

Fair Value and Historical Cost Dilemma: Modern Accounting Dynamics in Financial Statement Quality

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ABSTRACT

The use of fair value and historical cost is still debated in modern accounting regarding its application and effect on the quality of financial statements. Moreover, there is a conflict of interest between managers and stakeholders related to the need for asset valuation based on these methods. Therefore, a solution is needed to balance between relevance and reliability to meet the needs. This study aims to determine the effect of applying fair value and historical cost on financial statement information during economic volatility. The sample used is representative of companies in the financial, property, and energy sectors that were affected by the application of valuation methods during the financial crisis in 2008 and the COVID-19 pandemic in 2020. The research was conducted using the content analysis method and literature review to find out more about the financial statements. The results show that fair value exacerbates the company's financial decline during the volatility of the financial crisis, but describes the current condition of the company so which is relevant, but not reliable due to the subjectivity of valuation. Whereas historical cost does not result in changes so it is not relevant, but more reliable due to objectivity and verifiability. With this, the research contributes to provide input in the application of both methods with a hybrid approach in financial statements.

Keywords: COVID-19 Pandemic; Economic Volatility; Fair Value; Financial Crisis; Historical Cost

ABSTRAK

Penggunaan nilai wajar dan biaya historis masih diperdebatkan dalam akuntansi modern mengenai penerapan dan pengaruhnya terhadap kualitas laporan keuangan. Selain itu, ada konflik kepentingan antara manajer dan pemangku kepentingan terkait dengan kebutuhan penilaian aset berdasarkan metode tersebut. Oleh karena itu, diperlukan solusi untuk menyeimbangkan antara relevansi dan keandalan untuk memenuhi kebutuhan. Penelitian ini bertujuan untuk mengetahui pengaruh penerapan nilai wajar dan biaya historis terhadap informasi laporan keuangan selama volatilitas ekonomi. Sampel yang digunakan mewakili perusahaan di sektor keuangan, properti, dan energi yang terdampak penerapan metode penilaian selama krisis keuangan tahun 2008 dan pandemi COVID-19 pada tahun 2020. Penelitian dilakukan dengan menggunakan metode analisis konten dan tinjauan literatur untuk mengetahui lebih lanjut tentang laporan keuangan. Hasil penelitian menunjukkan bahwa nilai wajar memperburuk penurunan keuangan perusahaan selama volatilitas krisis keuangan, tetapi menggambarkan kondisi perusahaan saat ini sehingga relevan, tetapi tidak dapat diandalkan karena subjektivitas penilaian. Sedangkan biaya historis tidak menghasilkan perubahan sehingga tidak relevan, tetapi lebih dapat diandalkan

karena objektivitas dan verifikasi. Dengan ini, penelitian berkontribusi untuk memberikan masukan dalam penerapan kedua metode dengan pendekatan *hybrid* dalam laporan keuangan.

Kata kunci: Pandemi COVID-19; Volatilitas Ekonomi; Nilai Wajar; Krisis Finansial; Biaya Historis

INTRODUCTION

Asset valuation is essential for reliable financial statements and informed decision-making. Challenges arise due to globalization, financial innovation, and digitalization, leading to new asset types like derivatives, digital assets, and intangibles. The existence of inactive markets for these assets further complicates the valuation process, demanding a more rigorous approach and more adaptive methodologies (Gad, 2024). Normative Accounting Theory (NAT) includes two main valuation methods, namely fair value and historical cost (Patty et al., 2021). Fair value reflects the market price of the asset, allowing for dynamic adjustments to match current economic conditions (Black et al., 2022; Nordlund et al., 2022; Sampaio et al., 2022). In contrast, historical cost records assets at cost, providing stability but not reflecting changes in market value as they occur (Liao et al., 2021; Simanjuntak et al., 2023).

Modern accounting's dynamic development and volatile external conditions create dilemmas in valuation, where reliance on fair value and historical cost methods can lead to errors and misleading presentations (Tkachuk, 2019), as happened in the Enron case, where mark-to-market accounting on a fair value basis was used to overstate asset values and create the illusion of profitability (Dichev, 2008; Gwilliam & Jackson, 2008). This case relates to agency theory, where conflicts of interest and information asymmetry result in agents abusing their authority, harming principals. The fair value and historical cost methods in accounting remain debated regarding the financial information that stakeholders require. The 2008 financial crisis and the 2020 COVID-19 pandemic highlighted valuation issues in entities, revealing the strengths and weaknesses of various methods during economic instability. In 2008 during the financial crisis, the drastic drop in market prices caused fair value to reflect large losses in the income statement (Liao et al., 2021; Sampaio et al., 2022; Tkachuk, 2019), many financial entities are experiencing liquidity pressures due having to record losses based on falling market values (Dontoh et al., 2021). With this, fair value is blamed for market instability. Meanwhile, during the COVID-19 pandemic in 2020, the value of assets was difficult to measure because the market was not active (Prastyawan et al., 2022). Entities with fair value-based assets may experience large fluctuations in profit or loss. Even when market conditions are volatile, recording assets at historical cost does not change, but it does not reflect real losses either. It is more stable because asset values remain unadjusted, but less relevant in reflecting fluctuating economic conditions.

