accounting Principles.” The demand for high quality financial reporting and disclosure is enforced in a primarily market system, so there is a higher frequency and expected cost of shareholder litigation. Public corporations, with
securities listed in liquid markets, typically produce a larger fraction of economic output in common-law countries, in large part due to the quantity and quality of public disclosure.

In planning-oriented code-law countries, standard-setting and enforcement primarily are public-sector functions. Politicization leads to a “stakeholder” model in which major parties contracting with firms—suppliers of capital (typically banks), labor, major customers or suppliers, and governments—are represented in both writing the accounting code for firms generally and in the governance of individual corporations. Debt tends to be private (not publicly issued or traded), and shareholding tends to be concentrated in institutions such as banks (individual shareholders own comparatively little stock). Information asymmetry more likely is resolved by “insider” communication with stakeholder representatives, so there is a lower demand for high quality public financial reporting and disclosure. Consequently, there is a lower demand for timeliness in incorporating economic income (including economic losses) in accounting income. Conversely, in a typical code-law setting, the demand for accounting income arises more from compliance with tax codes and dividend and bonus payout policies, which affect preparers’ choices and reduce the sensitivity of accounting income to changes of market value. Auditors certify that financial statements conform to the code. Violation of the code is a criminal act, is enforced primarily by government, and bears statutory penalties such as fines or jail. Private corporations and conglomerates typically produce a larger fraction of economic output in code-law countries.

The four East Asian countries generally do not exhibit all traits of the code-law model. Their governments generally are not directly involved in accounting standard setting (except for Thailand, as discussed later), and tax codes generally have little influence on financial reporting (again, with the exception of Thailand). Labor, an important code-law stakeholder in Continental Europe, has little political influence generally, and little influence on standard-setting or corporate governance. However, two critical similarities remain: substantial political influence on financial reporting practice; and information asymmetry is resolved more through channels of private communication than through public disclosure. We believe these factors substantially influence preparers’ financial reporting incentives and practices. In the remainder of this section, we discuss salient features of the East Asian institutional environment, and conclude that the four countries generally have code-law reporting incentive features and also have unique institutional features that reduce the demand for financial reporting quality.

3.2. Influence of family control, guanxi and banks on the demand for public disclosure

An important institutional feature of these Asian economies is the dominance of family ownership in enterprises of all sizes, including large listed corporations. Claessens et al. (2000) document that in 1996, 66.7% of public companies in Hong Kong were family controlled, the corresponding numbers for Malaysia, Singapore and Thailand were 67.2%, 55.4%, and 61.6%, respectively. They also report that the top 15 families in Hong Kong controlled 34.4% of listed
Usually one family holds investments in various public and private enterprises that are tied together by complex cross-holdings and personal or kin relationships. Many of these family groups are of Chinese origin, even in Malaysia and Thailand, reflecting the significance of families in traditional Chinese ideology. The Chinese system of personal networking (guanxi) revolves around informal relationships rather than formal legal contracts. The predominance of networked family business groups is both due to and a cause of less developed capital markets: private networks and public markets are alternative contracting systems. We hypothesize that the prevalence of family controlled businesses and guanxi networks in East Asia reduces the demand for public disclosure, and therefore the demand for timely loss recognition. In this sense, the East Asian countries share much in common with the code-law model, in which internal communication with stakeholders plays a comparatively important role, and listed corporations are a less important part of the economy.

A related institutional factor that also reduces the demand for public financial reporting and disclosure in these countries is the prominence of banks as suppliers of capital, together with the banks’ close ties to company groups. Banks generally play a very important role in providing capital in economies at an early stage of development, as is the case in these countries. The abundance of family owned businesses also contributes to the importance of banks, because family controlled firms tend to have a preference for internal funds and bank loans over public equity and debt, even in Hong Kong where the financial markets are more developed. Similar to code-law countries, the importance of privately informed banks, and the commensurably lower importance of individual shareholders and public debt, reduces the demand for high quality public financial reporting and disclosure.

3.3. Political influences on financial reporting practice

The role of government in the economy varies across the four countries, as does the extent of political involvement in standard setting and financial reporting.

(footnote continued)
corporate assets (28.3%, 29.9%, and 53.3% in the cases of Malaysia, Singapore, and Thailand). Correspondingly, only 7.0%, 10.3%, 5.4%, and 6.6% of listed companies in the four countries were classified as widely held. The Hong Kong Society of Accountants (1997) reports similar numbers for Hong Kong, and also notes (p. 4) “controlling shareholders tend to appoint members of their family as executive directors to manage their listed companies on a full-time basis.”

Weidenbaum and Hughes (1996) report that in 1994, the total market capitalization of the 500 largest public companies in Asia controlled by overseas Chinese family groups exceeded $400 billion, with $155 billion in Hong Kong, $55 billion in Malaysia, $42 billion in Singapore, and $35 billion in Thailand. The $155 billion in Hong Kong represented over 60% of its total market capitalization. These statistics ignore smaller family controlled companies.

Contracting costs (including information, monitoring and other governance costs) likely are reduced for internal within-group contracting, but increased for external contracting, due to reduced public disclosure. See Khanna and Palepu (2000) on affiliated groups in India.

World Bank (1993, Chapters 5 and 6).
practice. The Hong Kong government has adopted a more laissez-faire approach to business, while the governments in Malaysia and Singapore have taken more interventionist roles. Thailand is the only case where the government is directly involved in accounting standard setting. While a professional body, the Institute of Certified Accountants and Auditors of Thailand (ICAAT), is responsible for establishing standards, formal approval is required from the Board of Supervision of Auditing Practices (BASP) under the Ministry of Commerce.\(^\text{12}\)

Political factors likely influence financial reporting practices in the region. There can be incentives to hide large profits and losses. Watts and Zimmerman (1978, 1986) argue that there generally are political costs of firms reporting large profits. Firms controlled by ethnic minorities are more likely to encounter political costs from reporting high profits. The economic power of minority ethnic Chinese has been a source of racial tension in many Southeast Asian countries.\(^\text{13}\) Ethnic tension has been strong in Indonesia, where there were racial riots in the 1950s and 1960s, and more recently in 1997. Among our sample countries, economic-related ethnic tension has been most important in Malaysia and Thailand. For example, after the 1969 racial riots, the Malaysian government implemented its New Economic Policy (NEP) to redistribute wealth to the native majority population, a policy which continues to this day. Consequently, firms controlled by ethnic minority Chinese would have political incentives to avoid reporting large profits.

Peltzman (1976) and Watts and Zimmerman (1986) argue that the political process generally is averse to firms reporting large losses. This too is likely to be magnified in East Asia. The term “crony capitalism” frequently is used to describe the close ties between governments and large corporations in East Asia.\(^\text{14}\) Without significant pressure from public investors for companies to report losses in a timely fashion, as in a common law setting, governments in East Asian countries often prevent or delay a company’s failure by allowing or encouraging it to paper over its losses. The government might seek to avoid bearing blame for corporate failures, or have close ties with corporate owners, or it might seek to avoid international intervention. For example, during the recent Asian economic crisis, a widely held view was that the government of Malaysia would not permit widespread reporting of losses and the technical defaults to foreign lenders that would arise from impaired balance

\(^{12}\) Saudagaran and Diga (2000) and Ma (1997).

\(^{13}\) See footnote 9. Also Richter (1999, Chapter 7 by George T. Haley and Usha C.V. Haley) reports the following statistics regarding the economic power of minority ethnic Chinese in several Southeast Asian countries in the mid-1990s:

<table>
<thead>
<tr>
<th>% of total population controlled by ethnic Chinese</th>
<th>% of market capitalization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Malaysia</td>
<td>29</td>
</tr>
<tr>
<td>Thailand</td>
<td>10</td>
</tr>
<tr>
<td>Indonesia</td>
<td>3.5</td>
</tr>
</tbody>
</table>

\(^{14}\) See, for example, comments by Chairman of Goldman Sachs at: http://www.asiasociety.org/speeches/corzine.html.
Therefore, we characterize companies in East Asian countries as having strong incentives to hide both large profits and large losses, and thus to report smoothed earnings.

