Prudential regulatory regimes, accounting standards, and earnings management in the banking industry

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Abstrak

We analyze if a change in accounting standard or a change in prudential regulation impacts banks loan loss provision. We find that, in general, the banks using a principles based accounting standard exhibit a lower level of earnings management compared to banks using a rules-based accounting standard. When a country moves from pro cyclical macro prudential regulations to a dynamic provisioning regime, banks are more likely to set aside a larger amount of loan loss provision for the purpose of income smoothing.