It can be concluded that historical cost is considered more reliable because it is based on real transactions, but it is less relevant in reflecting current economic value. Conversely, fair value is more relevant because it reflects current market conditions, but can be less reliable if market data is unavailable or too volatile. For a long time, valuation has played an important role in supporting stakeholders, such as investors and creditors, in decision-making. Investors and creditors want reliable and relevant financial statements (Li et al., 2020; Saputro & Indraswono, 2022). Entities must demonstrate high profitability, adequate liquidity, and solvency to minimize risk, promising growth prospects, and transparent and quality governance (Bhatia, 2023; Nguyen & Kimura, 2023; Saputro & Indraswono, 2022). However, to improve the performance of the entity, managers also have the flexibility to choose a valuation method that is favorable to them (Simanjuntak et al., 2023). In line with the concept of agency theory, there is potential for earnings management and reduced transparency. If valuations do not reflect true economic conditions, it can exacerbate information asymmetry and increase the risk of wrong decision-making for stakeholders. Recent market volatility has exposed the limitations of traditional valuation methods, as they sometimes fail to capture the risk when asset prices deviate from their intrinsic value (Gad, 2024). With that, valuation has the potential to affect the quality of information in financial statements received by investors and creditors, even if it is unintentional (Dong et al., 2022). It is essential to ensure that financial statements are both relevant and reliable.

This study examines the impact of fair value versus historical cost on the relevance of financial statements during economic volatility, focusing on the manager's method and its effects on investors and creditors. This research examines the latest challenges in asset valuation by examining the theoretical underpinnings and accounting standards, practical constraints, and policy impacts of the valuation methods used. The research implications in practice, enable entities to select valuation methods wisely, enhancing information quality for investors and creditors, and evaluating accounting policies. It also enriches accounting literature on asset valuation, linking theory to practice, and lays the groundwork for future policy research.

LITERATURE REVIEW

Agency Theory

Jensen and Meckling (1976) found agency theory that explores the dynamics between principals (such as stakeholders) and agents (such as managers), with a focus on the conflicts of interest. This theory addresses the problem of information asymmetry and mechanisms to align the interests of both parties. There are three main concepts in agency theory, first, the relationship between principals and agents is very complex in business, highlighting the challenges when their objectives conflict and the difficulty for principals to verify agents' actions (Peltokorpi, 2024). Second, information asymmetry, agency theory deals with information asymmetry *ex ante*

(hidden characteristics) and ex post (hidden actions), which can lead to welfare loss if not managed properly (Lesmono & Siregar, 2021; Riyono, 2024). Third, the existence of incentives and monitoring, this theory suggests the use of incentive instruments and monitoring arrangements to minimize conflicts and align the interests of principals and agents (Hendrastuti & Harahap, 2023).

Agency theory is closely related to this research, as there is a conflict of interest between principals, which in this study are investors and creditors, and agents, which are managers. This theory is crucial in understanding how different valuation methods, such as fair value and historical cost, impact this relationship. Agency costs arise when there is a misalignment of interests, leading to inefficiencies and potential losses for principals. While fair value provides more up-to-date information, it can increase volatility and agency conflicts. Historical cost provides stability but can lead to inefficiency due to less updated information. Balancing these factors is essential to minimize agency costs and align the interests of managers with those of investors and creditors. Therefore, agency theory is most suitable for use in this study.

