AKURASI Jurnal Studi Akuntansi dan Keuangan
p-ISSN : 2720-9067
e-ISSN : 2685-1059
Program Studi Magister Akuntansi
Fakultas Ekonomi dan Bisnis
Universitas Mataram

THE IMPACT OF THE FORWARD-LOOKING EXPECTED LOSS METHOD REFERS TO FINANCIAL ACCOUNTING STANDARD NO. 71 ON EARNINGS QUALITY OF THE INDONESIAN ISLAMIC BANKS

Silvya Eka Marenza[1], Nur Ariskawati[2], Sugiyarti Fatma Laela[3]
Tazkia Islamic University College[123]
[1]Corresponding author:ekamarenzasilvya@gmail.com

INFORMASI ARTIKEL

Article history:
Dikirim tanggal: 13/12/2023
Revisi pertama tanggal: 29/02/2024
Diterima tanggal: 8/04/2024
Tersedia online tanggal: 24/06/2024

ABSTRAK

Tujuan dari penelitian ini adalah untuk menganalisis pengaruh penerapan metode forward-looking expected loss sebagai konsekuensi Standar Akuntansi Keuangan (SAK) No 71 terhadap kualitas laba pada bank syariah. Oleh karena metode ini efektif pada tahun 2020, forward-looking expected loss diukur dengan menggunakan rasio loan loss provisions dengan dummy tahun untuk membedakan antara forward-looking dan non-forward-looking. Adapun prediktabilitas laba digunakan sebagai proksi kualitas laba. Sampel terdiri dari 16 bank umum syariah periode 2018-2021 sehingga menghasilkan 55 tahun buku sebagai unit yang dianalisis. Hasil analisis regresi data panel menunjukkan bahwa semakin tinggi cadangan kerugian penurunan nilai bank syariah maka semakin rendah kualitas labanya. Namun setelah penerapan PSAK 71, semakin tinggi cadangan kerugian penurunan nilai yang berbasis pada forward-looking maka kualitas laba pun semakin tinggi yang dibuktikan dengan kemampuan informasi laba dalam memprediksi laba masa depan.

Kata Kunci: Bank Umum Syariah, prediktabilitas laba, expected loss, COVID-19.

ABSTRACT

This research investigates the effect of applying the forward-looking expected loss method as a consequence of Financial Accounting Standard (FAS) No 71 on earnings quality. Since the technique is effective in 2020, forward-looking expected loss is measured using loan loss provisions ratio with a year dummy to differentiate forward-looking and non-forward-looking. At the same time, the predictability of earnings is used as a proxy of earnings quality. The sample consists of 16 Shariah commercial banks from 2018 to 2021, resulting in 55 firm years as a unit of analysis. Using panel data regression, the results show that the higher the reserve for impairment loss of Islamic banks, the lower the quality of earnings. However, after the implementation of SFAS 71, the higher the reserve, the higher the earnings quality, proven by the ability of earnings to predict future earnings.

Keywords: Shariah Commercial Bank, earnings predictability, expected loss, COVID-19

1. Introduction

The banking industry in Indonesia has a significant position by controlling around 75% of the total national financial assets. In particular, the market share of Islamic banking has grown to 7.31% of the entire national banking industry as of June 2023 (Binekasri, 2023). Banks act as financial intermediaries, collecting funds from the public and distributing them to various forms of financing (Primandasetio, 2021). In April 2023, Sharia Commercial Banks distributed financing worth IDR507.1 trillion, with an 18.5% annual growth rate. The main driver of this growth was Murabahah financing, which reached IDR237.5 trillion (OJK 2023). If the distribution of Murabahah financing runs smoothly, more income generated by Murabahah leads to higher profits for Islamic banks.

However, in practice, the bank's function as an intermediary presents risks, especially financing risk. Financing risk refers to the possibility of financial losses when borrowers cannot immediately repay their debts (Rahmadani 2016). According to the data (OJK, 2023), in April 2023, the value of Non-Performing Financing (NPF) reached IDR11.7 trillion, or equivalent to 2.3% of total financing. This increase in NPF was exacerbated by the COVID-19 pandemic, as customers decreased their ability to pay back their debts on time. The high value of NPF can disrupt bank liquidity, namely the bank's ability to fulfill its obligations to depositors.

The Indonesian Financial Service Authority (IFSA) responded to the impact of the spread of COVID-19 by issuing IFSA Regulation Number 48 of 2020, mandating the formation of impairment loss reserves (Cadangan Kerugian Penurunan Nilai /CKPN) for debtors who are considered unable to survive after financing restructuring is carried out (Firmansyah et al., 2022). The impairment loss reserve is a reserve formed by banks to cover possible losses due to impairment of financing (Vebriana et al., 2020). The impairment loss reserve regulation can lead to potential moral hazard if not carefully monitored. Moral hazard can occur if banks form too large a reserve to cover losses on financing so that bank profits look higher than they are (Sobarsyah et al. 2020). Therefore, the recording of the impairment loss reserve is regulated by SFAS No 71 to prevent misuse of these regulations so that the financial statements remain high quality and reflect economic reality.

The implementation of SFAS No.71 has been effective since January 1, 2020, in response to criticism of SFAS No. 55, which is considered too late in recognizing losses (Aboud et al., 2018). Implementing SFAS No 71 resulted in banks having to reserve more impairment losses on financial instruments based on the expected loss method, which is applying the expected financing losses earlier (Firmansyah et al., 2022), known as forward-looking expected loss.

In the forward-looking expected loss method, assessing the decline in value of financial assets emphasizes the relevance and up-to-dateness of information to support decision-making and manage financial assets. SFAS 71 reflects a paradigm shift by not waiting for objective evidence but rather continuously updating and recognizing asset risks from initial recognition to final maturity. With an increase in the risk of debtor default as an indication of a financial asset value decrease, this forward impairment loss reserve can directly affect the quality of company earnings (Dendy, 2019). In February 2020, Islamic banks in aggregate were recorded to have formed impairment loss reserves up to

IDR248.92 trillion. Then, in May 2020, the bank impairment loss reserve increased by IDR 21.24 trillion or 8.53% to IDR 270.16 trillion.