3.4. Links between tax and financial reporting

Thailand is the only country in the sample with explicit linkage between tax and financial reporting. Thai Tax Law requires conformity between financial and tax reporting if companies wish to claim expenses for tax purposes. This induces companies to adopt financial reporting methods that minimize taxes, for example for depreciation and goodwill (Ma, 1997), and to smooth reported income. We predict that reported earnings in Thailand conform more closely to firms’ tax policies and are less oriented to the timely incorporation of gains and losses.

3.5. Enforcement mechanisms

Shareholder litigation is an important mechanism to enforce high quality financial reporting—particularly timely loss recognition—in common-law countries. The Asian countries experience comparatively little litigation. Saudagaran and Diga (2000) report that there have been no cases of judicial actions against auditors in Malaysia and Thailand. While there have been lawsuits against auditors in Singapore and Hong Kong, they are less frequent than in common-law countries (Choi et al., 1999, Exhibit 9.4). Favere-Marchesi (2000 p. 121) concludes from an extensive survey of South East Asian auditing: “audit quality in some countries is seriously compromised due to a lack of rules ensuring auditors’ independence … some of the liability regimes in ASEAN do not provide an incentive for statutory auditors to provide quality audit services.” We hypothesize that the lower expected cost of shareholder litigation in the four Asian countries reduces the incentive of managers and auditors to recognize economic losses in a timely fashion.

The influence and independence of the accounting profession likely is an indicator of the effective enforcement of accounting standards. We hypothesize that it also is an indicator of the demand for high quality public financial reporting and disclosure. The economic significance of the accounting professional bodies varies a great deal across the four countries. The size of the profession relative to the population is considerably larger in Hong Kong and Singapore than in Malaysia and Thailand, and their accounting professions generally are considered more

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15 For example, The Sydney Morning Herald reported on 26 September 1998: “In Malaysia the politically controlled central bank announced measures aimed at allowing banks to paper over the seriousness of their problems … [Dr.] Mahatir has urged the banks to increase new lending this year by 8%, at a time when the credit quality of many borrowers is already low.” Japan’s long-unresolved bad loan problem is another prominent example of the government’s avoidance of corporate failures by allowing companies to understate their losses.

16 Malaysian accounting largely follows a Western model, but some companies operate under Islamic rules linking reporting to zakat, a special tax (Ma, 1997). We believe this does not influence reporting by listed companies.
influential. These indicators lead us to predict \textit{ceteris paribus} higher quality financial reporting in Hong Kong and Singapore than in Malaysia and Thailand.

Taken as a group, the institutional environments and enforcement mechanisms in these four Asian countries more closely resemble the code law model than the common law model. Considering managers’ and auditors’ incentives alone, the implication is reduced timeliness and conservatism in accounting earnings, even though these Asian countries have derived their accounting standards from a largely common-law model. Among the four countries, Thailand exhibits a closer link between accounting and tax-based income, and conversely Hong Kong and Singapore exhibit more market-oriented characteristics, including stronger professional bodies and higher expected litigation costs. These differences in institutional environment imply even further reduced financial reporting quality in Thailand (and perhaps also Malaysia).

3.6. Standards and incentives

There are many reasons why financial reporting practice is not determined by accounting standards alone (Ball et al., 2000). Standards do not address the level of detail of practice, they lag innovations in practice, and there is judgment involved in their implementation. Asset impairment standards, such as SFAS No. 121 in the US, provide an important case in point. Information that an asset is impaired (i.e., that an economic loss has occurred) typically takes the form of adverse information about future cash flow prospects, much of which is private to managers. Triggering an impairment write-off against income is an inherently subjective process in relation to most corporate assets (contrast property, plant and equipment, and intangibles, with marketable securities), and is not determined by accounting standards alone. Manager and auditor incentives, as well as political and tax considerations, influence the decision, and hence whether economic losses are recognized in a timely fashion or are incorporated in income gradually over the entire life of the impaired future cash flows. Thus, financial reporting practice is determined by the interaction between accounting standards and preparers’ incentives.

4. Sample, variable definitions and summary statistics

The sample comprises 2726 annual earnings announcements during 1984–1996 in four Asian countries, Hong Kong, Malaysia, Singapore and Thailand. We identify all firm/years for which annual earnings data for Asian-listed stocks are on the Global Vantage Industrial/Commercial (IC) file, and for which data on security prices and number of outstanding shares are on the Global Vantage Issue

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17 For example, in 1991, there was 1 accountant per 3000 persons in Malaysia, while the corresponding number for Singapore was 500, as in Australia. See Radebaugh and Gray (1997, Exhibit 20.2).

18 A notorious case is Japanese banks, which have recognized known loan losses gradually over time in order to avoid reporting politically unacceptable prudential ratios.
The earnings numbers are scaled by the beginning market value of equity (price times number of shares). Equivalently, they are also first defined on a per share basis, adjusted for any stock splits or stock dividends using the adjustment factor supplied by Global Vantage, and then divided by the beginning-of-period price.

The earnings variable \( N_t \) is \( X_t/(N_tP_{t-1}) \), where \( X \) is net income before extraordinary items (IC data 32), \( N \) is adjusted number of shares and \( P \) is share price. The earnings change variable \( \Delta N_t \) is \( (X_t - X_{t-1})/(N_tP_{t-1}) \), adjusted for splits.

Stock return \( R_t \) is the holding-period return, including dividends, over the company’s fiscal year, representing economic income (change in market value, scaled to reduce heteroskedasticity). It is relatively free of short-term microstructure effects. To control for possibly exogenous (to accounting earnings) market-wide effects on \( R_t \) such as changes in expected returns, we deduct the sample mean return in fiscal year \( t \) for the firm’s reporting country \( j \). The four East Asian countries are in comparatively early stages of development, and macroeconomic factors exert a larger influence on their stock returns (Morck et al., 2000). Controlling for market-wide returns creates an independent variable that sums to zero for each country-year and hence is risk-free in the context of a domestic CAPM model.

The first and 100th percentiles of each variable (\( NI, \Delta NI \), and \( R \)) and all firm/years with missing values for \( NI \) or \( R \) are excluded. For some tests, the four countries are aggregated into the category “Asia” and compared with two benchmark samples, “Common” (Australia, Canada, UK and USA) and “Code” (Germany, France and Japan) taken from Ball et al. (2000).

Table 1 contains sample descriptive statistics. The individual-country samples are pooled firm/years, with sample sizes ranging from 476 (Thailand) to 867 (Hong Kong). Panel A reports means, medians and standard deviations for annual returns and earnings. Returns are considerably more volatile in the Asia category than in both Code and Common categories, but earnings are not. For example the Asia category has approximately 40% greater stock volatility, but 50% less earnings volatility, relative to the Common category. The difference is consistent with greater “smoothing” of accounting income in the East Asian countries, with longer lags in incorporating value changes. Similarly, accounting income is left-skewed (means lower than medians) in common-law countries, consistent with Basu (1997) asymmetric conservatism, whereas in both the code-law and Asia categories they are right-skewed. Stock returns are right-skewed in all categories. These summary statistics are consistent with lower timeliness of Asia category income.

Panel B of Table 1 reports the distribution of ending months for companies’ fiscal years. Typical ending months vary internationally. Hong Kong, which we categorize as the least regulated of the sample East Asian countries, exhibits the greatest dispersion in fiscal year-ends, similar to the UK (Ball et al., 2000, Table 1). At the other extreme, over 90% of Thai firms use the December year-end of the tax code, reflecting the influence of regulation and tax on financial reporting in Thailand. Panel C shows that over 80% of the sample observations fall in 7 years 1989–1995.

There are likely other East Asia countries whose accounting standards have also been under common-law influence, notably Taiwan and the Philippines, but we require at least 250 observations per country.
We caution that, relative to the literature on the relation between earnings and returns in the US and other major countries, sample sizes here are small.

