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Effect of Debt Contracts Negotiation Toward Company To Perform Revaluation of Fixed Assets and Its Implications Toward Income Tax Expense

Erly Sherlita
erly.sherlita@widyatama.ac.id

Diana Sari
diana.sari@widyatama.ac.id

Yudhistian Rosavelly Putra Permana
Widyatama University

ABSTRACT

The purpose of this study was to empirically test the effect of negotiating debt contracts (through the level of leverage, the level of secured borrowings and decrease in cash flow from operating activities) as well as the company size against the company on administering the revaluation of fixed asset and the implication on income tax expense. The population of this study focused on the companies that were listed in Indonesian Stock Exchange in 2010. Based on this list, there were 5 companies that administered the revaluation on fixed assets in 2010. As for the companies that did not administer the revaluation of fixed assets, the researcher processed all samples with purposive sampling method. Furthermore, this research also used the secondary data obtained from the Indonesian Stock Exchange. Statistical tests performed used the logistic regression analysis and simple linear regression analysis.The result of the study showed that the level of leverage and the company size had a positive and significant effect on the rate of 10% of the company to administer the revaluation of fixed assets. On the contrary, the level of secured borrowings had a negative and insignificant effect for the company to administer the revaluation of fixed assets although it was originally predicted to be positive. The study also discovered that the decrease in cash flow from operating activities had a positive and insignificant effect for the company to administer the revaluation of fixed assets which overlooked the original prediction to be negative. Revaluation of fixed assets resulted in increased amount of depreciation expense over the useful life of assets, which in turn will reduce taxable income and income tax expense.

Key words :Revaluation of fixed assets, negotiating of debt contracts, level of leverage, level of secured debt borrowings, decrease in cash flow from operating activities, company size, income tax expense.

1. INTRODUCTION

The application of the historical value of fixed assets resulting values that were presented in the balance sheet does not reflect the actual value of the fixed assets, the difference may be lower valuations or higher. Higher valuation could be due to charging of depreciation is too low, this error can be reduced by the application of depreciation methods, usefulness duration and rational depreciation rates are. While undervaluation can be caused due to the rising price of fixed assets in the market, and this can occur due to various factors, such as inflation or currency depreciation.

Because of this, Based on Article 19 of Law no. 7 of 1983 as amended by Law no. 36 of 2008 explained that the Minister of Finance is authorized to establish regulations concerning revaluation (revaluations) of fixed assets and its adjustment factors (acquisition value of fixed assets and depreciation expense). Regulations on revaluation (revaluations) of fixed assets is contained in the Ministerial Regulation of Finance (PMK) No. 79/PMK.03/2008 set on May 23, 2008 governing the revaluation of fixed assets for tax purposes. PMK is effective on the date specified and is the replacement of the Minister of Finance Decree No. 486/KMK.03/2002.

Bintoro (2011) suggested that the Financial Accounting Standards Board (DSAK) from IAI (Indonesian Institute of Accountants) has set year 2008 as a target in which the fundamental differences between PSAK and IFRS is not there anymore. At that time DSAK have prepared Exposure Draft (ED) of the four standards that have been adapted to the corresponding IFRS standards. The most eagerly awaited by analysts and practitioners is the ED of PSAK 16 on fixed assets and other assets.

PSAK 16 (revised 2007) on fixed assets became effective in January 2008, replacing PSAK no. 16 (1994) on fixed assets and others. PSAK 16 (Revised 2007) has many differences with PSAK 16 (1994). Significant differences from PSAK 16 (revised 2007) with earlier is the measurement after initial recognition of fixed assets. Under PSAK No. 16 (revised 2007), the company has the option to choose the cost model or the revaluation model for the measurement of fixed assets. While in the previous PSAK 16, companies are only allowed to use the cost model for the measurement of fixed assets.

Revaluation model presents a measurement of fixed assets recorded at fair value. Thus the revaluation model presenting the financial statements that is more relevant in decision making. However, since the year 2008 where the revaluation was only allowed up to 2010 revaluation is only done by a minority of company listed on the Indonesia Stock Exchange. This is because the implementation costs are relatively large in revaluation and reliability value recorded on the revaluation amount is still in doubt.

