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Taxpayer Behavior Towards Fixed Asset Revaluation

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ABSTRACT

The development of tax incentive policies designed to suit the interests and prevailing tax laws and regulations so that this research is directed at identifying, analyzing, and designing effective tax incentive policies. This study aims to describe how taxpayers' behavior towards their decisions in fixed asset revaluation.This study is descriptive in nature, using the Research and Development approach through exploratory studies. This research is not designed to test hypotheses, but describes the data, facts and trends that occur, then analyzed and recommended what kind of Fixed Asset Revaluation policy model should be made to increase taxpayer compliance which can then increase tax revenue. Data obtained by interview techniques, with respondents consisting of corporate taxpayers and experts in the field of Asset Valuation Accounting. The research was conducted for 6 months, data collection was carried out in Bandung. The results of the research aim to be used as input for the Directorate General of Taxes in making tax incentive policies in Fixed Asset Revaluation.

Keywords: Fixed asset revaluation, tax incentives, taxpayer behavior

Introduction

Fixed asset revaluation has become the most controversial policy issue facing the accounting standards set around the world (Wang, 2006). Some argue that the fair value of fixed assets is more relevant in making economic decisions, therefore, it should be used in reporting fixed assets. Fair value-based implementation has an impact on company profitability and solvency but does not have an impact on company liquidity (Sparta & Sari, 2011). Furthermore, it is explained that an increase in the value of fixed assets reduces the company's profitability and increases the company's own capital which has an impact on the company's solvency for the better.

The purpose of carrying out asset revaluation is to provide more relevant information about the financial position of an organization for users of financial statements (Seng et.al., 2010). The considerable inconsistency between timing, frequency, and method of revaluation raises the question of whether relevance is the only reason for a firm's asset revaluation decision (Lin & Peasnell, 2000). According to the revised PSAK 16 2011, revaluation is a method of valuing fixed assets. If an entity chooses to use the revaluation method, this method must be consistently applied by the company. Companies should not only use the revaluation method occasionally for the purposes mentioned above, but revaluations must be carried out regularly.

Countries such as Indonesia allow managers to write up fixed assets if their current values are greater than the carrying values. Upward revaluations of fixed assets increase the carrying values of fixed assets and revaluation reserves in shareholders' equity, but can reduce future earnings, return on total assets and return on equity (ROE). Although upward asset revaluation practice mitigate part of the fundamental problem in historical cost accounting and provides users with more useful and relevant information (SSAP 12), it seems to contradict accounting conservatism in the sense that upward revaluations increase the carrying values of fixed assets before they are

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realised. Watts (2003a,b) argues that an important consequence of accounting conservatism is the persistent understatement of net asset values. Moreover, upward asset revaluations are widely believed to be subject to managerial discretion because current values of fixed assets are normally unavailable and any estimates are unverifiable. For example, Lin and Peasnell (2000) argue that upward revaluations in the UK tend to be discretionary in nature because managers are not only able to decide what assets and when these assets are revalued, but can also decide what revaluation amounts need to be recognised in financial statements. As a result, prior research has mainly focused on investigating managerial motivations for the upward revaluation decision, and has provided consistent evidence indicating managers are opportunistic and also revalue assets upwards at their discretion to reduce contracting and political costs (Brown et al., 1992; Lin & Peasnell, 2000).

Previous studies find that managers recognise upward revaluations when firms intend to reduce leverage and therefore contracting and political costs. Firms may delay upward revaluations if there is no immediate need for doing so. The above reasons may explain why only a small proportion of UK firms revalue their fixed assets upwards in practice. We find that only around 10 per cent of UK firms revalued their assets upwards during the test period of 1994-1998. Moreover, even for those firms that chose to do so, they only revalued their fixed assets approximately every five years (Aboody et al., 1999; Lin & Peasnell, 2000). Different from the contracting cost and signalling hypotheses that have been examined in prior research, this study contributes to the literature by further investigating whether managers make the upward revaluation decision on a timely basis and the extent to which the decision is affected by accounting conservatism.

The rest of the paper is organised as follows. Previous studies on upward revaluations are summarised in Section 2. Section 3 describes sample selection criteria. Section 4 discusses the research methodology used for our empirical tests. Section 5 reports the empirical results. Section 6 provides a summary of robustness tests. Section 7 concludes the paper.

Literature Review

Several earlier studies on upward asset revaluations are based in Australia. Most of them assume managers are opportunistic and revalue their firms' assets upwards to achieve certain financial objectives. For instance, the revaluation firms (revaluers) have borrowing limits in place, higher leverage and more growth opportunities than non-revaluation firms (non-revaluers). Further, companies with leverage approaching their borrowing limit are more likely to revalue their assets upwards. Brown et al. (1992) find revaluers normally have higher debt-to-total tangible asset ratios and property holdings (including land and buildings), lower tax-free reserves, and often declare a bonus issue or received a takeover bid in the revaluation year. Revaluers also appear to be larger and closer to violating their debt covenant constraints. argue asset revaluations increase the current value of any collateral security and are used to signal firms' available borrowing capacity. They find revaluers are more likely to have a higher ratio of total liabilities-to-total tangible assets and a less growth in operating cash flow in the revaluation year.