### Table 1
**Sample characteristics**

**A) Descriptive statistics**

<table>
<thead>
<tr>
<th></th>
<th>N</th>
<th>μ</th>
<th>Med</th>
<th>σ</th>
<th></th>
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<th>μ</th>
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<td>44.6</td>
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<td>7.8</td>
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**B) Observations by fiscal year end (month)**

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**C) Observations by year**

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<td>MYS</td>
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<td>3</td>
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<td>615</td>
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<td>8</td>
<td>55</td>
<td>77</td>
<td>89</td>
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<td>65</td>
<td>57</td>
<td>50</td>
<td>0</td>
<td>476</td>
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<tr>
<td>Total</td>
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<td>91</td>
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<td>295</td>
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<td>348</td>
<td>419</td>
<td>432</td>
<td>27</td>
<td>2726</td>
</tr>
</tbody>
</table>

*Sample:* The firm/years for the four Asian countries (Hong Kong, Malaysia, Singapore, and Thailand) were selected from the Global Vantage Industrial/Commercial and Issue files over 1984–1996, using the following procedure. First, for each variable (see below) the two extreme percentiles of firm/year observations are eliminated. Second, all firm/years with missing values for stock returns and earnings variables are eliminated. Third, all firm/years from countries with fewer than 250 observations are eliminated, leaving four countries represented. These four countries were aggregated into the category ‘Asia’. The two benchmark country categories are: (a) Common (Australia, Canada, UK, and USA) and (b) Code (Germany, France, and Japan), with data also from the Global Vantage database and the same sample period.

*Variables:* $R$ denotes security return over the fiscal year; $NI$ denotes annual earnings per share before extraordinary items deflated by beginning of period price; $N$ denotes the number of firm/year observations.
5. Results: change in market value of equity as proxy for economic income

Initially, we use fiscal-year changes in market value of equity (adjusted for current-period dividends and capital transactions with shareholders) to proxy for economic income. Accounting income equals fiscal-year change in book value of equity (adjusted for dividends and capital transactions with shareholders), assuming “clean surplus” accounting. We therefore study the flow of market-valued economic income into book-valued accounting income.

For each country or group of countries $j$, we estimate a scaled piecewise linear regression of accounting income on change in market value of equity:

$$ NI_{it} = \beta_{0j} + \beta_{1j} RD_{it} + \beta_{2j} R_{it} + \beta_{3j} R_{it} RD_{it} + \epsilon_{it}. $$

Here $i$ and $j$ denote the firm and the country under whose standards it reports, and $RD_{it}$ is a dummy variable equaling one if return $R_{it}$ is negative (indicating economic losses), and zero otherwise.

We initially estimate Eq. (1) for each country or country group from a pooled cross-section (across firms) and time-series (fiscal years) regression. The coefficient $\beta_{2j}$ on stock return measures the contemporaneous sensitivity of country $j$ accounting income to positive changes in market values of equity (our proxy for economic gains). The coefficient $\beta_{3j}$ on the product of stock return and the return dummy measures the incremental country-specific sensitivity of accounting income to contemporaneous negative changes in market values of equity (our proxy for economic losses). The total sensitivity of income to decreases in market value is measured by $(\beta_{2j} + \beta_{3j})$. International differences in earningstimeliness, for positive and negative market value changes combined, are reflected in the $R^2$s of the individual-country regressions.

Panel A of Table 2 summarizes the results. The timeliness of Asian countries’ earnings, as measured by the pooled Asia $R^2$ in Panel A, is 4.48%. This is similar to the code-law sample $R^2$ of 4.63%, in contrast with the common-law sample’s 14.60%.21 $R^2$ statistics are graphed in Fig. 1.22 Hong Kong exhibits the highest timeliness ($R^2$ of 11.91%), consistent with its more market-oriented reputation. Thailand has very low timeliness ($R^2$ of 0.96%), consistent with the strong influence of the tax code on Thai financial reporting. Similar conclusions regarding timeliness can be derived using alternative specifications of the earnings-returns relation found in Panels B–D. For instance, in the linear model reported in Panel C the Asian $R^2$ of 3.88% is similar to the code-law $R^2$ of 4.49% and contrasts with the common law $R^2$ of 7.66% (even though the latter is downward-biased due to the linearity constraint). In Panel D, the Asian $R^2$ of 4.99% is again close to the code-law $R^2$ of 4.77% and much smaller than the 9.72% $R^2$ for common-law countries. These results suggest that in terms of timeliness, accounting income in these Asian Countries is similar to

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20 This specification is largely due to Basu (1997). Ball and Brown (1968), Beaver et al. (1980) and Ball et al. (2000) are other steps in the development of this model.

21 Common-law and code-law comparative statistics are from Ball et al. (2000).

22 The Cramer (1987) estimated standard error of estimated $R^2$ indicates that a difference of about 5% between categories is statistically significant at the 5% level, assuming independence across the categories.
Table 2
Contemporaneous association between earnings and returns: various specifications

### Panel A
\[ NI = \beta_0 + \beta_1 RD + \beta_2 R + \beta_3 R \times RD + \varepsilon \]

<table>
<thead>
<tr>
<th></th>
<th>$\beta_2$</th>
<th>t($\beta_2$)</th>
<th>$\beta_3$</th>
<th>t($\beta_3$)</th>
<th>Adj.$R^2$</th>
<th>N</th>
</tr>
</thead>
<tbody>
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<td>0.07</td>
<td>4.70</td>
<td>0.04</td>
<td>1.54</td>
<td>11.91%</td>
<td>867</td>
</tr>
<tr>
<td>MYS</td>
<td>0.01</td>
<td>2.44</td>
<td>0.00</td>
<td>0.20</td>
<td>9.19%</td>
<td>768</td>
</tr>
<tr>
<td>SGP</td>
<td>0.01</td>
<td>1.29</td>
<td>0.01</td>
<td>1.00</td>
<td>7.15%</td>
<td>615</td>
</tr>
<tr>
<td>THA</td>
<td>0.02</td>
<td>1.71</td>
<td>-0.01</td>
<td>-0.70</td>
<td>0.96%</td>
<td>476</td>
</tr>
</tbody>
</table>

Common: 0.00 $-0.64$ 0.33 $57.10$ 14.60% 40,870
Code: 0.04 9.92 0.03 4.35 4.63% 11,996
Asia: 0.02 4.07 0.00 0.08 4.48% 2,726

### Panel B
\[ NI = \beta_0 + \beta_1 R + e \text{ (R}$\geq$0) \]
\[ NI = \beta_0 + \beta_1 R + e \text{ (R}$<0) \]

<table>
<thead>
<tr>
<th></th>
<th>$\beta_1$</th>
<th>Adj.$R^2$</th>
<th>N</th>
<th></th>
<th>$\beta_1$</th>
<th>Adj.$R^2$</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>HKG</td>
<td>0.07</td>
<td>4.90%</td>
<td>367</td>
<td>0.11</td>
<td>5.27%</td>
<td>500</td>
<td></td>
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<tr>
<td>MYS</td>
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<td>1.31%</td>
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<td>0.01</td>
<td>0.39%</td>
<td>479</td>
<td></td>
</tr>
<tr>
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<td>186</td>
<td>0.00</td>
<td>$-0.34%$</td>
<td>290</td>
<td></td>
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</tbody>
</table>

Common: 0.00 0.00% 18203 0.33 13.96% 22,667
Code: 0.04 1.91% 5309 0.06 2.16% 6,687
Asia: 0.02 1.43% 1108 0.02 0.32% 1,618

### Panel C
\[ R = \beta_0 + \beta_1 NI + \varepsilon \]

<table>
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</thead>
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<tr>
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<tr>
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<td>0.80</td>
<td>2.59</td>
<td>1.19%</td>
<td>476</td>
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</table>

Common: 0.71 58.23 7.66% 40,870
Code: 0.97 23.78 4.49% 11,996
Asia: 1.21 10.54 3.88% 2,726

### Panel D
\[ R = \beta_0 + \beta_1 NI + \beta_2 ANI + \varepsilon \]

<table>
<thead>
<tr>
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<th>N</th>
</tr>
</thead>
<tbody>
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<td>0.59</td>
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<tr>
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<td>0.98</td>
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<td>0.08</td>
<td>0.18</td>
</tr>
<tr>
<td>THA</td>
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<td>1.87</td>
<td>1.17</td>
<td>4.12</td>
</tr>
</tbody>
</table>

Common: 0.72 52.16 0.29 24.24 9.72% 40,455
Code: 0.88 19.77 0.28 6.53 4.77% 11,879
Asia: 1.02 7.69 0.74 5.54 4.99% 2,699
code-law countries, even though their formal accounting standards can be better described as having common-law origins.