According to Mansur and Wardoyo cited by Trisnawati (2005), the reason for the taxpayer revalued fixed assets is not only to present the financial statements to be more relevant in decision making, but also to enhance corporate value making it easier for companies in the process to raise funds through bank loans and the company stock sales, and to increase the burden of fixed assets in the future that allowed greater burden in the future and less tax expense at the present. When viewed from other perspective, with the revaluation of fixed assets the government implementation of provide opportunities in the areas of taxation including revaluation resulted in increasing the amount of depreciation expense over the useful life of assets, which in turn will reduce taxable income and taxes payable in subsequent years. Substantial tax savings for subsequent tax years following the revaluation because of increased depreciation expense is calculated based on the value of the assets that were revalued as its market price has gone up many-fold.

Research on the effect of debt contracts negotiation towards the revaluation of fixed assets has been widely applied, among others, by Cotter and Zimmer (1995), Zimmer (1999), and Seng and Su (2009). The results of these studies indicate that there is still a difference of influence between the leverage with revaluation of fixed assets.

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Debt Contracts Negotiation and Revaluation of Fixed Assets

Companies with higher debt contracts allow managers to use accounting procedures that can increase income or assets of the company (Scott, 2009). By doing the revaluation of fixed assets, it is expected to increase the value of the company's assets; therefore companies with higher debt contracts tend to do a revaluation of fixed assets that are expected to enhance the value of corporate assets.

Two main factors of negotiating debt contracts that can affect the revaluation of fixed assets as done Seng and Su (2010) in previous research is the level of leverage and decreasing cash flow from operations. In addition researchers also added a level of debt assurance which is also a debt contracts negotiation according to Cotter and Zimmer (1995).

Leverage levels and Revaluation of Fixed Assets

By doing the revaluation of fixed assets corporate leverage ratios are expected to decline, due to an increase in corporate assets due to revaluation. This decreasing leverage ratio can pull back the creditor trust because the creditor believes that the high company's net assets will be able to pay credit they provided if the company is liquidated

Lin and Peasnell in Seng and Su (2009) who conducted a revaluation study in the UK using two different samples, and the results of both studies suggest that there is a positive relationship between the action upward revaluations with its debt agreements. It is expected that companies with high leverage tend to use upward revaluation in expanding asset base and reduce the ratio of debt to restore the corporate borrowing capacity.
H_1: The level of leverage is a positive influence on the company to perform revaluation of fixed assets.

Debt Assurance Rate and Fixed Assets Revaluation

The company will be easier to obtain loan funds when the loan is secured by the assets of the company and the cost of borrowing will be issued less than unsecured loans. This is because unsecured loans are more risky for creditors, especially when the company is liquidated, and when the creditors the company is difficult to repay the loans. In a pledge for a loan, creditor expects that the pledged assets have been recorded in accordance with the current applicable fair value. This is due to the recording of the value of these assets; the creditors can more easily estimate the maximum loan that can be given to companies with assets that are pledged.

Research conducted by Cotter and Zimmer (1995) found that when the assets offered as collateral for the loan, the lender expects the current fair value of the assets offered as collateral for the debt has been recorded in the audited financial statements of the company. So the revaluation of assets can enhance credibility if the assets are included in the published report of the company. If this is the purpose of the revaluation, it is likely that the revaluation was done at an increase level of debt assurance recorded in the audited balance for the current year. This would be an efficient contract solution when the cost of fair valuation of assets as collateral is less than the increase in debt cost that would happen if the debt is obtained without assurance.

H_2: Debt assurance rate has positive effect for the company to revaluate its fixed assets.

Decrease in Cash Flows from Operating Activities

Cash flows from the company operating activities decreased from the previous year will cause great concerns by creditors due to the smaller cash flows from operating activities means the least likely debt given by creditor repaid. To increase the trust of the company's creditors to revalued the assets so that the company assets are expected to increase. With the increase in corporate assets then the creditor trust will increase again due to an increase in corporate assets.

Research conducted by Cotter and Zimmer (1995) that the revaluation of fixed assets would give a higher value on assets that can help the the company guaranteed to assure debtholders about the company's ability to repay debt through the potential of realizing higher corporate assets in accordance market value, so the asset revaluation will restore the lending capacity of the company. Therefore, companies that undergo decrease in cash flows have higher potential to revaluate its assets.
H_3: Decrease in cash flow from operating activities has negative effect on the company to perform revaluation of fixed assets.