In a survey of upward asset revaluation, Easton et al. (1993) found 40 per cent of Australian companies making the respondents state that their primary objective is to reduce the debt-to-asset ratio and 45 per cent that it is to present true and fair financial statements. In the investigation of the timeliness of upward revaluations among Australian companies, Easton et al. (1993) showshare price rather than current year share return is associated with upward revaluation, indicating the market already reflects upward revaluation in share price but that managers do not recognise an upward revaluation in the same year. The evidence also shows that cumulative upward revaluation over a three-year interval provides statistically significant explanatory power for cumulative share return over the same time period, implying upward revaluation is not recognised by managers on a timely basis. Easton et al. (1993) also find that an upward asset revaluation is positively associated with share return, but only when companies have a higher change in

debt and the level of their revaluation activity to date is relatively high. In other words, upward asset revaluation is timely only for firms with a higher increase in debt and higher balance of revaluation reserve. The above results generally suggest that upward asset revaluations in Australia are not always timely.

Research Method

The research method used in this research is descriptive-analytic method. The use of this qualitative approach is based on the concept of natural setting, grounded theory, is descriptive in nature, emphasizes process rather than results, design is temporary, and research results are negotiated and mutually agreed upon (Bogdan & Biklen, 1982; Lincoln & Guba, 1985). However, considering that the main objective of this research is not only to analyze the object under study through the process of exploring facts and object data in the field as it is, but also to try to analyze a wider area by providing an assessment and prediction of long-term needs for future. Therefore, to provide flexibility in adjusting to multiple matters, and to be more sensitive to the value sharpening encountered, the Evaluation and Policy Analysis method is used with the post policy analysis technique (McMilan & Schumacher, 2001), or in research and development terminology it is often referred to as quantitative and future oriented policy research methods.

This research was conducted using qualitative methods with an analytic approach. Data was collected by interviewing corporate taxpayers who are domiciled in the West Java I and Banten Regional Offices. The results of these interviews were then processed using NVivo to perform data coding effectively and efficiently. Therefore, the key to being able to present data in the form of tables, graphs, diagrams, and models for qualitative researchers using NVivo is how to code research data sources. The results of this interview were then discussed in a Focus Group Discussion activity, which produced several views from the FGD participants.

Results and Discussions

Figure 1 shows how the behavior of taxpayers in fixed asset revaluation, when talking about asset revaluation is actually to increase the value of the information in the financial statements because the essence of our financial statements shows that information is as close to reality as possible. Because it is impossible then that the financial statements describe the whole reality. One of the efforts is when we have to do asset revaluation. But this only applies to fixed assets that need to be revalued or which may be revalued. The goal was to make the information more relevant. It's just that as an entity I think we also have to understand the consequences if we do a revaluation. If I try to study it according to what I understand, if an entity decides to carry out a revaluation, there will be costs as well as benefits, there will be costs and benefits. First, the costs borne are at least appraisal costs, if the entity does not have the competence to value the revalued assets. Second, if the appraisal has been appraised and then the asset appreciates, there will be consequences for the tax to be paid, I don't know whether it's PPh or what, but the value is not small either, around 10% if I'm not mistaken, if the rate hasn't changed.

The results of this study are in line with Cheng and Lin (2009), where (1) Upward revaluation increases future depreciation expenses and therefore reduces future earnings and related financial ratios; (2) Most of countries require that goodwill be capitalised as an intangible asset and amortised during its useful life. UK was one of the very few countries in the world allowing firms to write off acquired goodwill against reserves. Aboody et al. (1999) argue upward revaluations are used to signal firms' superior future performance, which is better measured by changes in future operating income and cash flow. We follow their approach and replace share return with the change in future operating income and cash flow one year, two years and three years after the revaluation year.