For all Asian countries, Panels A and B also reveal an absence of income statement conservatism in accounting incomes, in that they exhibit no greater timeliness in recognizing economic losses relative to gains. The $\beta_3$ coefficients in Panel A are insignificant in all four countries: $-0.01$ ($t = -0.70$) for Thailand; $0.01$ ($t = 1.00$) for Singapore; $0.00$ ($t = 0.20$) for Malaysia; and $0.04$ ($t = 1.54$) for Hong Kong, the highest coefficient but still insignificant at conventional levels. The Asian group shows little evidence of timely loss recognition, with a group $\beta_3$ coefficient close to zero and a $t$-statistic of 0.08. The coefficient is lower than even the 0.03 ($t = 4.35$) of the code-law group, which itself is a far cry from the 0.33 ($t = 57.10$) of the common-law group. The sensitivities of accounting income to positive returns ($\beta_2$) and negative returns ($\beta_2 + \beta_3$) are plotted in Fig. 2. The lack of timely loss recognition in the Asian countries justifies a conventional linear return/earnings model (Fig. 3).

The absence of timely loss recognition in Asian countries can be restated in terms of the separate positive-return and negative-return sample regressions in Panel B. There is considerably less disparity between the gain and loss years’ slope coefficients in the Asian countries (0.02 versus 0.02) than in common-law countries (0.00 versus 0.33) and even code-law countries (0.04 versus 0.06). The differences in $R^2$ follow a similar pattern. Among the four Asian countries, Hong Kong and Singapore show evidence of more timely loss recognition (higher coefficients and $R^2$ for the negative-return years) than Malaysia and Thailand. This is consistent with their more frequent shareholder litigation, larger profession bodies, and greater market orientation.

Interpreting the slope coefficients is assisted by the following illustration. Assume the information arriving in period $t$ causes a positive revision of $\Delta_t CF$ in the annual expected future cash flow in an $L$-period annuity of expected future cash flows. The information might concern a new product, an increase in customer goodwill, a decrease in factor prices, or any matter that increases expected future cash flows over
multi periods. Assume the discount rate is zero, and there are no current-period dividends or capital contributions. It follows that economic income \( \Delta MV_t = \Delta_t CF \).

The Recognition Rules lead to accounting income incorporating the revised cash flows only at their realization: \( NI_t \) would incorporate an amount \( \Delta_t CF \) each period for \( L \) periods. In other words, accounting income is a moving average of economic gains, “smoothing” them over time by incorporating \( L^{-1} \Delta MV_t \) for \( L \) periods. In a regression of \( NI_t \) on \( R_t \), the predicted slope then is \( L^{-1} \), and it measures the degree of natural income “smoothing” due to the Recognition Rules of accounting. 23

Assume now that the information arriving in period \( t \) causes a negative revision in the annuity of expected future cash flows. The information might concern a failed product, a losing strategy, a plant closing, or any matter that decreases expected future cash flows over multi periods. Basu’s (1997) thesis is that US preparers’ incentives make them more likely to incorporate the full amount of the economic loss \( L \Delta_t CF \) in contemporaneous accounting income \( NI_t \). The implied slope for accounting income against economic losses then is in the order of unity.

23 Realized cash flows incorporated in \( NI \) differ from expectations, suggesting measurement error. Accounting income is the dependent variable in (1), so any error is a component of the disturbance, and we do not expect biased slopes.
Fig. 2. International differences in asymmetry in earnings response to good and bad news. Sensitivity to positive and negative returns from pooled regression of earnings on (a) annual return and (b) annual return times negative return dummy.

Fig. 3. Bias in estimating international differences in earnings timeliness when ignoring different asymmetric conservatism. $R^2$ from pooled regression of earnings on (1) annual return and annual return times negative return dummy versus (2) annual return alone.
The above is a simplified example, and many other factors influence the slopes in (1). Nevertheless, it illustrates several points. First, accounting income is a mixture of two separate processes, incorporating economic gains in a different fashion than losses. Second, accounting income “smoothes” the incorporation of economic gains over time; it is a moving average of present and past gains. Third, the regression slopes in (1) are inverse functions of the degree of smoothing. Ceteris paribus, higher slopes in a regression of accounting income on stock returns imply greater timeliness of accounting income.24 Fourth, accounting conservatism implies higher slopes for economic losses than economic gains (that is, more timely incorporation of losses). Fifth, in countries in which preparers do not have strong incentives for timely recognition of economic losses, they can be incorporated in accounting income in much the same way as economic gains: in a smoothed fashion over time, waiting until the reduced future cash flow realizations occur.

Interpreting the loss-recognition slope is further assisted by noting that it measures income reductions that are correlated with reductions in market value, and hence that are correlated with decreases in expected future cash flows. It does not simply reflect opportunistic “big baths” taken by managers simply to increase future reported earnings.

To address the effect of cross-sectional dependence on the estimated standard errors and t-statistics, we also conduct a Fama–MacBeth test on the mean slope from a time series of separate annual cross-sectional regressions for each country category. This procedure does not alter our conclusions. Nor does controlling for the SIC codes of all Asian, code-law and common-law firms using the method in Ball et al. (2000, Table 7, model (5)).

A formal test of the statistical significance of differences in gain and loss recognition among country groups is provided by pooled (across countries) regression (firm/year subscripts omitted, $j$ denotes country group):

$$NI = \beta_0 + \sum_j \beta_{0j}CD_j + \beta_1RD + \sum_j \beta_{1j}RD.CD_j$$
$$+ \beta_2R + \sum_j \beta_{2j}R.CD_j + \beta_3R.RD + \sum_j \beta_{3j}R.RD.CD_j.$$  

Model (A) uses raw returns for the independent variables $R$ and $RD$, whereas model (B) uses returns adjusted by subtracting the annual country-specific mean return, as in previous tables. The reference sample is the code-law observations, and dummy variables (CD) are used to distinguish results for the Asia and common-law observations. Hence, $CD = 0$ for firm/years in code-law countries.

24 Contrary to what appears to be an accepted view, low slopes in a conventional regression of returns on earnings (ERCs) imply a high rate of contemporaneous incorporation of economic income, indicating high “value relevance.” The accepted view appears to be founded on the false assumption that accounting income is a random walk (Kothari and Sloan, 1992). This is inconsistent with the Recognition Rules, which make accounting income a moving average of economic gains. In the good-news example above, first differences in accounting income $\Delta NI$ are independent up to lag $L$, so accounting income resembles (but is not) a random walk (Ball and Watts, 1972). Fully “value relevant” accounting income is transitory in the levels (not first differences), like economic income, with an ERC of unity.
Results are in Table 3. Consistent with Table 2, the Asia group does not indicate significantly more timely loss recognition, compared to the code-law group. The incremental slope is 0.01 ($t = 0.32$) in model (A) and $-0.03$ ($t = -1.27$) in model (B). We therefore are unable to reject the hypothesis that the Asia and code-law groups follow identical loss recognition practices.