Company Size and Fixed Asset Revaluation

Revaluation of fixed assets would increase the value of corporate assets, the higher the value corporate assets, the greater the cost of depreciation, and with greater cost of depreciation would lower company's profits. And also added the cost of implementation to revaluation would further reduce the company profits.

Watts and Zimmerman (1986) in the positive accounting theory states that the size of the company are used as a guide to the political costs and political costs will increase along with the rise of company size and risk. Large companies are politically more sensitive and have a relatively larger transfer of wealth imposed on them rather than smaller companys.

Lin and Peasnell in Seng and Su (2009) states upward revaluation can be an effective way to reduce reported profits through depreciation expense due to an increase in the value of the revalued assets. This is done to reduce the political pressure faced by large companies from the government or the labor unions. Therefore, it is expected that there is a positive relationship between the sizes of the company with the revaluation decision.
H_4: The size of the company has a positive influence on the company to perform revaluation of fixed assets.

Revaluation of Fixed Assets and Income Tax Expense

With the passing of the Minister of Finance Regulation No. 79/PMK.03/2008 concerning the Revaluation of Company's Fixed Assets for the Purpose of Taxation, Directorate General of Taxation issued a regulation Director General of Taxation Number PER-12/PJ/2009 on Procedures for Application Submission and Administration of the Company's Fixed Asset Revaluation for Taxation purpose. Company that revalued fixed assets for taxation purposes must obtain approval from Director General of Taxation by submitting an application to the Head Office of the DJP which oversees the Tax Office where the company is registered.

When viewed from different point of view, by implementing revaluation of fixed assets, the government provides opportunities in the areas of taxation including revaluation resulted in increasing amount of depreciation expense of assets over their useful duration, which in turn will reduce taxable income and payable taxes in subsequent years. Substantial tax savings for the subsequent tax years following the revaluation because of increased depreciation expense which is calculated based on the value of revalued assets which its market price has gone up many-fold.

Through the revaluation of fixed assets, the government provides opportunities in the field of taxation including revaluation resulted in increasing amount of depreciation expense during the useful duration of assets, which in turn will reduce taxable income and payable taxes in subsequent years. The excess of the revaluation is subject to income tax at 10% which is final.

Suandy (2008) stated that the revaluation of fixed assets for a company has functions:
1) Calculation of base cost will generate value approaching a reasonable base cost,
2) Improving equity structure, meaning that the ratio between the loan (debt) and capital / equity or debt-to-equity ratio (debt to equity ratio-DER) to be improved. With the improvement of DER company can withdraw the funds, either through loans from third parties or through the emission of shares.
3) Payment of PPh on the excess over the revaluation of fixed assets at 10% of final whether interesting enough for the company to conduct a revaluation.

Irawadi (2004) stated that the revaluation of the fixed assets of the company will have an impact on the financial statements, such as the balance sheet will show the position of wealth in accordance with the market value or actual value in the income statement will show a more realistic depreciation expense.

Therefore, it is expected that there is a positive relationship between the revaluations of fixed assets with income tax expense.
H5: The size of the company has a positive influence on the company to perform revaluation of fixed assets.

3. RESEARCH METHOD

3.1 Population and Sample

In this research, the researchers took the population for companies that are listed on the Stock Exchange which revaluate in 2010. As for the companies that are not revaluating, the researchers used a technique of sampling which is purposive sampling. According Riduwan (2003), purposive sampling is a sampling technique which researchers use when researchers have certain considerations in sampling for a particular purpose. The selected companies are

companies that have the following criteria
1. Companies listed on the Indonesia Stock Exchange in 2010
2. Companies that are not revalued its fixed assets adjusted for similar sub-sector with companies that revaluating.
3. All the data necessary variables in the study are vailable

3.2 Operational Variables

The independent variable in this study, among other :

a. Leverage level: measured by the ratio of total debt divided by total tangible assets before revaluation adjustments.
b. The level guaranteed debt: using a nominal scale which is a dummy variable, given the value 1 if the company guaranteed debt experienced an increase in revaluation years, and given the number 0 if the company guaranteed debt does not experience increase in revaluation year.
c. Decrease in cash flows from operating activities: measured through changes in cash flow from operating activities for the past two years divided by the number of intangible assets.
d. Company size: measured by LnAset because asset prices are relatively more stable in measuring the company size (Sudarmadji and Sularto, 2007).
e. Income tax expense: calculation of corporate income tax expense before and after revaluation of fixed assets.