Based on this background, this study analyzes whether the impairment loss reserve referring to SFAS 71 affects earnings quality. Several studies have been conducted regarding SFAS 71. Research conducted by Arifullah & Firmansyah (2020) evaluates the readiness of banking companies to implement SFAS 71 on receivables provisions. Research on the difference in the value of impairment loss reserve before and after the implementation of SFAS 71 in conventional banking has also been carried out previously by Harindra et al. (2023) and Firmansyah et al. (2022). Harindra et al. (2023) conducted an empirical study on the implementation of SFAS 71 and its impact on the profitability of banking companies in Indonesia. The findings indicate that impairment loss reserve positively influences the profitability of companies, contrasting with the period before the implementation of SFAS 71 when the impairment loss reserve did not affect profitability. Additionally, research by Firmansyah et al. (2022) concludes that the adoption of SFAS 71 results in a notable change, specifically an increase in the value of impairment loss reserve, which is a component that reduces equity in the financial statements of listed banks on the Indonesia Stock Exchange in the years 2019 and 2020. The application of impairment loss reserve on murabahah income and its relation to the financial performance of Islamic Commercial Banks was conducted (Suhartini & Anwar, 2018).

This research offers two novelties. First, this research analyzes content regarding the application of the forward-looking expected loss method in accordance with SFAS 71 in Islamic commercial banks which only became effective in 2020 to calculate reserves for impairment losses. By using dummy variables, this research compares forward-looking loss reserves in 2020 and 2021 which refers to SFAS 71, and loss reserves in 2019 and 2018 which refers to SFAS 55. Second, in context, this research involves abnormal economic conditions due to the impact of COVID-19, which will influence the number of loss reserves created by banks. The implementation of SFAS 71 began in 2020, as a result, the research periods are not only capturing the impact of SFAS 71 but also the impact of the pandemic on potential declines in the value of financing.

Using 16 Islamic commercial bank financial statement data from 2018 to 2021, this study was analyzed using the Panel Regression Analysis technique. This research contributes by highlighting the positive role of implementing SFAS 71 in improving the profit quality of Islamic banks. By considering macro factors that may occur in the future, SFAS 71 helps produce more accurate and predictable profit information.

2. Literature Review and Hypothesis Development

Fiedler (1998) developed contingency theory, which incorporates that the design and use of management control systems are highly dependent on the organizational context. In other words, contingency theory is a management theory in which no one approach or method is suitable for all organizational practices. Instead, this theory argues that the most effective practices depend on an organization's unique circumstances or possibilities. The contingency theory in the accounting context recognizes that each organization has unique characteristics and environments that affect its accounting practices (Otley, 2019). Banks, in anticipating uncertainty, are required to create reserves for financing losses, and even

Islamic banks prohibit the practice of interest. It presents challenges and various business risks, one of which is financing risk, which arises from the uncertainty of the return on financing activities (Sholahuddin, 2004). The amount of this reserve will depend (contingent upon) on the conditions of each customer, the internal condition of the individual bank such as bank size, liquidity, efficiency, and profits (Andayani et al., 2022) as well as macroeconomic conditions that affect the customer's business.

Before the introduction of SFAS 71, SFAS No. 55 was previously utilized as a guideline for the recognition and determination of reserves for Impairment Losses on financial instruments by Islamic banks. In SFAS 55, the determination of reserve generally relied on the Historical Loss method, which focused on past loss experiences. While SFAS 55 provided reliable guidelines, the replacement with SFAS No 71 reflects an evolution in approach, particularly with the introduction of the Forward-Looking Expected Loss approach (Mukaromah & Krisnaningsih 2023). This practice helps financial institutions proactively manage the potential for abnormal conditions such as the COVID-19 pandemic. However, the obligation of banks to provide loss reserve on non-performing financing is greater than before, which can also decrease bank profits (Firmansyah et al., 2022). The previous study by Tungga et al.(2021), Prena & Nareswari (2022) and Hasibuan et al. (2023) state that CKPN using the Expected Loss method significantly affects the quality of banking profits. Therefore, Islamic banks also need to consider the right strategy to manage the risk of non-performing financing and ensure long-term profit sustainability.

The Islamic banking industry in Indonesia has a significant role in the economy, with a growing market share of Islamic banking. Banks function as financial intermediaries that collect funds from the public and distribute them in the form of financing (Primandasetio, 2021). However, banks face financing risks (Riyanah et al., 2023). Especially during the COVID-19 pandemic, the financing risk has an impact on increasing the Non-Performing Financing (NPF) ratio (Gemina & Supriyadi, 2018; Nugrohowati & Bimo, 2019), which can also threaten their liquidity (Hamdi & Herianingrum, 2022). Thus, banks need to implement earnings management strategies to survive economic uncertainty.