6. Results: transitory gain and loss components of accounting income

A potential criticism of the above research design is its use of stock market returns to proxy for economic income. One concern is that differences in slopes and $R^2$s estimated from (1) are due in part to differences in how individual countries’ stock markets incorporate information. Under our own hypothesis, the East Asian countries have generally lower levels of public disclosure and liquidity than common-law countries, which could make stock returns (the Basu model’s independent variable) noisier proxies for economic income in these countries. In defense of the model we argue that in countries where public disclosure levels are relatively low, the mechanism for impounding information in prices is more likely to involve trading by privately informed parties, so lower public disclosure does not in itself imply noisier prices. In addition, by using annual returns, we largely avoid problems in measuring returns due to lower market liquidity (less frequent trading). Nevertheless, we also conduct an analysis based solely on the time-series properties of earnings.

Following Basu (1997) and Ball and Robin (1999), we also study the persistence of changes in accounting income, as a function of the sign of the past-period change. Economic income is assumed to be completely transitory, or independent across time. The logic behind this assumption is identical to that underlying the “random walk” model of security returns, our proxy for economic income: that is, rational revisions of expectations of future cash flows do not exhibit time dependence (Bachelier, 1900). To the extent that accounting income reflects economic income in a timely manner, primarily by recognizing gains and losses due to changes in expected future cash flows, it will incorporate transitory components. To the extent that accounting income smooths economic income over time, primarily by awaiting the realization of changes in cash flows, it will exhibit persistence. If accounting income is asymmetrically conservative in the Basu (1997) sense, primarily by anticipating decreases but not increases in expected future cash flows, it will exhibit larger transitory decreases than increases.

While this method avoids using stock returns, it has disadvantages for measuring timeliness. If unrealized gains or losses are not recognized in a timely fashion as

---

25 $F$-statistics of 258.13 and 361.52 for the two models indicate significant differences among the three groups, though most is due to loss recognition in the common-law group, previously reported in Ball et al. (2000).

26 Bhattacharya and Daouk (2002) note that circa 1990 insider trading was not illegal in most continental European countries. The first enforcement of insider trading laws occurred in 1993, 1994 and 1996 for Thailand, Hong Kong and Malaysia, respectively. The outlier is Singapore, which had its first insider trading law enforcement in 1978.
Table 3
Comparative asymmetry in the contemporaneous returns-earnings relation: pooled regressions with country category effects

\[
Y = \beta_0 + \sum_j \beta_{0j} CD_j + \beta_1 RD + \sum_j \beta_{1j} RD CD_j + \beta_2 R + \sum_j \beta_{2j} R CD_j + \beta_3 R RD + \sum_j \beta_{3j} R RD CD_j
\]

<table>
<thead>
<tr>
<th>Model</th>
<th>(R_t) \quad (R_t - \bar{R}_p)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(\beta)</td>
<td>(t(\beta))</td>
</tr>
<tr>
<td><strong>Earnings sensitivity to value increases</strong></td>
<td></td>
</tr>
<tr>
<td>(\beta_2) (Base category = code)</td>
<td>0.04</td>
</tr>
<tr>
<td>(\beta_{2j}) (Incremental country category dummies)</td>
<td></td>
</tr>
<tr>
<td>Common</td>
<td>-0.03</td>
</tr>
<tr>
<td>Asia</td>
<td>-0.02</td>
</tr>
<tr>
<td>(F)-statistic for</td>
<td>8.58</td>
</tr>
<tr>
<td>All country category dummies</td>
<td></td>
</tr>
<tr>
<td>(p = 0.00)</td>
<td></td>
</tr>
<tr>
<td><strong>Incremental earnings sensitivity to value decreases</strong></td>
<td></td>
</tr>
<tr>
<td>(\beta_3) (Base category = code)</td>
<td>0.03</td>
</tr>
<tr>
<td>(\beta_{3j}) (Incremental country category dummies)</td>
<td></td>
</tr>
<tr>
<td>Common</td>
<td>0.32</td>
</tr>
<tr>
<td>Asia</td>
<td>0.01</td>
</tr>
<tr>
<td>(F)-statistic for</td>
<td>258.13</td>
</tr>
<tr>
<td>All country category negative return dummies</td>
<td>(p &lt; 0.00)</td>
</tr>
</tbody>
</table>

**Regression:**
\[
N = 55,592 \\
\text{Adj.} R^2 = 13.21\% \\
F = 769.99 \\
\text{Adj.} R^2 = 14.39\%
\]

**Sample:** The firm/years for the four Asian countries (Hong Kong, Malaysia, Singapore, and Thailand) were selected from the Global Vantage Industrial/Commercial and Issue files over 1984–1996, using the following procedure. First, for each variable (see below) the two extreme percentiles of firm/year observations are eliminated. Second, all firm/years with missing values for stock returns and earnings variables are eliminated. Third, all firm/years from countries with less than 250 observations are eliminated, leaving four countries represented.

**Country categories:** The four countries are aggregated into the category ‘Asia’. Two benchmark categories are: (a) Common (Australia, Canada, UK, and USA) and (b) Code (Germany, France, and Japan). The country category identifier \(CD_j = 1\) for firm/years in country category \(j\) and \(= 0\) otherwise. Code is the “base category," with \(CD_j = 0\).

**Variables and controls:** \(R\) denotes holding-period security return over the fiscal year in model (A) and returns net of annual country mean return \(\bar{R}_p\) in model (B); \(NI\) denotes annual earnings per share before extraordinary items deflated by beginning of period price; \(RD = 1\) if \(R < 0\) (market value decrease over fiscal year) and \(= 0\) otherwise (market value increase).

**Analysis:** Statistics are from regressions using the pooled cross-section and time-series of firm/year observations for all country categories. Results are not reported for the intercept, the negative return intercept and their respective country category dummies.
single, transitory elements of income, then this method will identify that. However, the method cannot identify whether transitory decreases in income occur with a lag or even whether they arise from income manipulation by managers, because it does not correlate income with contemporaneous stock returns. The two methods thus have their advantages and disadvantages.

We estimate the following pooled regression for each country or country group \( j \):

\[
\Delta NI_t = \beta_0 + \beta_1 NID_{t-1} + \beta_2 \Delta NI_{t-1} + \beta_3 NID_{t-1} \Delta NI_{t-1}. \tag{3}
\]

The dummy variable \( NID_{t-1} = 1 \) if \( \Delta NI_{t-1} < 0 \). Non-negative slopes reflect persistence in income changes, and negative slopes indicate transitory components of accounting income. \( \beta_2j \) measures the persistence or otherwise of positive income changes, and \( \beta_3j \) measures the incremental persistence or otherwise of negative income changes (\( \beta_3j < 0 \) implies asymmetric income-conservatism).

Table 4 presents estimates for model (3). Sample sizes are reduced by the additional data requirements to calculate income changes in two consecutive years. Consistent with timely loss recognition in common-law countries, their income decreases are shown to be much less persistent (more transitory) than their increases, with a \( \beta_3 \) coefficient of -0.87 (\( t = -39.52 \)) that is incremental with respect to the \( \beta_2 \) coefficient of 0.06 (\( t = 5.01 \)). This is an indicator that accounting income reflects economic losses more quickly than economic profits in common-law countries, consistent with the returns-based results in Ball et al. (2000). There is some evidence of asymmetric loss recognition in code-law countries, with \( \beta_3 \) negative and significant (-0.23, \( t = -5.78 \)), though considerably smaller than for the common-law group.
The code-law countries also have a negative $\beta_2$ ($-0.09, \ t = -3.47$), indicating transitory positive earnings changes.

In contrast, the Asian group $\beta_3$ coefficient is positive ($0.26, \ t = 3.69$), indicating negative earnings changes are less transitory than positive changes, consistent with accounting income incorporating losses more slowly than gains. This is the opposite of what accounting conservatism predicts. A negative $\beta_2$ ($-0.36, \ t = -6.87$) also is observed, with a much larger absolute magnitude than the coefficient for code-law countries. Singapore demonstrates the most evidence of asymmetric loss recognition, with its $\beta_3$ being significantly negative. Overall, the time-series analysis confirms the results from Tables 2 and 3, that is, accounting incomes in the Asian countries generally are not as timely in recognizing losses as in common-law countries, even though their formal accounting standards follow a predominantly common-law model.