Fair Value Importance

The fair value method evaluates assets based on current market conditions (Gad, 2024; Jaijairam, 2012), which reflects prices that could be exchanged in an orderly transaction between market participants on the measurement date. This method provides real-time valuation, thus providing more current and relevant financial information (Beigman et al., 2023; Black et al., 2022; Nordlund et al., 2022). Fair value can also increase transparency and assist in decision-making by reflecting the current market situation (Liao et al., 2021). Therefore, fair value is more relevant for valuing assets that are active in the market. However, it has the potential to cause volatility and systemic risk (Aremu & Owolabi, 2023; Chang et al., 2021), especially during an economic crisis such as in the case of 2008, as market-driven valuations amplify the decline in asset values during periods of distress (Liao et al., 2013; Riyono, 2025; Sampaio et al., 2022). Valuations can be subjective and less reliable when market prices are not available (Aremu & Owolabi, 2023; Gad, 2024), as in the case of the Enron scandal shows the potential for manipulation and earnings management related to fair value (Gwilliam & Jackson, 2008). Gad (2024) argues that the integration of unrealized gains and losses at fair value can cause distortions in the entity's true performance due to the illusion of profitability when the market is weak. This can lead investors and creditors astray as to the long-term sustainability of the entity.

Historical Cost Importance

Measurement using the historical cost method values assets at their historical cost (Jaijairam, 2012; Simanjuntak et al., 2023). This method provides stability and reliability by using verifiable and objective data (Ayu, 2023; Maroun & van Zijl, 2022). Since it is recorded at historical cost, it avoids the volatility associated with market fluctuations (Biondi & Oulasvirta, 2023; Grecco et al., 2023; Jadi et al., 2022),

providing a consistent basis for financial reporting. However, it does not reflect current market conditions, potentially resulting in outdated and irrelevant financial information (Barradale et al., 2022). Therefore, historical cost is more informative for less liquid assets. According to Gad (2024), by avoiding unrealized gains and losses, historical cost provides a clearer and more conservative picture of the entity's financial position, especially during periods of economic stress. However, because historical cost is unable to adjust its value to market changes over time, when economic conditions change, the value of the asset can deviate significantly from its historical cost (Barradale et al., 2022; Biondi & Oulasvirta, 2023). Therefore, the financial statements do not provide accurate information about the entity's assets, especially when the market is volatile, where the value of assets can rise or fall quickly, which is not reflected in the historical cost (Grecco et al., 2023). All of this could potentially also mislead investors and creditors as to the true value of the entity's assets.

METHODS

This research is conducted with a qualitative approach with case study analysis in the entity to determine the difference in the impact of fair value and historical cost implementation on the relevance of information in financial statements. After that, it will be linked to the perspective of investors and creditors, whether they will be affected or not. The population taken is the financial, property, and energy sectors in 2008 and 2020. Sampling is done by purposive sampling method with criteria: a) have financial statements for 2008 and 2020, b) have assets measured at fair value, and c) income statement impacted by the 2008 financial crisis and the COVID-19 pandemic. With this, the entities in each of the selected sectors are: a) financial sector: PT Bank Mandiri (Persero) Tbk. and PT Bank Maybank Indonesia Tbk, b) property sector: PT Lippo Karawaci Tbk, and c) energy sector: PT Perusahaan Gas Negara Tbk. and PT Medco Energi International. Entities within a sector play an important representative role, advocating for collective interests and demonstrating sector-specific challenges (Prewysz-Kwinto, 2019). All entities use the same accounting standards to recognize, measure, and present financial statements. This includes consistent formats of the statement of comprehensive income and statement of financial position within a sector, so that representative entities adequately represent themselves financially within sectoral norms and practices (Prewysz-Kwinto, 2019). Research sources were obtained from the 2008 and 2020 financial statements of the selected entities as samples. The analysis method is carried out by content analysis and literature review based on theory and previous research.

In 2008, there was a global economic crisis caused by the subprime mortgage crisis in the United States (Sampaio et al., 2022). This event impacted all countries, including Indonesia, resulting in a very significant market decline (Sampaio et al., 2022). As well as the COVID-19 pandemic in 2020, the market became inactive due to the lockdown (Prastyawan et al., 2022), resulting in less reliable market information

and subjective measurements. Both events make market conditions volatile and inactive, which will affect the fair value measurement process (Dichev, 2008; Gwilliam & Jackson, 2008; Prastyawan et al., 2022; Sampaio et al., 2022). So this provides a difference between the implementation of fair value and historical cost on financial statements, especially on the income statement, with a declining economic event.