From the regulatory side, one of the efforts to mitigate financing risks, the Financial Services Authority (OJK) has established regulations regarding Reserve for Impairment Losses based on Forward-Looking Expected Loss Under SFAS No 71 to maintain the stability of the banking business (Otoritas Jasa Keuangan, 2020). Previous research shows that banks that have adequate loss reserves have a greater chance of surviving and recovering from crises such as COVID-19 (Mla & Rizkianto 2023; Burhan, 2023; Hasan & Syahira, 2022). The application of Forward-Looking Expected Loss which refers to SFAS 71 takes into account expectations of future losses, thereby allowing banks to predict profits more accurately. This is important because the predictability of earnings is an indicator of quality earnings. Previous research shows that the Forward-Looking Expected Loss method produces more accurate credit loss estimates than traditional methods. This is proven by research by Suriawinata (2023) which found that Forward-Looking Expected Loss was able to predict Non-Performing Loan with a higher level of accuracy than the loss incurred method. In addition, research states that a high loss reserve can produce more accurate earnings quality because it can predict profits better, so it can influence the

quality of the company's profit. Furthermore, findings by Valdiansyah & Murwaningsari (2022) show that low or even negative profits can be caused by excessive loss reserve policies, which ultimately reflect poor asset quality and increase the bank's financial risk. Based on the framework that states that the COVID-19 pandemic impacts the increase in non-performing financing, Islamic banks decided to set a larger Reserve for Impairment Losses. In line with this, the greater the reserve set by Islamic banks, the greater the possibility of earnings management, which harms the quality of Islamic banks' earnings. Therefore, this study proposes the following hypothesis:

H_1 : Earnings quality is higher when implementing Forward-Looking Expected Loss under SFAS No. 71.

3. Research Method

The population for this study comprises Islamic banking entities registered with the Financial Services Authority. Purposive sampling was employed for sample selection. Samples were chosen based on the following criteria:

Table 1. Sampling Criteria

No	Criteria	Total
1.	Islamic banking registered with the Financial Services Authority (OJK) 2018-2021	17
2.	Islamic banking is officially registered with the Financial Services Authority (OJK) in 2021	(1)
3.	Islamic Banks is not implementing PSAK 71 starting January 1, 2020	0
4.	Total banks used in the research	16
5.	Total observations (4 years x 16 banks)	64

This study used 16 samples of Islamic commercial banks in Indonesia, with a research period of 4 years. However, three banks, experienced a merger into one banking entity in 2021, so the research subjects became 14 starting in 2021. In the research span of 4 years, 55 financial years are the focus of analysis. The secondary data used in this study are annual financial reports of Islamic commercial banks obtained from www.ojk.go.id. This research used a panel data regression analysis with the following model:

$$EQ_{i.t} = a + b_1RIL_{i.t} + b_2RIL*DY_{i.t} + b_3LIQ_{i.t} + b_4EFF_{i.t} + b_5SIZE_{i.t} + b_6DY + E_{i.t}$$

Where,

$EQ_{i.t}$: Earnings quality of Indonesian Islamic Commercial Banks
a : Constant value
$b_{1.....6}$: Regression coefficient value
$RIL_{i.t}$: Reserve for impairment losses of murabahah
$RIL*DY_{i.t}$: Interaction between reserve for impairment losses and dummy year
$LIQ_{i.t}$: Liquidity of Islamic commercial bank in year t
$EFF_{i.t}$: Efficiency of Islamic commercial bank in year t
$SIZE_{i.t}$: Company size of Islamic commercial bank in year t
DY : Dummy year, 0 for years before SFAS 71, and 1 for after SFAS 71.
$E_{i.t}$: *Error term*

This model consists of a dependent variable, independent variable, and control variable presented in Table 2 about measurement variables. Earnings quality shows how much profits banks report correspond to actual reality (Utami et al., 2019). In this research, earnings quality is measured using the earnings predictability indicator (Yetty et al., 2022), which means the company can provide accurate and consistent forecasts of its financial performance in the future. The higher the level of earnings predictability, the more reliable the company's financial information and the higher earning quality. Schiemann & Guenther (2013) explain that earnings predictability is measured from the residual standard deviation of the earnings persistence formula. The impairment loss reserve for Murabahah Financial is an independent variable. This model detects risks in financial instruments since initial recognition using forward-looking information based on IFSA Circular Letter No. 9/SEOJK.03/2020 (Otoritas Jasa Keuangan, 2020).

In this research, control variables consist of liquidity, efficiency, bank size, and the Covid pandemic. Liquidity is the company's ability to meet its financial obligations in the short term with available current funds (Gusmawanti et al., 2020; Pham et al., 2018). Efficiency is a measure that compares the output value of a process with its input value (Prena & Nareswari, 2022). This study's efficiency measurement uses the. BI Circular Letter No.6/23 / DPNP issued on May 31, 2004, states that if the ratio level is at < 96%, management is good at controlling expenses or operating expenses with operating income and vice versa. Bank size is the level of identification of the size or size of a bank (Yuniari & Badjra, 2019), which is measured by Ln total financing (Damayanti & Mawardi, 2022).

Table 2. Measurement of Variables

No	Variables	Measurement
Dependent Variable		
1.	Earnings Quality	Earnings predictability indicator. $ER_t = a + ER_{i\,t-1} + e_{i.t}$ ER_t : Earnings at bank i in year t a : Constant Value. $ER_{i.t-1}$: Earnings at the bank i in before year t. $e_{i.t}$: *Error term*
Independent variable		
2.	Impairment loss reserve for Murabahah financial	Expected Loss method: $\frac{CKPN\ on\ Financial\ Assets}{Total\ Productive\ Assets}\ X\ 100\%$
Control Variables		
3.	Liquidity	Financing to Deposit Ratio (FDR): $\frac{Total\ Funds\ provided}{Total\ Third\ Party\ Funds}\ X\ 100\%$
4.	Efficiency	Operating Expenses and Operating Income (BOPO) ratio $\frac{Total\ Operating\ Expenses}{Total\ Operating\ Income}\ X\ 100\%$
3.	Bank Size	$Bank\ Size = Ln\ (Total\ Financing)$
4.	Dummy COVID-19	Time dummy variable: 1 = After the COVID-19 crisis in 2020-2021, 0 = Before the COVID-19 crisis in 2018-2019

In this study, panel data regression was analyzed using STATA software. The analysis uses three approaches, namely CEM (Common Effect Model), FEM (Fixed Effect Model), and REM (Random Effect Model). Napitupulu et al (2021) explain that to choose the right model, there are several tests. The first, namely the Chow test, is used to select the most appropriate model for estimating panel data between the CEM or FEM models. Second, the Hausman test is used to determine the most appropriate FEM or REM model to estimate panel data. Coefficient of determination analysis is conducted to explain the relationship between dependent variables and independent variables in the research model.