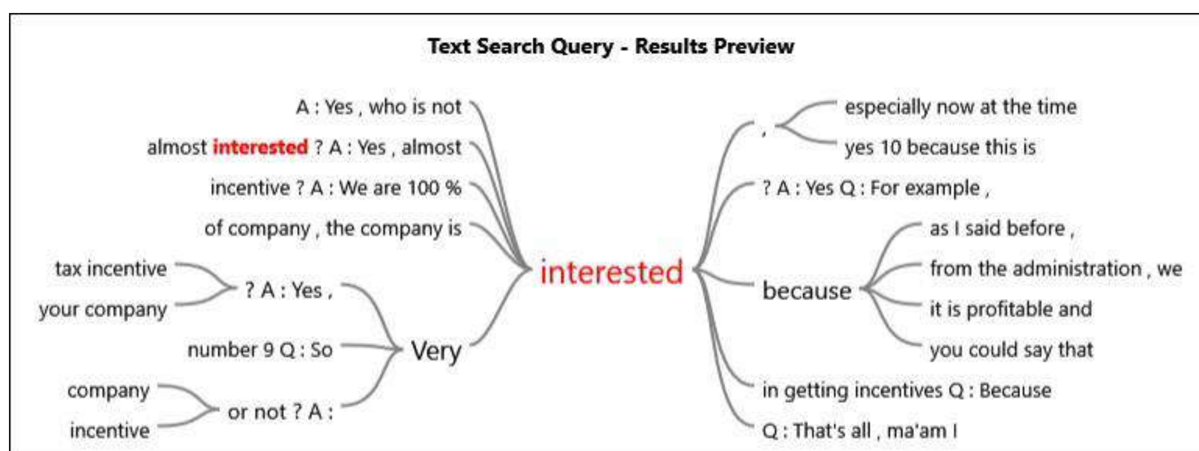

Figure 1. Description of the taxpayer's interest in conducting fixed asset revaluation

That's due to the increased appreciation. Whereas for the revalued fixed assets, the value will likely be quite high, meaning that the tax burden borne by the entity will also tend to be high as well. Then in the next reporting process, if the company chooses to use the revaluation method, this cannot be done once but must be consistent, so when the company has decided to revaluate, then in subsequent years it must be consistent in using the revaluation method. And for the group of assets to be revalued, everything must be done, so it cannot be done only in part, for example, a company decides to evaluate a building, then for buildings that have the same function that the company has, it must also be revalued. So, I think the tax consequences of 10% will be quite significant and quite burdensome for the company. What I identified with Mr. Nur, this is a sacrifice for the benefits that can be obtained when we carry out a revaluation, among others, our financial statements contain information that is more reasonable or closer to reality; secondly, the value of the company's assets increases, thereby increasing the company's access to sources of funds, especially external sources of funds; Third, of course, there will be an increase in depreciation costs in the future which are expected to save taxes as well. It's about the cost and benefit. If it is related to the subject, this revaluation to my understanding is only mandatory for companies that use financial accounting standards, which adopt IFRS, which means companies with full public accountability including the capital market and so on. However, revaluation is not mandatory for companies that do not adopt SAK. If we are in a company that is not obliged to carry out a revaluation, then when we are going to do a revaluation, the benefits and costs must be properly thought out, lest the decision ends up being greater than the benefits that will be obtained, because in terms of performance it will not necessarily increase when doing the revaluation. Even if we analyze profitability, it could be that the revaluation will decrease later because ROI may decrease when assets increase but the income does not increase significantly with an increase in assets, then the performance will be considered to be decreased. So, the only reason economically I think that the company will carry out a revaluation is if it wants to access funding sources. Does he want to add or get credit from banks, or he will look for sources of funds from the capital, or companies that will be sold, acquired, or melted down. Companies may have rational economic reasons for carrying out a revaluation, but beyond that, I think the company should think long and hard when doing a revaluation because to my understanding the cost is clear but the benefits are not certain. That's my understanding. What I am saying is that I want to get confirmation whether it is a correct view or not, meaning that in my position as a WP or let's say I am on the side of the WP, I would suggest that the WP or entity needs to be careful when carrying out a revaluation. then when carrying out a revaluation, it seemed as if the assets had increased but there were other consequences that they had not thought of and I think that an increase in assets cannot be said to have increased

performance, even if there was an increase it was relatively smaller, because the increase had not been realized.

Conclusions

Financial reporting aims to convey relevant information that is closest to reality for decision-making. One of the information is the AT value, which is generally conveyed based on its Book Value (HP - AP), so that it may become irrelevant for AT which is experiencing fluctuating market prices. For the information about AT to be relevant, it is necessary to do a revaluation. In its implementation, the revaluation will (definitely) trigger costs, including:

1. Appraisal fee
2. Income tax of 10% on the increase in value (appreciation) of the validated AT
3. Dynamics in the subsequent reporting process, because if a company chooses to use the revaluation method, it must be carried out consistently and carried out on all fixed assets in the same class (similar nature and use in the entity's operations, whether done simultaneously or gradually.
4. Revaluation can also burden the company's cash flow

The benefits of doing a revaluation include:

1. Financial reports contain information that is more reasonable or closer to reality;
2. Asset value may increase, which increases the company's access to external funds (long debts and/or new shares);
3. Increased depreciation costs that can save taxes on Annual Income Tax

Therefore, in deciding whether or not to carry out fixed asset revaluation by taking into account and comparing the costs and benefits that must be borne and will be obtained by the company.

For business in the real sector, as long as the business is running, as usual, there is no interest in obtaining external sources of funds, there are plans for mergers, sales of new shares, or will be acquired, the economic benefits that can be obtained from asset revaluation are minimal if you don't want to say any. It could be different if it is done by a financial sector company that always has an interest in increasing its equity to increase its ability to bear financial risks.

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