The sector most affected by the fluctuating economic and market conditions in 2008 and 2020 was the financial sector (Altawalbeh, 2020), property (Ghosh et al., 2020), and energy (Fallery & Tjendrasa, 2022). Because there are assets that have a large value and are recorded using the fair value method. As in the financial sector, entities such as PT. Bank Mandiri (Persero) Tbk. and PT. Bank Maybank Indonesia Tbk. record its bonds, notes and marketable securities financial assets at fair value. During the global crisis years of 2008 and 2020, fair value may have experienced volatility in the financial statements, potentially exacerbating financial instability by increasing the cost of fair value losses (Maroun & van Zijl, 2022). In the property sector, entities like PT. Lippo Karawaci Tbk. also experienced very significant losses on real estate investment trusts (REITs) assets carried at fair value in 2008 and 2020. This unique structure of the property sector makes it particularly sensitive to fair value, which can lead to significant fluctuations in the reported value of such assets during economic downturns (Ghosh et al., 2020). In the energy sector, energy entities such as PT Perusahaan Gas Negara Tbk. and PT Medco Energi International measure oil and gas reserves using fair value. During 2008 and 2020, there was a significant decline in global oil prices (Prastio & Muhani, 2022), resulting in the entity recognizing a loss on the fair value of its oil. Meanwhile, other sectors such as the manufacturing, telecommunications, health, and consumer goods sectors are more resistant to economic crises because most of the large-value assets are measured at historical cost, such as fixed assets and inventories, so they are not affected by fluctuating market values. Therefore, the financial, property, and energy sectors, represented by each selected entity in the sector, can be an example in a case study to determine the effect of using fair value during an economic crisis on the relevance of financial statement quality and the difference with historical cost.

RESULTS AND DISCUSSION

Entity Case Study Results Within the Financial Sector

As disclosed in CALK 2g and 2h, PT Bank Mandiri (Persero) Tbk. (BMRI) has securities held for trading in the money market and bonds, which are estimated based on their fair value. If the marketable securities increase or decrease in fair value, BMRI records it in the consolidated statement of income for the year as unrealized gain or loss. The difference between the sales price and the fair value recorded at the end of the year is recognized as realized gain or loss on sale. As indicated in BMRI's profit and loss and CALK no. 38 and 39, in 2008, during the financial crisis, BMRI recorded a total gain from the increase in value of securities and bonds of Rp. 1,486,000,000.

Meanwhile, BMRI obtained a total loss from the sale of securities and bonds of Rp. 54,061,000,000. Available-for-sale securities and bonds are also presented at fair value, but unrealized gains or losses from increases or decreases in fair value are not recognized in profit or loss, but in the statement of financial position in equity. Such gains or losses are recognized in profit or loss upon realization. As in the equity section of the statement of financial position, BMRI recorded a net unrealized loss on available-for-sale securities and bonds of Rp. 170,310,000,000. Meanwhile, in 2020 during the COVID-19 pandemic, BMRI recorded an unrealized gain from the increase in fair value of marketable securities of Rp. 483,464,000,000 in CALK 7a.

PT Bank Maybank Indonesia Tbk. (BNII) has reported a decrease in the fair value of trading securities and government recapitalization bonds by Rp 882,486,000,000, reflecting market conditions that can affect asset valuations. This fluctuation impacts the reliability of financial conditions, as it may lead to recognized paper gains or losses. During the 2008 financial crisis, BNII recorded a loss of Rp 128,615,000,000 from the sale of securities and bonds. Conversely, in 2020, despite negative economic sentiment, BNII experienced a rise in equity from unrealized gains of Rp 422,847,000,000 and gains from sales amounting to Rp 234,914,000,000. However, an impairment of Rp 5,136,000,000 for trading securities was noted due to the pandemic's declining market conditions. Through this, it was found that the use of fair value could potentially result in a loss due to the rise and fall of the value of the assets held as a result of market fluctuations. However, it also does not always result in losses because the whole is also influenced by many other internal factors, such as corporate governance and management, so that under certain conditions it can still make a profit, as in BMRI and BNII during COVID-19 in 2020. But this measurement shows the company's actual state in accordance with its current condition. Thus, providing relevant financial statement information for stakeholders who use it.

Entity Case Study Results Within the Property Sector

Similar to the banking sector, the property sector recognizes fair value in its reporting. PT Lippo Karawaci Tbk (LPKR) measures its investment assets at fair value, reporting unrealized losses of Rp. 19,105,477,190 due to market volatility. This is also reflected in its investment in REITs, which faced losses of Rp. 147,328,541,721, impacted by the financial crisis and international market conditions, particularly on the Singapore stock exchange. In 2020, LPKR reported a fair value loss of IDR 61,475,000,000, likely linked to the COVID-19 pandemic, along with a significant loss of Rp. 1,282,971,000,000 as detailed in its financial statements. Similarly, PT Ciputra Development Tbk (CTRA) reported a loss of Rp. 10,746,575,041 from investment sales. These losses negatively affect overall company performance and profit potential until the market stabilizes. The interpretation obtained for the property sector in the form of the nature of the use of fair value disclosures will cause volatility, thus creating a tendency to incur expenses or losses when there is negative sentiment. Of course, with the characteristics of the property sector, the impact of fair value disclosure cannot be generalized to other sectors. However, it cannot be denied that

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the use of fair value will often be used because the majority will hold land and building assets which usually require the condition of their current market prices to create relevant reporting for creditors and investors. On the other hand, due to the presentation of relevant values, there is recognition of "paper" losses or impairments that do not represent real cash conditions. Therefore, fair value has the advantage of reflecting current conditions and presenting relevant information, but it creates risks to the reliability of the presentation because it does not capture long-term prospects and real conditions.