4. Result and Discussions

Table 3 presents descriptive data for earnings quality, loss reserve, liquidity, efficiency, bank size, and year dummy variables on a sample of Islamic commercial banks during the 2018–2021 period.

Table 3. Descriptive Statistics

Variable	Scale	Mean	Std. dev.	Min	Max
RIL 2018-2019	Millions	.0239934	.0160708	0	.61196
RIL 2020-2021	Millions	.0366108	.0280699	0	.61196
Liquidity	Ratio	.0540489	.0267152	.0257835	.2402401
Efficiency	Ratio	4.520682	.3171598	4.028205	6.060057

Source: Research Data, 2024

Reserve for Impairment Loss with a standard deviation of 0.016 shows that reserve values generally tend to vary within a relatively small range around an average value of 0.0239 million. The forward-looking reserve, which is the reserve value for 2020 and 2021 after SFAS 71 becomes effective, has a mean value of 0.0366, which is higher than the overall reserve value. This indicates that SFAS 71 has an impact on increasing the value of reserves made by banks. The liquidity ratio shows large variations in banks' ability to manage liquidity, with a mean of 0.0540489 and a standard deviation of 0.0267152. The Efficiency Ratio reflects variations in operational efficiency between banks, with an average ratio of 4.520682 and a standard deviation of 0.3171598.

In testing the hypothesis, this study begins with an analysis of earnings predictability as the indicator of earnings quality as presented in Equation 2. Using the procedure of panel data regression, the final equation is generated through the Chow, Haussman, and Lagrange Multiplier (LM) tests to select the most appropriate model between the CEM (Common Effect Model), FEM (Fixed Effect Model), and REM (Random Effect Model) (Napitupulu et al., 2021). The Chow test results show a Prob value of 0.1405>0.05, so the selected model is CEM. Then, the Lagrange Multiplier Test compares REM with the CEM, and the results confirm that a Prob value of 1,000>0.05, so the best model is the CEM. After passing the classical assumption test of multicollinearity and heteroscedasticity, the following equation 3 is obtained for the earnings predictability model: $ER_t = 134{,}98 + 0{,}40ER_{i.t-1} + E_{i.t.}$

Referring to equation 3, earnings predictability as the dependent variable is measured from the residual standard deviation. This study then carries out the panel data regression to test the influence of all independent variables on earnings predictability as the dependent variable using Equation 1. The Chow test is conducted to determine whether the model used is a common effect or a fixed effect. If the probability is > 0.05, the approach used has a common effect. Conversely, if the probability is <0.05, then the model used is a fixed effect (Napitupulu et al., 2021). Based on the results obtained, the Prob value is 0,0003< 0.05. Then, the selected model is FEM. The next step is the Hausman test, The Probability value is 0,1964 >0,05, so, the selected model is REM. The last test is the Lagrange Multiplier (LM) compares REM with the CEM, and the results confirm that a Prob value of 0,1447>0.05, so the best model is the CEM (Common Effect Model). The LM test determines whether the Random Effect model is better than the Common Effect method. If the probability value of Breusch-Pagan> 0.05, the suitable model is the Common Effect Model and vice versa (Napitupulu et al., 2021). Based on the results obtained, the Prob value of 0.2007> 0.05, the selected model is Common Effect. The common and fixed effect models use the OLS (ordinary least square) methods. Meanwhile, the Random Effect model is an estimation method that uses the GLS method. This study uses a common-effect approach. Therefore, the classic assumption test must be carried out. Based on (Napitupulu et al., 2021) with the common effect model, researchers only need to test for multicollinearity and heteroscedasticity. To test for multicollinearity problems, you can look at the correlation matrix of the independent variables. If there is a correlation of more than 0.85, there is multicollinearity (Napitupulu et al., 2021). Based on the multicollinearity test results, all independent variables have a value of less than 0.05, so it can be concluded that there is no multicollinearity in the model. Furthermore, in the heteroscedasticity test, the Breusch Pagan Godfrey results using the probability chi-square parameter with a value of 0.9624 are greater than the probability value of 5% (0.05), so it is concluded that the regression model is homoscedasticity. Based on the model selection test conducted, the common effect model is used in estimating panel data in this study.

Table 4. Common Effect Model Regression Test Results

Variables	Coefficient	Std. err.	t	P>t
_cons	9.86785	1.418482	6.96	0.000
RIL	-.1199505	.0587557	-2.04	0.047
RIL*DY	2.133402	.7264731	2.94	0.005
Liquidity	-6.377887	2.552937	-2.50	0.016
Efficiency	-.9487072	.3068849	-3.09	0.003
Size Bank	.1863462	.0659417	2.83	0.007
DY	-.3976383	.2028015	-1.96	0.056
Adj. R^2 = 0.3884;				
Sig F = 0.0001.				

The F value based on the results of panel data regression testing is 6,50 with a probability of less than 5%, indicating that the overall model fits the data. The model can explain variations in earnings quality by 38,84%. Based on the test of each variable, almost

all variables significantly influence earnings quality: Reserve for Impairment Loss (RIL), RIL*DY after implementing SFAS 71 for the years 2020 and 2021, Liquidity, efficiency, and bank size. Meanwhile, the year dummy variable is in a marginal position, meaning that the period of 2020 and 2021 which represents the pandemic condition has an influence on earnings quality but with a fairly weak influence.

Referring to Table 4, the overall Reserve for Impairment Loss has a significantly negative impact on the earnings quality of Islamic Banks, shown by the coefficient value of -0.119 with a probability of 0.005 < 0.05. The higher the reserve, the lower the earnings quality. This means that an increase in reserves causes current earnings information to have a decreased ability to predict future earnings.