In this research, the dependent variable or a bound variable (Y) is a dummy variable. It is coded 1 for companies that revalued its fixed assets and coded 0 for companies that do not perform revaluation of fixed assets.

3.3 Method of Data Analysis

The hypothesis testing in this research using logistic regression techniques to determine the effect of debt contracts negotiation and political cost to the company to conduct revaluation of fixed assets.

Logistic regression model that is used to test the hypothesis is:

$Ln\ \frac{RM}{1-RM}$ = β0 + β1 DTAR + β2 THJ + β3 ΔCFFO + β4 TA + E

$Ln\ \frac{RM}{1-RM}$ = dummy variable for the use of revaluation model
RM = Revaluation Model Probability
DTAR = Rasio total hutang dibagi total aset berwujud
THJ = The ratio of total debt divided by total tangible assets
ΔCFFO = Changes in Cash Flows from Operating Activities
TA = Total Asset
E = residual errors

The second hypothesis testing using simple reression.

4. DATA ANALYSIS AND DISCUSSION

4.1 Descriptive Statistics

Total amount of companies researched 35 companies, 30 companies that are not revalued its fixed assets in 2010, and 5 companies that revaluate in 2010. General description of the sample with variable levels of leverage, the level of changes in cash flow from operating activities, and the size of the company can be seen in the following table of descriptive statistics:

Tabel 1
Descriptive Statistics

	N	*Minimum*	*Maximum*	*Mean*	*Std. Deviation*
DTAR	35	17,682	179,805	65,13914	37,701103
ΔCFFO	35	-24,654	20,140	-,67166	8,376014
TA	35	17,353	25,437	21,02294	1,783737
Valid N (listwise)	35				

Source : processed secondary data

Descriptive statistics table above shows the number of the observation of this research amounted to 35 companies. From 35 corporate data it is obtained that the average level of leverage of the company in question was 65.139. These results indicate that the average proportion of liabilities of the company is larger than the company's capital.

Furthermore, the average value of the company ΔCFFO levels studied were -0.67166. From these results it is indicated that the average change in cash flow from operating activities of companies tends to be slightly decreased from year 2009 to year 2010. Then the average value of total assets (LnSize) of the company in question was 21.02294..

4.2 Hypothesis Testing

Testing hypotheses using logistic regression models to examine the effect of the level of leverage, guaranteed debt level, reduced cash flow from operating activities, and company size.

Tabel 2
Regression Coefficient Test Table

	B	Sig.	Hasil
Step 1 [a] *Leverage*	0,037	0,086	Tidak signifikan
Guarantee Debt Rate	-1,906	0,265	Tidak signifikan
Changes in Cash Flows from Akt. operation	0,353	0,132	Tidak signifikan
Company Size	1,096	0,097	Tidak signifikan
Constant	-28,197	0,71	

Source: processed secondary data

The table shows the results of logistic regression test with 5% significance level. From the logistic regression equation testing then the logistic regression model is obtained as follows:

$$Ln\ \frac{RM}{1-RM} = \mathbf{-28,197 + 0,037DTAR + -1,906THJ + 0,353\Delta CFFO + 1,096TA + E}$$

Hypothesis 1 : Leverage Level

Test results of logistic regression showed that variable levels of companies leverage does not significantly influence the company to conduct revaluation of fixed assets. It can be seen from the testing of hypotheses in which the value of leverage a significance level at 0.086, which means the value is above 0.05 significance but only meet 10% significance level.

These results are consistent with the research conducted by Zimmer (1999), and Missonier-Piera in samples 1994 and 2000 (2007) which only found evidence that the level of leverage to affect the company to revalued its fixed assets at 10% significance level. As well as Seng and Su (2010) that found no evidence that the leverage level to affect the company to revalued its fixed assets. On the other hand, these results do not correspond with the results of research conducted by Missonier-Piera on a sample of 1997 which found evidence that the level of leverage affect the company to revalue its fixed assets.