Entity Case Study Results Within the Energy Sector

PT Perusahaan Gas Negara Tbk (PGAS), a key player in the energy sector, has experienced significant fluctuations in fair value disclosures in its profit and loss segments. Fair value losses on derivatives rose dramatically from Rp. 452.7 billion in 2007 to Rp. 2.5 trillion in 2008, largely due to the financial crisis and market sentiment. Additionally, the COVID-19 pandemic in 2020 severely impacted oil prices, causing a decrease in PGAS's oil and gas property values by \$75.7 million. The pandemic also affected PGAS's investments, resulting in losses of \$296,666 as reported in PGAS CALK 4. PT Medco Energi Internasional Tbk (MEDC) also reported significant financial impacts in its income statement, highlighting losses of \$39,208,020 in asset values, \$33,859,109 in short-term investments, and \$10,041,234 from derivative transactions, linked to the 2008 financial crisis. The unrealized gains/losses from short-term investments reflect market price changes, while losses from derivatives stem from failing to meet hedging criteria. MEDC also disclosed asset impairment due to indications that carrying values were not recoverable. In 2020, the company adjusted the fair value of cash flow hedges, resulting in an equity impact of \$13,125,193 due to the COVID-19 pandemic. Despite some losses, MEDC recorded a gain of \$31,144,000 on fair value adjustments of financial assets and a loss of \$19,010,762 from dilution of long-term investments, along with a significant asset impairment loss of \$65,071,523.

From the perspective of the energy sector, the use of fair value is highly utilized to reflect the current market price of the oil being traded. This makes the energy sector vulnerable to price changes due to the use of fair value disclosures. For example, the pandemic phenomenon in 2020 dropped oil prices and resulted in significant losses for companies in the energy sector. However, the use of fair value is inevitable as energy sector companies have to measure their assets to determine the difference from the traded assets and integrate it into the operational aspects of the company. Furthermore, this can also create a cycle that triggers a decrease in financial ratios or profitability due to a decrease in asset value, which indirectly leads to a decrease in investor or creditor interest in the company's valuation. Furthermore, the company is less likely to get funding from investors and loans from creditors, which can then be the beginning of another cycle of crisis, and vice versa if there is an increase in asset value. Thus, the use of the fair value method has a two-way effect on the company's financial statements that can potentially lead to losses or gains as well as increases or decreases in asset values that can have an impact on the company's evaluation.

The Effect of Fair Value and Historical Cost on the Relevance and Reliability of Financial Statements

The opportunity for agents or managers to benefit themselves is very large with the asymmetric information in the financial statements as in agency theory. So it allows managers to take advantage of the selection of these two methods to improve information on their financial performance. Based on the results of case studies in all

sectors, both in the financial, property, and energy sectors, both fair value and historical cost methods have their advantages and disadvantages, as shown in Table 1, which affect how financial information is perceived and used by stakeholders. Fair value is relatively more relevant than historical cost because it can reflect current market conditions with the recognition of losses or gains from decreases or increases in the market value of assets, as is the case for all companies in the case studies, especially the energy sector. Therefore, fair value can provide up-to-date asset information, which can be crucial for decision-making (Fukui & Saito, 2022; Petrović et al., 2023). This relevance is especially apparent in the valuation of actively traded securities (Gad, 2024), as fair value provides a more accurate reflection of market dynamics, such as during the 2008 financial crisis and the 2020 COVID-19 pandemic. However, its relevance can be limited by market volatility and the subjectivity involved in valuing less liquid assets. In contrast, historical cost is often seen as more reliable as it is based on actual transaction prices, which is verifiable and less subjective than fair value estimates. It can also be very informative for assets that are not actively traded. The reliability of fair value can be compromised by the subjectivity involved in estimating value for assets that are not actively traded, with the potential for inconsistency and manipulation, as in the Enron case.