Interestingly, the implementation of Forward Impairment Loss Reserve based on SFAS 71, which uses Expected Financing Loss (EFL), has been proven to have a significant influence on earnings quality as shown by the coefficient value of RIL*DY 2.133 with a probability of 0.047 <0.05. These findings can be statistically interpreted from two points of view. Firstly, the implementation of SFAS 71 which is effective in 2020 changes the direction of the influence of the reserve for impairment loss on earnings quality, from previously the higher the reserve, the lower the ability of earnings to predict future earnings, to the higher the reserve, the higher the ability of current earnings to predict future earnings. The finding may be attributed to SFAS 71 which can accommodate future macro factors that have the potential to influence business performance (Sugiarto & Suroso, 2020). Compared to SFAS 55, this approach encourages accountants to be more careful in assessing and can strengthen proactive and preventive aspects of risk management. As a result, reserve based on SFAS 71 provides a stronger basis for capturing the variability of complex and dynamic market conditions, reflecting earnings quality with a higher degree of precision. Therefore, the hypothesis is accepted.

Forward-looking loss reserves have accommodated significant economic uncertainty and profound changes in the business environment, which are likely to cause instability in corporate financial performance (Lassoued & Khanchel, 2021). External factors such as market fluctuations, supply chain disruptions and unexpected changes in consumer behavior can all have impacts that are difficult to predict, reducing the ability of earnings to provide consistent and reliable information as a basis for predicting future financial results (Ozili, 2021), therefore needs to be anticipated by taking into account the risk of loss due to these external factors in the forward-looking loss reserve.

Bank size as a control variable has a significantly positive impact on profit predictability. This indicates that larger banks have more diverse asset and funding portfolios which can help banks to be more resistant to economic and market fluctuations so that earnings will be more predictable. Other variables, namely liquidity (FDR) and efficiency (BOPO) have a negative and significant impact on earnings predictability. An increase in the FDR ratio indicates high liquidity risk and has the potential to increase non-performing financing thereby reducing earnings quality. Meanwhile, a high BOPO ratio indicates high operational costs. Therefore earnings obtained will be lower.

This research aims to analyze the effect of implementing reserve impairment loss using the Expected Loss approach in accordance with SFAS 71 on the earnings quality of Islamic Banks in Indonesia. Earnings quality is measured using the earnings predictability

value, where the more accurately the predicted earnings, the higher the earnings quality (Abou-El-Sood & El-Sayed, 2022). From the findings, Islamic banks tend to apply the principles of prudent banking to anticipate the possibility of an increase in risk caused by macro factors. The principle of prudent banking is an approach that means that Islamic banks in Indonesia tend to be very careful in recognizing income and expenses. One of the impacts of implementing the prudential banking concept is determining a comprehensive loss reserve by considering possible risks that occur in the future that will affect earnings. In Islamic banks, prudence in recognizing earnings, especially through Murabahah financing is crucial as Murabahah financing is dominant compared to other modes of financing. It needs to be taken into account that this financing also carries risks that need to be anticipated. In contrast to SFAS 55, reserve impairment loss in SFAS 71 using the Expected Financing Loss method provides a framework that estimates financing risk from the start, which ultimately influences the increase in Allowance for Impairment Losses in the banking sector, especially when faced with unexpected events such as the COVID-19 pandemic. The finding shows that the application of Expected Loss to Murabahah financing has a significant impact on improving the earnings quality of Islamic Banks in Indonesia.

These findings are consistent with research by Suriawinata (2023) which found that Forward-Looking Expected Loss was able to predict Non-Performing Loans with a higher level of accuracy than the loss incurred method. In addition, research by Atika (2017) states that a high loss reserve can produce more accurate earnings quality because it can predict profits better, so it can influence the quality of the company's profit. Furthermore, findings by Valdiansyah & Murwaningsari (2022) show that low or even negative profits can be caused by excessive loss reserve policies, which ultimately reflect poor asset quality and increase the bank's financial risk.

However, this finding is not consistent with previous studies which indicate that the higher the reserve, the lower the earnings quality of Islamic banks. For example, research conducted by Maurida (2022), highlights the impact of high reserves on reducing bank net profits, and similar findings by Hasibuan et al. (2023) show that reserve SFAS 71 has a negative influence on earnings quality in banking sub-sector companies on the Indonesia Stock Exchange. An excessive increase in the reserve for impairment loss can reduce net profit. Diah & Sholikhah (2016) also found that reserve for impairment loss has a positive influence on NPF, which means that the higher the reserve for impairment loss, the higher the level of problematic financing in banks. This will have an impact on reducing the quality of profits in banking. Likewise, Valdiansyah & Murwaningsari (2022) added the dimension that high reserve for impairment loss policies can also contribute to low or even negative profits.

The year dummy variable has a value of 1 for the 2020 and 2021 periods, which are the effective years when SFAS 71 was implemented, which coincides with the pandemic and appears to have had a marginal impact on the decline in the quality of profits in banking. The pandemic situation causes an increase in credit risk because a lot of financing is provided to customers who may experience difficulties in repayment. However, due to tight regulations and the strength of the banking system, the impact on decreasing earnings quality is not that strong (probability 0.056, significant if the test is 10%). The uncertain

economic situation during the pandemic makes it difficult for banks to provide stable and predictable profit information, but banks can respond proactively to the crisis that occurs (Augeraud-Véron & Boungou 2023). Islamic Banks choose to anticipate potential losses and protect assets, although this has a negative impact on short-term profits, this step strengthens their position in the long term (Rastogi et al., 2022). By calculating potential losses and setting up reserves, demonstrating that they can manage risks and adapt to changing market conditions, increases investor and customer confidence, which can ultimately help banks recover more quickly after the pandemic ends. In line with research that shows that banks that have adequate reserves have a greater possibility of surviving and recovering from the crisis (Mla and Rizkianto 2023; Burhan 2023; Hasan & Syahira 2022).