The results of this study indicate that the ratio of high leverage is not a compelling reason for companies to do revaluation of fixed assets. That is because creditor or lender know about revaluation, this allows them to consider revaluation value in calculating the leverage ratio of companies, even exclude revaluation value in the calculation of the leverage ratio. This is in accordance with the opinion of Lin and Peasnell in Seng and Su (2010) which states that the revaluation is uncertain whether effective in increase the lending capacity, because the power of the lender, they exclude the revaluation from the basis used to calculate the debt ratio.

Hypothesis 2 : Guarantee Debt Rate

Test results of logistic regression showed that variable of guaranteed debt rate of companies has no effect on the company to perform revaluation of fixed assets. It can be seen from the test of the hypothesis in which the value of the significance level of guarantee debt of 0.265, which means the value is above the 0.05 significance. Furthermore correlations obtained were contradictory where the correlation results shown indicate a negative value of -1.906. This research therefore rejects the second hypothesis which states that the level of debt guaranteed affects companies to do revaluation of fixed assets.

These results are consistent with the research conducted by Zimmer (1999) that found no evidence that the level of guaranteed debt affects companies to do revaluation of fixed assets. On the other hand, these results are not in accordance with the research conducted by Cotter and Zimmer (1995) who found evidence that the level of guaranteed debt affects companies to do revaluation of fixed assets. These results indicate that the level of guaranteed debt does not affect the companies to do revaluation of fixed assets. That is because companies can pledge assets other than fixed assets owned by the company to obtain guaranteed debt funds.

Hypothesis 3 : Decrease in Cash Flows from Operating Activities

Test results of logistic regression showed that the decrease in variable cash flows from the company's operating activities does not have a significant effect towards company to revaluate its fixed assets. It can be seen from the hypothesis test where the significant value of changes in cash flow from operating activities amounted to 0.132, which means the value is above the 0.05 significance. Furthermore correlations obtained were contradictory where the correlation results obtained show a positive value of 0.353. This research therefore rejects the third hypothesis which states that the decline in cash flow from operating activities affecting the company to conduct revaluation of fixed assets.

These results are consistent with the research conducted by Cotter and Zimmer (1995), Zimmer (1999), and Seng and Su (2010) who found no evidence that the decrease in cash flows from operating activities affecting the the company to conduct revaluation of fixed assets.

These results suggest that the decrease in cash flows from operating activities does not affect the company to conduct revaluation of fixed assets. Cash flow from operating activities is only part of the company's overall cash flow. The decrease in operating cash flow likely to be offset by the cash flow from other activities. Therefore, the creditors may be looking at the overall cash flow provided by the company rather than focusing on only the operating cash flow (Missonier, 2007). In addition, a decrease in cash flow from operating activities is not a major problem for the creditors when the company still had a low leverage level. That is because if the company is liquidated, then the assets are expected to still be able to repay their debts. It is possible according to the research conducted by Cotter and Zimmer (1995), in which the decrease in cash flow from operating activities has no significant effect on asset revaluation of the total obtained sample, but the decline in cash flow from operating activities have a significant influence on the sample who have high leverage level.

Hypothesis 4 : Company Size

Test results of logistic regression showed that the variables company size has no effect on company to perform revaluation of fixed assets. It can be seen from the hypothesis test in which the significant value of company size amounting 0.097 which means that the value is above the 0.05 significance.

These results are not in accordance with the research conducted by Seng and Su (2010) who found evidence that company size significantly affects the rate of 5% towards the company to conduct revaluation of fixed assets.

Asset Revaluation Effect towards Corporate Income Tax

Table 3
Regression Calculation Result

Model		Unstandardized Coefficients		Standardized Coefficients Beta
		B	Std. Error	
1	(Constant)	4.70	.131	
	Revaluasi Aset	-0.49	.004	.755

a. Dependent Variable: Income Tax Expense

Based on statistical calculations using linear regression analysis derived mathematical equations Y = 4.70 - 0:49 X means that each increment X or any increase in the value of fixed assets due to the implementation of revaluation of fixed assets will reduce Y or will reduce corporate income tax expense. This means that the revaluation the fixed assets have inverse relationship with the income tax expense. While the Pearson correlation analysis obtained by the correlation coefficient is - 0.8045, it means that the relationship between these two variables is very strong and inversely proportional. Furthermore from the results of determination analysis showed that the effect of revaluation of fixed assets acquired 64.72% results towards income tax expense using the formula determination coefficient. While the remaining 35.28% indicate other influences that can affect income tax expense.