Studies also show that fair value can improve the quality of financial reporting by offering more transparency and relevance (Altawalbeh, 2020; Barradale et al., 2022; Ghosh et al., 2020). This method can provide transparency by aligning the value of assets with current market conditions, such as what happened in the energy sector, to adjust the value of its oil assets along with the REIT's declining properties, thus improving investor confidence and decision-making. However, it can also result in volatility in the income statement and financial position during economic downturns, such as the 2008 financial crisis in the energy sector, which resulted in companies recognizing huge losses. The reliance of fair value on market conditions can also lead to systemic risk and challenges in valuing illiquid assets (Gad, 2024). On the other hand, historical cost can provide stability and consistency in valuing assets at historical cost, in the case study, all assets measured at historical cost were not impaired, and therefore no impairment loss was recognized. Historical cost provides a more stable result that can be favorable during economic downturns. However, it may not accurately reflect current economic realities, potentially leading to less up-to-date financial information.

Table 1. Fair Value and Historical Cost Comparison

Indicator	Fair Value	Historical Cost
Volatility	High, in line with changing market conditions	Low, more stable at cost
Transparency	Provides up-to-date information on conditions	Asset value may deviate from market value

Usefulness During Economic Crisis	May exacerbate the decline through revaluation	More stable, but not reflective of the actual condition
Application	Better for easily liquid assets	More common for fixed assets and illiquid assets
Application During Economic Crisis	May increase the loss burden due to changes in fair value	Can avoid fair value losses
Fraud Risk	High, potentially subjective if the asset is not active in the market	Low can be verified with historical cost
Benefit	More favorable for external stakeholders such as owners, investors, and creditors	Can be used to evaluate internal management
Long-term Asset Suitability	Not suitable, as market fluctuations may occur	Very suitable to show the investment that is held

The Effect of Fair Value and Historical Cost on Entity Performance

In accordance with agency theory, between agents and principals, there is often a conflict of interest, managers as agents prefer to carry out activities that benefit them by improving entity performance to obtain incentives. So that agents can take advantage of information asymmetry to improve entity performance with valuation, as is the case with the Enron case, with the mark-to-market accounting method on a fair value basis used to overstate asset values and create the illusion of profitability. So that potentially the use of valuation methods is potentially misused by entities to make financial statements that look good. Meanwhile, stakeholders or principals want a transparent and reliable entity performance. In the case studies across all sectors, due to the market downturn in 2008, all selected entities recognized a loss on the decline in the fair value of their assets, this loss is presented in the income statement, thus impacting the entity's earnings before tax and interest (EBIT). However, according to Sackey (2023), the fair value method has a positive influence on return on assets than historical cost. This suggests that fair value may better reflect the economic reality of the entity's operations, leading to improved earnings performance. Meanwhile, Amaefule et al. (2018) found that the use of fair value does not affect entity performance as measured by earnings per share and return on equity. There are also significant differences in financial ratios when using fair value compared to historical cost, although these differences are not always nominally significant (Anojan & Nimalathan, 2018). In this case study, it was also found that the entity's EBIT in 2008 and 2007 did not differ much despite the recognition of losses on the decline in fair value of assets because it was not material, the main driver of the decline in EBIT was due to a decrease in the company's sales so that this recognition was not a major issue for the company, but it could still present more relevant asset information. This shows that although fair value can change the presentation of financial statements with additional losses or gains from an increase

or decrease in fair value, fair value does not always have an impact on the financial health of the entity.

As explained earlier, the choice between fair value and historical cost does not have much impact on the performance of the entity. Therefore, the use of this method cannot necessarily be used to improve financial conditions. Even in the context of agency theory, the use of fair value generally benefits entities more than historical cost by increasing transparency and reducing agency costs (Edholm, 2022; Tkachuk, 2019). Due to the use of fair value, entities can provide a more accurate reflection of financial statements, thereby increasing transparency and stewardship. This transparency helps to align the actions of managers with the interests of stakeholders, thereby reducing agency costs. By providing full disclosure and focusing on the current value of assets, fair value can also reduce information asymmetry, as it requires managers to be more accountable for their valuations. However, it is still entirely influenced by the entity's corporate governance, if it is weak, it will increase the possibility of fraud. Even if there are agency conflicts, fair value is also proven to minimize them, so cases like Enron are more influenced by the aggressiveness of entity managers to improve entity performance.