The utilization of robustness tests in this study substantiates the reliability of the analytical model. This study examines the same model using different measures of earnings quality, namely accrual quality as previously used by Lyimo (2014), An (2017), Selfiani & Murtanto (2020), Fonou Dombeu & Nomlala (2023). This study uses discretionary loan loss provision (DLLP) as the measure of earnings quality (Zgarni & Fedhila, 2019; Hegde & Kozlowski, 2021). The higher the DLLP, the lower the quality of earnings. The finding indicates that the impact of Reserve Impairment Loss after implementing SFAS 71 (RIL*DY) on earnings quality is significantly negative, suggesting that the implementation of Forward Impairment Loss Reserve based on SFAS 71 in the years 2020-2021, utilizing Expected Financing Loss (EFL), reduces Discretionary Loan Loss Provision (DLLP), indicating a higher earnings quality. With a coefficient of 14.881 and a probability of less than 5%, strong support is provided for this finding. This robustness test yields a consistent result when earnings quality is measured through earnings predictability. Table 5 presents the robustness test.

Table 5. Common Effect Model Regression Test Results

Variables	Coefficient	Std. err.	t	P>t
_cons	-18.913	10.843	.091	0.028
RIL	56.377	12.913	-1.465	0.010
RIL*DY	-14.881	30.887	1.825	0.004
Liquidity	-.026	39.984	.372	0.011
Efficiency	-.014	.052	-.511	0.002
Size Bank	1.345	.076	-.180	0.008
DY	.990	2.623	.513	0.004
Adj. R^2=.481; Sig. F=.0004				

Dependent Variable: Accrual Quality using DLLP

RIL: Reserve Impairment Loss; DY: Dummy Year (0: before SFAS 71; 1 after SFAS 71)

5. Conclusions, Implications, and Limitations

By considering the variables size, liquidity, and efficiency, as controlling variables, based on the results of hypothesis testing, it can be concluded that the higher the reserve of an Islamic bank, the lower the quality of earnings. However, after the implementation of SFAS 71, the higher the reserve, the higher the earnings quality. SFAS 71 uses Expected

Financing Loss, which considers macro factors that are likely to occur in the future that influence earnings. These findings indicate that reserves based on SFAS 71 are more comprehensive in predicting risks that may arise. Therefore earnings information is more accurate and has more predictability. The implication of this research for regulators is as input in drafting regulations on reserves. The impairment loss reserve may reduce the quality of earnings, which is prone to being used as an earnings management tool. For investors, the results of this study are input in evaluating Islamic bank performance as an investment alternative. The limitation of this research is the use of a single measure for earnings quality, namely only the predictability of earnings over two years, so it does not describe the trend of the impact of impairment loss reserves (CKPN) on earnings quality. Future research could examine the impact of CKPN on various earnings quality measures, including earnings predictability over three years to provide a more comprehensive understanding. In addition, it is realized that the data available in this study is relatively limited. Therefore, it is recommended to conduct further research using cross-country data. This can expand the scope and generalization of research results, as well as provide a more comprehensive understanding of the phenomenon being observed.

References

Aboud, A., Roberts, C., & Mansour Zalata, A. (2018). The impact of IFRS 8 on financial analysts' earnings forecast errors: EU evidence. *Journal of International Accounting, Auditing and Taxation*, *33*, 2–17. https://doi.org/10.1016/j.intaccaudtax.2018.08.001

An, Y. (2017). Measuring earnings quality over time. *International Journal of Economics and Financial Issues*, *7*(3), 82–87.

Andayani, E., Prasetyo, A., & Yusuf, M. (2022). Factors affecting management accounting practices and their impact on organizational performance in the private sector in Jakarta. *Jurnal Riset Akuntansi 14*(1), 1–19. https://doi.org/10.24036/jea.v5i4.1134

Atika. (2017). Analisis penerapan PSAK No. 50 & 55 atas cadangan kerugian penurunan nilai (CKPN) pada PT. Bank Sumut. *Jurnal Akuntansi Bisnis dan Publik, 8* (1), 20-31.

Augeraud-Véron, E., & Boungou, W. (2023). The impact of COVID-19 on bank profitability: Cross-country evidence. *SSRN Electronic Journal*, *4*(1), 10–12. https://doi.org/10.2139/ssrn.4318881

Binekasri, Romys. (2023). Potensi keuangan syariah di Indonesia sebesar ini. CNBC Indonesia.

Burhan, F. A. 2023. Siap-siap restrukturisasi kredit berakhir, Mandiri BCA Cs Amankan Pencadangan. *Bisnis.Com [Online]. Web. 7 Mar. 2024*

Damayanti, A. C., & Mawardi, W. (2022). Pengaruh ukuran bank (size), loans to deposit ratio (LDR), capital adequacy ratio (CAR), non-performing loans (NPL), diversifikasi pendapatan, dan BOPO terhadap kinerja bank di Indonesia (Studi pada bank umum konvensional yang terdaftar di BEI tahun 2016-2020). *Diponegoro Journal of Management, 11*(1). Retrieved from https://ejournal3.undip.ac.id/index.php/djom/article/view/33940

Dong, X., Liu, J., & Hu, B. (2012). Research on the relationship of commercial bank's loan loss provision and earning management and capital management. *Journal of Service Science and Management*, *05*(02), 171–179. https://doi.org/10.4236/jssm.2012.52021

Firmansyah, A., Ningrum, N. C., & Lubis, P. M. (2022). Cadangan kerugian penurunan nilai piutang perusahaan perbankan sebelum dan setelah implementasi PSAK 71. *Journal of Financial and Tax*, *2*(1), 32–47. https://doi.org/10.52421/fintax.v2i1.206