7. Conclusions and implications

We study how accounting income incorporates economic income in four East Asian countries: Hong Kong, Malaysia, Singapore and Thailand. The chief proxy for economic income is fiscal-year change in the market value of equity, though we also utilize a test based on the transitory nature of economic income.

Each of these East Asian countries has been substantially influenced in the past by UK or US accounting standards, and each continues to be influenced by International Accounting Standards (IAS). UK, US, and IAS standards are universally viewed as being “high quality” and are associated with timely recognition of economic losses (Ball et al., 2000). Based on their formal standards alone, one therefore would expect accounting income in these East Asian countries to incorporate economic income—particularly economic losses—in a timely fashion. On the other hand, based on the incentives faced by managers and auditors in issuing financial statements, one would expect the opposite. Our evidence is consistent with the latter view. Incentives appear to dominate accounting standards as a determinant of financial reporting in Hong Kong, Malaysia, Singapore and Thailand.

If there is an “Asian model” in financial reporting, then our evidence suggests that timely financial statement recognition of economic income—particularly economic losses—is not part of it. Nevertheless, there is evidence of variation among the countries in the region. Hong Kong exhibits the highest timeliness in incorporating both economic gains and losses, consistent with its more market-oriented reputation. Thailand exhibits very low timeliness, consistent with the strong influence of government codification and income taxation on its financial reporting practices. We do not study variation within the country samples, either across firms or across time.

Our analysis of financial reporting quality in the four East Asian countries is descriptive, not prescriptive. The hypothesis is that quality is an endogenous function of market demands and political influences that are specific to each country: that is, quality is what a country’s institutional environment demands. Nevertheless, our results do have some interesting implications.
One implication of our results is that it is incomplete and misleading to classify countries in terms of their formal accounting standards, or even their standard-setting institutions, without giving substantial weight to the institutional influences on preparers’ actual financial reporting incentives. Yet standards are given almost exclusive attention in some contexts. For example, international accounting texts typically give substantially less attention to the wide variation across countries in preparers’ incentives than they give to the variation in standards. Transparency ratings, such as PricewaterhouseCoopers’ “opacity index” (which ranks Singapore higher than US and Britain), are based largely on standards.

A second implication of our results is that for countries striving to achieve higher financial reporting quality, changing manager and auditor incentives is more important than mandating foreign accounting standards. In mandating IAS for its member countries from 2005, the European Commission announced on 7 June 2002 that this would ensure that “company accounts throughout the EU are more reliable and transparent and that they can be more easily compared. This will in turn increase market efficiency and reduce the cost of capital for companies.” We note that the only changes were to accounting standards; none of the political and economic determinants of preparer incentives was changed, to our knowledge, particularly in relation to timely loss recognition.

A third implication of our results is that international differences in reporting incentives inherently limit the extent to which international comparability of accounting information can be achieved through homogenization of accounting standards alone. In particular, the International Accounting Standards Board (IASB, formerly IASC) is empowered under its constitution to promulgate its IAS standards, but it possesses no worldwide enforcement mechanism. Complete comparability of financial statements actually prepared and reported under IAS would require a uniform set of manager and auditor incentives internationally, which in turn would require complete worldwide integration of economic, legal and political systems.27 Our results imply the U.S. Securities and Exchange Commission (SEC) was well-advised in concluding that a condition for acceptance of International Accounting Standards (IAS) for financial reporting purposes in the US is that “the standards must be rigorously interpreted and applied.”28

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27 We are not implying that international institutional integration is desirable. Ball (1995) argues that it is undesirable. Our point is that there would be an enormous amount of economic, legal and political change required to make the demands placed on accounting information identical across nations, and to give managers and accountants identical reporting incentives worldwide. Such fundamental and widespread change is unlikely to occur, so homogenizing accounting standards alone will have a limited effect on the quality of accounting information actually reported.

28 A 1996 speech by SEC Commissioner Isaac C. Hunt, Jr. on “The Impact of the SEC on Financial Reporting” lists three prerequisites for the Commission’s acceptance of IAS: “(1) the standard must include a core set of accounting pronouncements that constitute a comprehensive, generally accepted basis of accounting; (2) the standards must be of high quality—they must result in comparability and transparency, and they must provide for full disclosure; and (3) the standards must be rigorously interpreted and applied.” The importance of a supporting infrastructure for quality reporting was also emphasized by the American Accounting Association’s Financial Accounting Standards Committee (1999) in its response to the IASC discussion paper.
also imply that the *de facto* standard for financial reporting practice, in a country that does not suppress stockholder litigation rights, is determined by market demand (as enforced by private litigation), so that technical differences between IAS and US GAAP standards are an over-rated factor.

The result that high-quality standards do not guarantee high-quality financial reporting has implications for the acceptance of the IAS “brand name” in the US, and in other economies with generally high financial reporting quality. Some commentators have noted that IAS may be adopted in some countries to gain “instant respectability” or to serve as a “politically correct substitute” for their own accounting standards. If such adopters do not drastically alter their enforcement mechanisms and the other political, legal and economic institutions affecting reporting incentives, then we predict that despite the IAS label their financial statements will not be of high quality. The IAS brand name therefore risks being identified with low quality. Spence’s (1973) signaling model implies that unless countries adopting IAS also reform their institutions so preparers pay costs for low-quality disclosure, they will not be able to credibly signal that their financial statements are of high quality. The cost to a country of adopting IAS or stating it has based its standards on IAS can be economically trivial; for small or developing countries, adopting IAS actually can be cheaper than maintaining domestic standards. In the Spence model, if signaling is costless then all players signal they are of high quality, and the signal loses its informativeness in discriminating among them. One conjecture then is that low-cost adoption of IAS by low-quality countries will erode its brand name and cause high-quality countries to not fully accept the IAS label. This conjecture is not based on the quality of the IAS standards themselves (which is where the debate has been centered to date), but on standard-setters in countries with high financial reporting quality protecting their reputation.

A related area in which the role of incentives is relevant is the decisions of individual firms to follow high-quality financial reporting practices (in particular, timely loss recognition), by reporting under IAS or US GAAP. But their capacity to signal that they in fact are reporting with high quality is hindered by their inability to distinguish themselves from low-quality firms. This is because firms without high-quality incentives also will find reporting under IAS or US GAAP attractive, because

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29 Saudagaran and Diga (1997, p. 22) and Tan (1996).
30 On its website at http://www.iasc.org.uk IASC Secretary-General Sir Bryan Carsberg commented: “It does not make sense for every country in the world to incur the enormous cost of developing its own national standards.”
31 We describe this as a “conjecture” due to the mixed results from Crawford and Sobel (1982) “cheap talk” models.
32 An example of insufficient attention to incentive issues is the following conclusion from Epstein and Mirza’s (1999, p. 17) survey of IAS adoption: “Among the more important converts to or protagonists of IAS are Germany, Belgium, France, Australia, and Italy. Other adopters include Hong Kong, Malta, Korea, Barbados, Zimbabwe, Lebanon, Turkey, Trinidad, and Tobago, Uganda, and Mongolia. ... To summarize, the international accounting standard-setting process ... is now poised on the brink of achieving wide-spread legitimacy, which may result, over time, in the IASCs becoming the premier accounting standard-setter.”
the costs of falsely signaling high quality is trivial (additional accounting and auditing costs). The international capital markets therefore might find it difficult to discriminate between the high- and low-quality individual-firm adopters of IAS or US GAAP, just as they might find it difficult to distinguish at the country level. A more effective way of signaling high quality would be to list one’s stock in a high-quality country, thereby exposing preparers to the incentives implicit in that country’s legal system. In our view, preparer incentives have received insufficient attention in the analysis of such issues.

Appendix A

Common Law Influence on the Four East Asian Countries’ Accounting Systems

Hong Kong
Pre-1973
Strong British influence in accounting training, education and practices. Accountants in Hong Kong could only become qualified through gaining membership in overseas professional bodies from UK and other Commonwealth countries.