The Effect of Fair Value and Historical Cost on Investors and Creditors

The effect of applying fair value and historical cost on investors and creditors can also be seen with agency theory, where there is also a conflict of interest between principals, namely investors and creditors, and agents or managers. The choice between fair value and historical cost affects how information in financial statements is presented and also decision making by investors and creditors (Angelo & Nuryani, 2021). Based on the previous explanation, fair value is said to be more transparent and relevant because it reflects real-time market conditions, thus increasing investor confidence and providing more relevant information. With this, the condition of financial health becomes clearer, thereby reducing agency costs and stewardship for investors because the behavior of agents is in line with the wishes of principals (Khelil & Khelif, 2024). However, in times of market fluctuations, fair value leads to high volatility that can reduce investor confidence, as in the case study due to the recognition of losses on the decline in fair value. Also, if the asset is not active in the market and difficult to measure, managers will also use subjective estimates, resulting in opportunistic behavior and potential earnings management.

Whereas historical cost provides stability in the value of assets at cost, it provides objective and verifiable financial data, reducing managerial discretion over reported values. As in the case study, financial instruments measured at historical cost have not decreased, so they still provide consistent asset values. Therefore, historical cost is favorable for creditors to predict the entity's future financial condition (Edholm, 2022). This measure has proven to be more effective in predicting credit losses, which is crucial for creditors to assess credit risk. However, historical does not reflect current market conditions, potentially leading to information asymmetry and higher agency costs.

Both fair value and historical cost methods affect information asymmetry. Fair value can reduce asymmetry by providing current market information, while historical cost can increase it due to outdated valuations. There are also considerations of agency problems in moral hazard, with fair value accounting, managers can potentially manipulate asset valuations to achieve their targets, while with historical cost, managers can also record asset valuations above the actual value to create ex ante and ex post information. If managers choose historical cost, they can hide impairment, which leads to mispricing of risk (Amaefule et al., 2018). It is also in line with Positive Accounting Theory (PAT) by Watts and Zimmerman (1990) that the use between the two accounting valuation policies is driven by the Bonus Plan Hypothesis that managers choose the most profitable way to increase the entity's profits to increase the manager's bonus. Meanwhile, investors and creditors rely heavily on financial statements to assess risk. Creditors prefer historical cost because it provides a predictable and stable financial metric for debt. However, investors trust fair value more to obtain real-time risk, especially during unstable economies and markets. So, there is also a conflict in method preference between stakeholders.

The Need for a Hybrid Approach

Based on all this, it is known that the problem of using the fair value and historical cost methods is also strongly correlated with agency theory, especially for investors and creditors. First, fair value and historical cost both have the risk of being inaccurate in financial statements under certain conditions. Second, the opportunistic behavior of managers to commit fraud in both fair value and historical cost by taking advantage of asymmetric information. Third, assets that are difficult to value or illiquid assets require managers to use subjectivity in valuing assets. Fourth, a conflict of interest between managers and stakeholders to improve entity performance. Fifth, there is the difference in valuation method preferences between creditors and investors, where creditors prefer valuation at historical cost while investors prefer fair value. But from this, both methods also have their advantages and disadvantages. Where fair value is more relevant and transparent to financial statements because it reflects current conditions, but not as reliable as historical cost which is more objective and verifiable. To balance relevance and reliability in the financial statements and also find the middle point of the conflict of interest, a hybrid approach is needed that combines elements of both methods. The goal is to align asset values with economic reality while mitigating excessive volatility. Integrating the two methods obtains a framework that is also transparent by avoiding market distortions, while also guarding against the risk of overvaluation and undervaluation. So that the quality of information in the financial statements can be maintained and can also be trusted and used by all stakeholders and reduce the risk of fraud due to asymmetric information between agents and principals.

The Statement of Financial Accounting Standards (PSAK) is the main guideline for all accounting in preparing financial statements. With this, all entities are required to follow PSAK to recognize, measure, and present all financial information. PSAK has

now adopted both fair value and historical cost methods for the valuation of an entity's assets. As in PSAK 68, which requires disclosure of instruments or items measured at fair value in the financial statements to provide transparency to stakeholders, followed by PSAK 71, which regulates assets and liabilities that must be measured at fair value, such as investments in stock securities, accounts receivable, deposits, and derivative instruments. As for debt such as bonds payable, accounts payable, and derivative liabilities. Financial instruments measured at amortized cost are loans to third parties, trade receivables that are not traded in an active market, and long-term debt measured at amortized cost. As well as financial instruments classified as fair value through other comprehensive income (FVOCI) such as investments in bonds with strategic or long-term objectives and in shares not held for trading purposes. Meanwhile, financial instruments classified as fair value through profit or loss are derivative instruments held for trading purposes and investments in securities held for trading purposes. Historical cost is also regulated in PSAK 14 regarding inventories and PSAK 16 regarding fixed assets, which both must be measured at historical cost. Therefore, PSAK has accommodated entities to reduce conflicts of interest and adjust to the information needs of stakeholders. Through the integration of these two methods, it also reduces the risk of deviation of asset value from economic reality with fair value and can also mitigate excessive volatility with historical cost. So, entities need to establish both methods to maintain financial performance during a crisis and provide reliable and relevant information for users of financial statements.