Firmansyah, A., Rizky, M., & Qodarina, N. (2022). Manajemen laba sebelum dan setelah penerapan PSAK 71 pada perusahaan subsektor perbankan di Indonesia. *Owner*, *6*(2), 1363–1372. https://doi.org/10.33395/owner.v6i2.706

Fisher, J. G. (1998). Part II. Social and Behavioral Sciences Applications in Accounting and Management Control Research - Contingency Theory, Management Control Systems, and Firm Outcomes: Past results and future directions. *Behavioral Research in Accounting, 10. Web. 7 Mar. 2024*

Fonou Dombeu, N. C., & Nomlala, B. C. (2023). Earnings quality research: Trend, recent evidence and future direction. *International Review of Management and Marketing*, *13*(5), 1–8. https://doi.org/10.32479/irmm.14577

Gemina, D., & Supriyadi, D. (2018). The effect of murabahah, mudharabah and ijarah earnings upon the profit of Bank BRI Syariah, branch office Sukabumi. *The Management Journal of Binaniaga*, *3*(01), 35. https://doi.org/10.33062/mjb.v3i1.239

Ginoga, L. F., & Syahwani, A. K. I. (2022). Analisis dampak NPL, CKPN, LDR, dan suku bunga kredit terhadap penyaluran kredit perbankan pada masa pandemi COVID-19. *Ekonomi & Bisnis*, *21*(1). https://doi.org/10.32722/eb.v21i1.4569

Gusmawanti, A., Supaijo, S., Iqbal, M., & Fasa, M. I. (2020). The nexus between FDR, NPF, BOPO toward profitability of Indonesian Islamic bank. *Al-Amwal : Jurnal Ekonomi dan Perbankan Syari'ah*, *12*(2), 167. https://doi.org/10.24235/amwal.v12i2.7155

Hamdi, B., & Herianingrum, S. (2022). Determinan risiko likuiditas bank syariah dan konvensional sebelum dan selama pandemi Covid-19. *Jurnal Ekonomi Syariah Teori dan Terapan*, *9*(4), 573–585. https://doi.org/10.20473/vol9iss20224pp573-585

Hana, K. F., Aini, M., & Putri Karsono, L. D. (2022). Pandemi Covid 19: Bagaimana kondisi likuiditas bank syariah di Indonesia? *Al Maal: Journal of Islamic Economics and Banking*, *4*(1), 16. https://doi.org/10.31000/almaal.v4i1.5840

Hasan, Z., & Syahira, N. (2022). Opportunities and challenges of Islamic banks during the COVID-19 pandemic. *Jurnal Multidisiplin West Science*, *01*(02), 57–64. https://doi.org/10.58812/jmws.v1i02.19

Hasibuan, A., Juliyanto, D., & Firmansyah, A. (2023). Dampak implementasi PSAK 71 pada kinerja perusahaan perbankan di Indonesia. Financial and Tax, 3(1), 15-27. www.idx.co.id. https://doi.org/10.52421/fintax.v3i1.377

Hegde, S. P., & Kozlowski, S. E. (2021). Discretionary loan loss provisioning and bank stock return: The Role of economic booms and busts. *Journal of Banking & Finance*, *130*, 106186. https://doi.org/10.1016/j.jbankfin.2021.106186

Kanagaretnam, K., Lobo, G. J., & Mathieu, R. (2004). Earnings management to reduce earnings variability: Evidence from bank loan loss provisions. *Review of Accounting and Finance*, *3*(1), 128–148. https://doi.org/10.1108/eb043399

Khasanah, S. K. A. K. (2022). Analisis perbandingan kualitas laba sebelum dan sesudah implementasi PSAK 71 pada perbankan yang terdaftar di Bursa Efek Indonesia. *E-Journal Field of Economics, Business, and Entrepreneurship 1* (4), 391-399 https://doi.org/10.23960/efebe.v1i4.54

Lyimo, G. D. (2014). Assessing the measures of quality of earnings: Evidence from India. European Journal of Accounting Auditing and Finance Research 2(6), 17-28.

Maurida, Z. M. (2022). Analisis penerapan expected credit loss (ECL) terhadap pembentukan cadangan kerugian penurunan nilai menurut PSAK No. 71 pada lembaga pembiayaan di Indonesia. *Jurnal Akuntansi dan Keuangan*, *27*(2), 120–131. https://doi.org/10.23960/jak.v27i2.373

Mla, P. B., & Rizkianto, E. (2023). Analysis of pandemic influences on nonperforming loans in Bank XYZ for the period of 2020-2022. *Dynamic Management Journal 7*(2), 254–268.

Napitupulu, R. B., Simanjuntak, T. P., Hutabarat, L., Damanik, H., Harianja, H., Sirait, R. T. M., & Tobing, C. E. R. L. (2021). P*enelitian Bisnis : Teknik dan Analisa Data dengan SPSS - STATA - EVIEWS*. Madenatera, 1, 230.

Nugrohowati, R. N. I., & Bimo, S. (2019). Analisis pengaruh faktor internal bank dan eksternal terhadap Non-Performing Financing (NPF) pada bank perkreditan rakyat syariah di Indonesia. *Jurnal Ekonomi & Keuangan Islam*, *5*(1), 42–49. https://doi.org/10.20885/jeki.vol5.iss1.art6

OJK. (2020). *Statistik Perbankan Syariah 2020*, *53*(9), 1689–1699. *[Online]. Web. 14 Feb.*

OJK. (2023). Statistik Perbankan Indonesia - April 2023. *Statisktik Perbankan Indonesia April 2023*, *21*. *[Online]. Web. 14 Feb. 2024*

Otley, D. T. (2019). The contingency theory of management accounting: Achievement and prognosis. *Management Control Theory*, *5*(1980), 305–320. https://doi.org/10.1007/978-1-4899-7138-8_5