1932 Company Ordinance was based on UK Companies Act of 1929. Later versions of Company Ordinance incorporated provisions of UK 1948 Companies Act.

1973–1982
Hong Kong Society of Accountants (HKSA) was founded in 1973. There are two routes to be admitted into membership of the HKSA, which is a necessary step to become a CPA. One is to pass the professional exam and meet the practice requirements. The other route is to become a full member of an overseas accounting body recognized by the HKSA, which are accounting bodies from UK and the former British colonies, provided that the same practice requirements are met. Even though HKSA had been running its own independent exams offered, most students took the exams by the UK Charted Association of Certified Accountants (CACA).

Non-mandatory accounting standards were issued during this period. They were essentially re-issues of UK accounting standards.

Post 1982
In 1982, the HKSA and UK CACA started to offer joint exams, the completion of which satisfies the examination requirements from both bodies.

Formal standard setting structure was introduced in 1982. Hong Kong accounting standards were issued based the UK standards.

As the UK standards became increasingly influenced by considerations of harmonization within the European Union, and with Hong Kong’s growing business ties with Mainland China, HKSA started to shift to International Accounting Standards for future guidance. In 1992, HKSA officially switched to IASC standards as models for future accounting standards and guidelines.

Malaysia
Pre-1957
Accounting and reporting practices originated from the UK. A majority of accountants were trained in UK and retained their membership of the UK professional body. Those who pursued accounting education at home sat for the examinations of the (UK) CACA and Australia professional body.

(Cont.)
1957–1978
Malaysian Association of Certified Public Accountants (MACPA) was established in 1958. MACPA devised accounting education and exam schemes based on the UK model. The Accountants Act (1967) established the Malaysian Institute of Accountants (MIA) as the national accounting body and empowered the MIA to regulate the practice of accounting in Malaysia. Full or associate members in UK and various Commonwealth countries’ accounting professional bodies were also eligible for the MIA membership.
Enactment of the Companies Act 1965, which was based on the UK Companies Act 1948. During this period, Malaysian professional accounting standards did not exist. Financial reporting was based on a small number of statements issued by MACPA and recommendations from various foreign accounting bodies, such as the (UK) CACA.

Post-1978
Since 1978, MIA and MACPA started adopting standards issued by the International Accounting Standards Committee. Each IASC standard issued is reviewed for relevance in the Malaysian context by following the due process. The final standards are promulgated also as International Accounting Standards (IAS), with the same acronym and serial numbers as the original IASC standards. Several domestic accounting standards have also been issued in areas not covered by the IASC standards.

Singapore
Pre-1963
Before 1963, there was no established accounting profession in Singapore. Trained accountants mostly obtained their qualifications in UK or Australia. Anyone with accountancy qualifications acquired in a British Commonwealth country was automatically recognized. Company law and legislations were enacted based on legislations in UK, the influences of which persist till today.

1963–1987
Singapore Society of Accountants (SSA) was established under the Singapore Society of Accountant Act 1963. There was no standard setting at this stage. Accounting standards were mainly based on UK standards; no attempts were made to adapt the overseas standards to reflect local circumstances. In 1982, the SSA started to administer joint professional examinations with (UK) CACA, reflecting strong UK influence.

Post-1987
The Accountants Act 1987 superseded the SSA Act 1963 and established the Institute of Certified Public Accountants (ICPAS). ICPAS issues Statements of Accounting Standards (SAS) based on IASC standards. Certain SASs with no corresponding IAS statements are based on UK standards, such as SAS 6 on Earnings Per Share and SAS 28 on Accounting for Goods and Services Tax.

Thailand
Pre-1962
The Institute of Certified Accountants and Auditors of Thailand (ICAAT) was established in 1948, originally under the name of the Institute of Certified Accountants of Thailand.

1962–1987
The accountancy profession was formally recognized in 1962 with the promulgation of the Auditor Act. Accounting standards were issued under the influence of UK and US standards. Contrary to the highly codified Thai law, the accounting standards conform closely to the Anglo-American model.
Post-1987
In 1987, Thailand started to shift to IAS for guidance in its accounting standard setting.

Information in this table is obtained from the following sources. Ma (1997): Chapter 10 Hong Kong, by Pak Auyeung; Chapter 11 Singapore, by Teoh Hai Yap and Ng Eng Juan; Chapter 12 Malaysia, by Teoh Hai Yap and Chuah Soon Guan; and Chapter 15 Thailand, by Pamela Angus-Leppan. Cooke and Parker (1994): Chapter 5 Hong Kong, by P. Phenix; Chapter 6 Thailand, by J.S.W. Tay; Chapter 7 Malaysia, by J.S.W. Tay; and Chapter 8 Singapore, by Foo See Liang and Ng Shwn Yng. Baydoun et al (1997): Chapter 4 Accounting in Hong Kong, by Anthony Moung Yin Chan, Kin Cheung Liu and Patrick Po Hing Ng; Chapter 5 Accounting in Malaysia and Singapore, by A. MacGregor, M. Hossain and K. Yap; and Chapter 12 Accounting regulation and practice in Thailand, by Mahmud Hossain and Mike Adams. Saudagaran and Diga (1997).

Appendix B

Accounting Standards in Four East Asian Countries: Comments by the Public Accounting Firms of Price Waterhouse and Ernst & Young

Hong Kong


"The Hong Kong Society of Accountants is a member of the International Accounting Standards Committee (IASC). Its current SSAPs comply in all material respects with the applicable IASC statements"

Ernst & Young (1993)

"Because a significant number of the HKSA’s members were trained in the United Kingdom, the accounting practices and audit procedures adopted in Hong Kong tend to reflect the influence of the UK accounting bodies. Currently the majority of accounting and auditing standards and guidelines issued by the HKSA are based almost entirely on the statements issued in the United Kingdom.”

"Most current Hong Kong SSAP are almost identical to the UK SSAP issued by the former UK Accounting Standards Committee.”

"Because it closely follows the UK standards, which generally comply with corresponding International Accounting Standards, Hong Kong has ensured that its standards are also largely consistent with International Accounting Standards.”

Malaysia

Ernst & Young (1992, 1997)

"The principal source of accounting principles is the series of approved accounting standards issued jointly by the Malaysian Institute of Accountants and the Malaysian Association of Certified Public Accountants (MACPA). Many of these standards are derived from international accounting standards. Local standards have also been developed to address areas of accounting not covered by the international standards.”

Price Waterhouse (1996)

"As members of the International Accounting Standards Committee (IASC), the MIA and MACPA have undertaken to support by specific adoption the International Accounting Standards (IASs) promulgated by the IASC. In addition to the specific adoption of IASs, the MIA and MACPA also undertake to issue Malaysian Accounting Standards (MSS) to cover topics not dealt with in IASs and topics where particular features of the Malaysian environment warrant a domestic standard written specifically to address those features.”

(cont.)

“Virtually all the International Accounting Standards issued by the International Accounting Standards Committee have been adopted by as SAS, although there might be a time lag in the effective date of each standard.”

“Where the accounting treatment is not prescribed in the SAS or recommended, guidance may be taken from generally accepted accounting principles elsewhere; for example, Australia, the United Kingdom or the United States.”

Thailand  Ernst & Young (1990 and 1996)

“The Institute of Certified Accountants and Auditors of Thailand issues accounting standards pronouncements that must be followed in preparing financial statements. The accounting principles established under these pronouncements closely follow International Accounting Standards (IAS) and US generally accepted accounting principles (GAAP).”

Ernst & Young—1996

“If no local accounting standards has been established for an accounting issue, listed companies must follow IAS, or US GAAP if a pronouncement on the issue is not included in IAS.”

Information obtained from the Ernst & Young’s International Business Series and Price Waterhouse Information Guide on “Doing Business in” each of the four countries.