5. CONCLUSIONS AND SUGGESTIONS

5.1 Conclusions

Based on logistic regression testing performed, it can be deduced as follows: :

1. *Leverage Level*
   Leverage level of company does not affect the company to conduct revaluation of fixed assets. The results only showed that the level of leverage affects only revaluation of fixed assets at 10% significance level. Thus it can be said that high leverage level is not a good reason for companies to do revaluation of fixed assets.
2. Guarantee Debt Rate
   Guarantee Debt Rate does not affect the company to conduct revaluation of fixed assets. Revaluation of fixed assets is not dependent on the increase or decrease in company guarantee debt. It is suspected that the company may pledge assets other than fixed assets owned by the company to obtain guarantee debt funds. This is because creditors are more interested with the guaranteed assets that are more liquid than the guarantee in the form of fixed assets. creditors tend to loan to companies which reported value of their assets at fair value as disclosed by the Missonier Nichols and Buerger (2007), but researchers suspect that the revaluation of fixed assets has no significant effect for the creditors to make loans because there are a number of other criteria that may be of higher priority by creditors such as the continuity of the business, company leverage level, total bank debt / net worth (gearing), and so on.
3. Decrease in Cash Flows from Operating Activities
   Decrease in cash flow from operating activities does not affect the company to conduct revaluation of fixed assets. That is because creditors tend to see overall cash flow provided by the company rather than just focusing on operating cash flow alone.
4. Company Size
   Company size does not affect the company to conduct revaluation of fixed assets. The results only show that company size affects only revaluation of fixed assets at 10% significance level. From these results the researchers suspect the difference in significance levels obtained by the researchers with other research is because in Indonesia, companies that revaluate were subject to revaluation tax rate of 10%. This may result in companies that revalued its fixed assets which was originally performed in order to reduce the political costs now, but it will eventually lead to revaluation tax which must be borne by the company.

4 Revaluation of fixed assets resulted in the increase in the value of fixed assets of the company. With the increase in value of fixed assets from the book value which are valued at market value or is also referred as increment revaluation of fixed assets causes increased depreciation in accordance with the increase in the value of each type of fixed assets divided by the useful or economic duration of each type of fixed assets. The increase in depreciation expense will reduce company profits so that the burden of taxes paid will also be reduced or also known as tax savings.

5.2 Limitations

The limitation of this research is :

1. The independent variable in this study is using only one proxy in performing test towards the company to conduct revaluation of fixed assets.
2. Only the debt contracts negotiation and political cost that is being tested on the company to perform revaluation of fixed assets.
3. Researchers only get 5 companies that revalued its fixed assets in Indonesia Stock Exchange in 2010.
4. Samples for companies that are not revaluate its fixed assets (non-revaluers), is only taken by subsector similar with the companies that revalued its fixed assets in Indonesia Stock Exchange in 2010.
5. Research carried out only in 2010.

5.3 Suggestions

For academics

1. Proxy used for the independent variable is not only one proxy for obtaining better results.
2. Can use other independent variables that may affect company to conduct revaluation of fixed assets.
3. Samples taken can be more extensive.
4. Research carried out is not just one year long.

For companies

Revaluation should be done by the company to increase the relevance of the company's financial statements that are presented as a basis for decision-making of the stakeholders. Companies that revaluate its fixed assets with the intent to improve the trust of creditors and increase lending capacity should be reconsidered because most creditors assess changes in the value and presentation of financial statements due to revaluation so that the creditors notice revaluation value in making decisions. Revaluation meant to reduce the political costs would lead to tax increases due to revaluation to be borne by the company. Therefore, the revaluation should not be done for the purpose of cost reduction policy.

For Investor

Companies that revaluate its fixed assets have a higher relevance value as it is measured at fair value, and therefore investors should also pay attention to revaluation of fixed assets in assessing company. Fixed assets are assets of great value for most companies, the difference in the application of accounting policy on fixed assets will have a significant effect on the financial statements. Therefore, companies that revaluate its fixed assets can not be compared to companies that do not conduct revaluation of fixed assets if the recorded revaluation value does not take into account. Investors also need to consider whether there is a specific purpose for a company that revaluate its fixed assets and how the result of the recording of the revaluation of the fixed assets towards decision-making.

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