Otoritas Jasa Keuangan. (2020). Peraturan OJK Nomor 48/POJK.03/2020. *Peraturan OJK Nomor 48/POJK.03/2020*, *53*(9), 1689–1699. *[Online]. Web. 14 Feb. 2024*

Pane, A. A., & Rahmadhani, S. N. (2021). Pengaruh struktur modal dan volatilitas laba terhadap kualitas laba PT. Bank Sumut. *Jurnal Akuntansi dan Bisnis*, *7*(1), 81–89. https://doi.org/10.31289/jab.v7i1.4476

Prena, G. Das, & Nareswari, S. K. D. (2022). Pengaruh penerapan PSAK 71, BOPO dan NPL terhadap profitabilitas pada perbankan yang terdaftar di BEI . *Wacana Ekonomi (Jurnal Ekonomi, Bisnis dan Akuntansi)*, *21*(September), 175–184. https://doi.org/10.22225/we.21.2.2022.175-184

Primandasetio, J. (2021). *Ekonomi syariah* (A. Rasyid, Ed.; pertama). Departemen Ekonomi dan Keuangan Syariah - Bank Indonesia. *[Online]. Web. 13 Oct. 2023*

Rastogi, S., Sharma, A., Pinto, G., & Bhimavarapu, V. M. (2022). A Literature review of risk, regulation, and profitability of banks using a scientometric study. *Future Business Journal*, *8*(1). https://doi.org/10.1186/s43093-022-00146-4

Riyanah, R., Purwanti, Y., & Astutik, W. S. (2023). Analisis rasio likuiditas untuk mengetahui pengaruh corona pada kinerja keuangan perbankan syariah di Indonesia. *Moneter - Jurnal Akuntansi Dan Keuangan*, *10*(1), 72–79. https://doi.org/10.31294/moneter.v10i1.15641

Rusydiana, A. S., Herindar, E., & Laila, N. (2022). The impact of COVID-19 on Islamic economics and finance industry: Text analytics using R. *Global Review of Islamic Economics and Business*, *9*(2), 055. https://doi.org/10.14421/grieb.2021.092-05

Schiemann, F., & Guenther, T. (2013). Earnings predictability, value relevance, and employee expenses. *The International Journal of Accounting*, *48*(2), 149–172. https://doi.org/10.1016/j.intacc.2013.04.001

Selfiani, & Murtanto. (2020). The effect of accrual quality to share price synchronization with Good Corporate Governance (GCG) as a moderating variable. *South East Asia Journal of Contemporary Business, Economics and Law*, *23* (1), 135–146. https://doi.org/10.32509/jakpi.v2i1.2043

Sholahuddin, M. (2004). Risiko pembiayaan dalam perbankan syariah. *Benefit* 8(2), 130-138.

Sobarsyah, M., Soedarmono, W., Yudhi, W. S. A., Trinugroho, I., Warokka, A., & Pramono, S. E. 2020. Loan growth, capitalization, and credit risk in Islamic banking. *International Economics*, *163*(December), 155–162. https://doi.org/10.1016/j.inteco.2020.02.001

Suhartini, M., & Anwar, S. (2018). Penerapan cadangan kerugian penurunan nilai, pendapatan murabahah dan kinerja keuangan pada bank umum syariah tahun 2014. *Liquidity*, *5*(2), 119–126. https://doi.org/10.32546/lq.v5i2.52

Suriawinata, I. S. (2023). The implementation of SFAS 71, bank equity valuation, and the moderating effect of bank size. *The Indonesian Journal of Accounting Research*, *26*(01), 1–24. https://doi.org/10.33312/ijar.648

Tombi, T. N. H., Johan, Burhamzah, D., & Oky Tenri Famauri, A. (2022). Penerapan kebijakan restrukturisasi kredit oleh bank terhadap debitur yang terdampak Covid-19. *Jurnal Sosio Sains*, *8*(1), 72–90. 10.37541/sosiosains.v8i1.674

Utami, R. B., Nuzula, N. F., & Damayanti, C. R. (2019). The effect of earnings quality on financial performance in Indonesia : is the state-owned bank better than private bank? *Asia Pacific Management and Business Application*, *008*(02), 105–116. https://doi.org/10.21776/ub.apmba.2019.008.02.3

Valdiansyah, R. H., & Murwaningsari, E. (2022). Earnings quality determinants in pre-corona crisis: another insight from bank core capital categories. *Asian Journal of Accounting Research*, *7*(3), 279–294. https://doi.org/10.1108/AJAR-08-2021-0134

Vebriana, S. A., Setyowati, D. H., & Nurdin, A. A. (2020). Pengaruh non-performing loan dan loan to deposit ratio terhadap cadangan kerugian penurunan nilai. *Indonesian Journal of Economics and Management*, *1*(1), 245–256. https://doi.org/10.35313/ijem.v1i1.2433

Wijayanti, R., & Diyanti, V. (2017). Pengaruh volatilitas laba, perataan laba dan corporate governance terhadap kualitas laba bank syariah dan konvensional. *Jurnal Akuntansi dan Investasi*, *18*(1), 66-79. https://doi.org/10.18196/jai.18161

Yetty., Imelda, E. & Wirianta, H. (2022). Pengaruh surplus free cash flow terhadap earnings predictability dengan moderasi corporate governance. *Jurnal Paradigma Akuntansi, 4*(1), 366. https://doi.org/10.24912/jpa.v4i1.17528

Yuniari, N. P., & Badjra, I. B. (2019). Pengaruh likuiditas, efisiensi, dan ukuran bank terhadap profitabilitas. *E-Jurnal Manajemen Universitas Udayana*, *8*(6), 3502. https://doi.org/10.24843/ejmunud.2019.v08.i06.p08

Zgarni, A., & Fedhila, H. (2019). Discretionary loan loss provisions, earnings management, and capital management in banks. *WSEAS Transactions on Business and Economics*, *16*(1999), 424–432. https://doi.org/10.5539/ass.v15n7p144