Appendix C

Comparison of Four East Asian Countries’ Accounting Standards with International Accounting Standards as of 1995

<table>
<thead>
<tr>
<th>IAS</th>
<th>Hong Kong Statement of standard accounting practice (SSAP)</th>
<th>Malaysia Malaysian IAS (MIAS) and Malaysian accounting standard (MAS)</th>
<th>Singapore Statements of accounting standards (SAS)</th>
<th>Thailand Thai standards (SFASs) and exposure drafts (EDs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Accounting policy disclosure</td>
<td>MIAS 1</td>
<td>SAS 1</td>
<td>SFAS 1 &amp;2</td>
</tr>
<tr>
<td>2</td>
<td>Inventories</td>
<td>MIAS 2 [The standard does not permit LIFO.]</td>
<td>SAS 2</td>
<td>SFAS 22</td>
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</tbody>
</table>

(cont.)
<table>
<thead>
<tr>
<th></th>
<th>Topic</th>
<th>SSAP</th>
<th>MIAS</th>
<th>SAS</th>
<th>SFAS</th>
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<tbody>
<tr>
<td>4</td>
<td>Depreciation</td>
<td>17</td>
<td>4</td>
<td>4</td>
<td>10</td>
</tr>
<tr>
<td>5</td>
<td>Disclosures</td>
<td>Practice generally conforms with IAS</td>
<td>5 [The standard requires additional disclosure on dividend and tax credits.]</td>
<td>5 [Financial institutions are exempt. Entities with sales less than $1 million need not disclose sales figure.]</td>
<td>23</td>
</tr>
<tr>
<td>7</td>
<td>Cash flow</td>
<td>15 [Not required for certain small entities]</td>
<td>7</td>
<td>7 [Entities with gross assets less than $5 million are exempt.]</td>
<td>25</td>
</tr>
<tr>
<td>8</td>
<td>Net profit or loss, fundamental errors and changes in accounting policies</td>
<td>2 [SSAP 2 does not permit the IAS alternative treatment of reporting adjustments from accounting changes in current period net income.]</td>
<td>8</td>
<td>8</td>
<td>3 &amp; 4</td>
</tr>
<tr>
<td>9</td>
<td>R&amp;D costs</td>
<td>16</td>
<td>9</td>
<td>9</td>
<td>14</td>
</tr>
<tr>
<td>10</td>
<td>Contingencies and events after balance sheet date</td>
<td>8 &amp; 9</td>
<td>10</td>
<td>10</td>
<td>21</td>
</tr>
<tr>
<td>11</td>
<td>Construction contracts</td>
<td>3</td>
<td>11</td>
<td>11</td>
<td>8</td>
</tr>
<tr>
<td>12</td>
<td>Taxes</td>
<td>12 [IAS 12 permits either deferral or the liability method. Only the later is permitted under SSAP 12. IAS 12 allows full or partial provision; SSAP 12 requires only partial provision.]</td>
<td>12 [The standard requires disclosure of tax effects relating revalued assets, unless the entity has no intention of disposing of the asset in foreseeable future.]</td>
<td>12 [Recording of deferred tax as an asset is strongly discouraged.]</td>
<td>18 [Generally, companies charge tax payable in the current period to income. Deferred tax accounting is used primarily by listed companies.]</td>
</tr>
<tr>
<td></td>
<td>Presentation of current assets and current liabilities</td>
<td>Practice generally conforms with IAS</td>
<td>MIAS 13</td>
<td>SAS 13</td>
<td>SFAS 12 &amp; 16</td>
</tr>
<tr>
<td>---</td>
<td>--------------------------------------------------------</td>
<td>-------------------------------------</td>
<td>---------</td>
<td>--------</td>
<td>--------------</td>
</tr>
<tr>
<td>14</td>
<td>Segments</td>
<td>AG 6 [Disclosure of segmental information is applicable only to listed companies.]</td>
<td>MIAS 14</td>
<td>SAS 23 [Financial institutions are exempt.]</td>
<td>SFAS 24 [SFAS requires disclosure of only segment sales and assets.]</td>
</tr>
<tr>
<td>15</td>
<td>Changing prices</td>
<td>Not adopted</td>
<td>Not adopted</td>
<td>Not adopted</td>
<td>Not adopted</td>
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<tr>
<td>16</td>
<td>Property, plant, and equipment</td>
<td>SSAP 13 &amp; SSAP 17 [Separate disclosure required for land holdings.]</td>
<td>MIAS 16 [Revaluation of property, plant and equipment has to be approved by Malaysian Securities Commission.]</td>
<td>SAS 14</td>
<td>SFAS 9</td>
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<td>MIAS 18</td>
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<td>19</td>
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<td>MIAS 19</td>
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<td>20</td>
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<td>Not adopted</td>
<td>Not adopted</td>
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<td>ED 30 general conforms with IAS</td>
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<td>21</td>
<td>Exchange rate changes</td>
<td>SSAP 11</td>
<td>MIAS 21 [Income statement items are translated at the closing rate when translating financial statements of a foreign entity for consolidation purposes.]</td>
<td>SAS 20</td>
<td>ED 13 [Practice general conforms with IAS]</td>
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<td>22</td>
<td>Business combinations</td>
<td>AG 4 [AG 4 allows elimination of positive goodwill against reserves. Under</td>
<td>MAS 2</td>
<td>SAS 22</td>
<td>SFAS 20 [Allocation of goodwill not covered. Practice is to capitalize (cont.)</td>
</tr>
</tbody>
</table>
### 23 Borrowing costs

AG 5 [AG 5 accepts only the IAS alternative treatment of capitalizing borrowing costs.]

**MIAS 23**

SAS 19 [The phrase “where asset is ready for its intended use” is defined as “the date when Temporary Occupation Permit is issued.”]

SFAS 15

### 24 Related party disclosure

Not adopted

[There are minimal disclosure requirements in the company legislation.]

**Exposure Draft issued**

SAS 21 [Financial Institutions are exempt.]

SFAS 13

### 25 Investments

SSAP 13 [IAS 25 requires investment properties to be treated as property subject to depreciation; SSAP 13 requires them to be disclosed at market value without depreciation.]

**MIAS 25** [Not applicable to financial institutions. Revaluation of investments by licensed valuers at regular intervals. Revaluation reserves relating to disposed assets are transferred to retained earnings.]

SAS 25

SFAS 17

### 26 Retirement benefit plans

Not adopted

**MIAS 26**

SAS 24

Not adopted

### 27 Consolidation and accounting for investments in subsidiaries

SSAP 7 [SSAP 7 specifically defines control as control of the board, control of more than half of the voting power, or holding of more than half of the issued share capital.]

**MIAS 27 & MAS 6** [MAS 6 prescribes a maximum amortization period of 25 years.]

SAS 26

SFAS 18 & 19

(continuation)
<table>
<thead>
<tr>
<th>No.</th>
<th>Topic</th>
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</table>

Local standards without corresponding IAS:

- SSAP 5 Earnings per share
- AG 1 Preparation and presentation of accounts from incomplete records
- AG 2 The effect of international accounting standards
- AG 3 Accounts of dealers in securities
- AG 7 Accounting for textile quota entitlements
- MAS 1 Earnings per share
- MAS 3 Accounting general insurance business
- MAS 4 Accounting for life insurance business
- MAS 5 Accounting for aquaculture
- MAS 7 Accounting for property development
- SAS 6 Earnings per share
- SAS 28 Accounting for goods and services tax
- SFAS 5 Earnings per share
- SFAS 11 Accounting for doubtful receivables.
- SFAS 26 Realization of Income from Real Estate Business
- SFAS 28 Accounting for Debt conversion and debts issued with Warrants

Primary a collection of information reported in Ma, (1997): Chapter 10 Hong Kong, by Pak Auyeung; Chapter 11 Singapore, by Teoh Hai Yap and Ng Eng Juan; Chapter 12 Malaysia, by Teoh Hai Yap and Chuah Soon Guan; and Chapter 15 Thailand, by Pamela Angus-Leppan.

**References**


Ernst & Young’s International Business Series, 1992 and 1997. Doing business in Malaysia, Ernst & Young, Malaysia.
Ernst & Young’s International Business Series, 1993. Doing business in Hong Kong, Ernst & Young, Hong Kong.