Agency Theory Verification

The results of this study verify the agency theory that there is a conflict of interest and information asymmetry between agents and principals. Where in this study managers experience a dilemma to choose between the use of fair value and historical cost which can be used under certain conditions to create ex ante and ex post information to maintain the entity, especially when there is a fluctuating market. Meanwhile, investors and creditors need relevant and reliable information related to financial statements, with this agency cost increasing due to the opportunistic behavior of managers to commit fraud. The use of fair value and historical cost itself also both have advantages and disadvantages, so that it cannot be balanced between the relevance and reliability of financial statements. As well as investors prefer to use fair value, while creditors prefer historical cost, it also creates agency costs between agents. Therefore, to balance between relevance and reliability, a hybrid approach is needed to combine both elements in one financial statement.

CONCLUSION AND SUGGESTION

The main methods of asset valuation, fair value and historical cost, both have advantages and disadvantages. While fair value can be more relevant and transparent as it reflects current conditions in the financial statements with market value calculations, it is not as reliable as historical cost, which is more objective and

verifiable. The weakness of fair value is very visible during the financial crisis such as in 2008, where this method worsens the entity's financial condition due to the burden of unrealized losses on the decline in fair value, while historical cost does not cause such negative effects but the value of the asset is at risk of deviating from the actual value in the market. Fair value measurements can also be subjective and even unreliable when valuing assets with inactive or illiquid markets, whereas historical cost is based on acquisition costs, making the valuation more verifiable. Due to the subjectivity of market value, managers also have opportunistic behavior to improve the entity's finances with valuation, as in the case of Enron, resulting in fraud in the financial statements. However, fair value also needs to be used despite these risks and weaknesses to provide the current condition of the entity by also considering the risk of volatility in financials due to a decrease in market value. The main decision-making basis for investors and creditors is the same financial statements, thus requiring relevant and reliable information for both parties. Investors prefer fair value valuation to get up-to-date information to determine the entity's risk, especially during a financial crisis. However, managers also have the potential to make overstatements and understatements in fair value financial statements, making the reports unreliable. On the other hand, creditors prefer the historical cost method because it provides a predictable and stable financial metric for debt. But historical cost is detrimental to investors as the information becomes outdated and irrelevant.

Referring to the previous statement, to balance relevance and reliability, it is necessary to integrate financial statements with both fair value and historical cost methods. The goal is to align asset values with economic reality and also mitigate excessive volatility. With fair value, reports can be more relevant, while historical cost helps to reduce the burden due to a decrease in market value. Through this, the conflict of interest between investors and creditors can also be reduced because they have obtained the information needed for both parties. On the manager's side, it also reduces his opportunistic behavior to commit fraud in financial statements because with fair value, financial statements will become more transparent and also the use of historical cost on various instruments makes the opportunity for subjectivity to decrease. PSAK has also used these two methods in the process of measuring assets and liabilities. Therefore, entities need to use a hybrid approach of both methods to create quality financial statements.

The implications of this research have a broad impact, both practically and in the literature. Practically, the findings of this study can provide insights for various entities in determining the most appropriate valuation method, thereby increasing the reliability and relevance of the financial information presented. This also benefits investors and creditors in making more informed economic decisions. In addition, this research also contributes to the evaluation and formulation of accounting policies, which can improve the transparency and quality of financial statements. In literature, this research enriches the accounting literature by deepening the understanding of asset valuation, along with correlating the gap between theory and practice. Thus, it

can also serve as a foundation for the development of accounting policies that are more adaptive and responsive to evolving economic and regulatory dynamics.

This study is limited to taking a sample of companies in the property sector, due to the limited number of companies that have financial statements in 2008 and have explicit disclosure of losses in the fair value of their assets. Therefore, researchers can only obtain one company, PT Lippo Karawaci Tbk. which can be evaluated in depth. While PT Ciputra Development Tbk. is also used as a complement in 2008. Future research suggestions can conduct quantitative testing using a comparison of differences in the use of fair value and historical cost on company performance from the perspective of stakeholders in specific companies to avoid bias due to differences in corporate governance between companies. Research can also use the theory of Positive Accounting Theory by Watts and Zimmerman (1990) to explore the behavioral aspects of managers. This theory is also found to be in line with the findings in this study, as mentioned earlier.

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