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Client and Auditor Conservatism in Timely Loss Recognition of Liabilities for Long-term Employee Benefits from Thailand's New Labor Protection Act

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Abstract

The December 2018 amendment of the Labor Protection Act in Thailand caused different accounting practices for reporting the effect of the amendment among listed companies in the country. Some of them recognized the effect in 2018 while some of them delayed the recognition to 2019. Their different accounting practices call for an investigation into the role of accounting conservatism in Thailand. By using data of 580 listed companies, we found that clients were more likely to opt to delay the recognition and only disclosed the effect in 2018 when there was the official guideline that allowed them to opt to recognize or delay recognizing the effect of the amendment to the later year. With Thailand's unique culture, clients behave more accounting conservative by recognizing/disclosing the greater estimated amounts of the effect of the amendment in 2018 whilst the auditors might at least challenge their clients to disclose the effect in 2018. However, there was doubt as to whether auditor conservatism was undermined by Thailand's Krengjai norm and smooth interpersonal relationship orientation. We then suggest that a clear guideline for the different accounting practices is necessary to reduce the divergence of accounting practices as well as promoting accounting conservatism.

Keywords

Client conservatism, Auditor conservatism, Timely loss recognition, Employee benefits

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Introduction

Accounting conservatism is one of extant important accounting principle (Ball, 2001) which has been the researchers' focus for a very long time as it influences accounting practice (Watts, 2003), quality of financial reporting (Iatridis, 2011), alleviates agency costs (Watts & Zimmerman, 1986) and mitigates information symmetry (Hu, Li, & Zhang, 2014; LaFond & Watts, 2008). However, the level of accounting conservatism varies from country to country (e.g., Ball, Robin, & Sadka, 2008; Ball & Shivakumar, 2005; Chi & Wang, 2010) because of its different institutional settings (LaFond & Watts, 2008). Obviously, it is of interest to investigate accounting conservatism in each country.

There are three main reasons why we chose to observe accounting conservatism in Thailand. First, accounting conservatism in Thailand may differ from other jurisdictions because of its unique institutional settings, especially culture. Owing to its culture of strong uncertainty avoidance, more collectivism, high power distance, more femininity, more long-term orientation (Hofstede et al., 2010), accounting practices in Thailand are more conservative. However, accounting conservatism in Thailand may be undermined by its Krengjai norm and smooth interpersonal relationship orientation (Tangruenrat, 2014). Second, recent evidence of accounting conservatism focusing only on Thailand (e. g., Bangmek et al., 2016; Herrmann et al., 2008; Kiatapiwat, 2010) is limited. Third, the 2018 amendment of the Labor Protection Act caused different accounting practices for reporting the effect of the amendment among listed companies. Some of them recognized the effect in 2018 while some of them delayed the recognition to 2019. Their different accounting practices may lead financial statements incomparable and could in turn impact financial statement users' decision making. These different accounting practices therefore call for an investigation into the role of accounting conservatism in Thailand.

Literature Review and Hypothesis Development

Accounting for Employee Benefits

Employee benefits are defined by TAS 19 as "all forms of consideration given by an entity in exchange for service rendered by employees" (Federation of Accounting Professions, 2018, para. 7). Employee benefits include short-term employee benefits, post-employments benefits, termination benefits, and other long-term employee benefits. Short-term employee benefits are those which employers are expected to pay their employees completely before 12 months after the end of the reporting date in which the employees perform their service. Short-term benefits are, for example, wages and salaries, bonuses, and compensated absences. Post-employment benefits refer to, for example, pensions, lump-sum payment on retirement, and post-employment medical care and life insurance. Termination benefits are those which are settled in case that employment agreements are

terminated. Those benefits other than those included in the previous three categories are defined as other long-term benefits, for example, sabbatical leaves, long-term service leaves, jubilee benefits, and long-term disability benefits.

According to The International Financial Reporting Standards Foundation (2020), these four categories of employee benefits are recognized and measured differently. The short-term employee benefits are recognized when the employees have performed the service and the amount expected to be paid for the service are measured without discount. Post-employment benefits other than termination benefits which are paid after the completion of employment are recognized and measured according to the classification of employee benefit plans. The plan can be classified into either a defined contribution plan or a defined benefit plan. Under the defined contribution plan, an employer pays fixed contribution to other entity which has fully legal or constructive obligation to pay all employee benefits in exchange for employees' service performed in the past and current periods. The employer recognizes this contribution simply as a liability and an expense. On the other hand, a defined benefit plan is a plan other than a defined contribution plan. Under the defined benefit plan, an employer estimates the ultimate cost in exchange for employees' services in the past and current periods. The estimated ultimate cost is then recognized as a defined benefit obligation which is discounted to measure at present value. Plan assets which the employer invested to reserve the fund for settlement of the obligation are also recognized and measured at fair value. Both defined benefit obligation and plan assets are remeasured each period. Deficit or surplus from remeasurement is recognized in profit/ loss or other comprehensive income in the current period. Termination benefits is recognized as a liability and expense when the employer is unable to negotiate the offer of benefits with the employees anymore or when the employer recognizes a restructuring cost where the payment on termination benefits is included in the cost. The recognition and measurement of other long-term benefits are similar to those of defined benefit plans.

Thailand's New Labor Protection Act

In Thailand, the Labor Protection Act was amended and has affected employee benefit plans. The new Labor Protection Act stipulates the increase in the payment on a termination or a retirement from 300 days to 400 days for employees who have rendered the service to employers for an uninterrupted period of 20 years or more. Such employees are eligible to be paid for the termination or the retirement not less than the sum of the final 400 days' pay. The National Legislative Assembly passed a resolution to approve the draft of the new Labor Protection Act on 13 December 2018. The act was later published in the Government Gazette on 5 April 2019.

The passage of the new Labor Protection Act brought the recognition of additional post-employment benefits resulting from the amendment of the new act led to the questions

when and how to recognize the effect of the amendment. On 23 January 2019, the Thailand Federation of Accounting Professions (hereafter TFAC), the Board of Trade of Thailand, the Federation of Thai Industries, and the Thai Bankers' Association had a meeting to discuss these questions. On 7 February 2019, the TFAC circulated the resolution of the meeting. According to the resolution, listed companies were encouraged to exercise their judgement on the recognition of the effect of the amendment on the past service cost of the post-employment benefits. Choice between recognizing the past service cost in the income statements for 2018 or 2019 depends on the listed companies' judgment about in which year the amendment had occurred.

As a result of the listed companies' uses of judgment on the recognition of the effect of the amendment, some of them recognized the effect in 2018 while some of them recognized the effect in 2019. For example, Bangkok Bank Public Company Limited recognized the effect of the amendment as expense in its 2018 income statement amounting to 2.5 billion Baht while Siam Commercial Bank Public Company Limited recognized the effect of the amendment as expense in the first quarter of their 2019 income statement amounting to 1.4-1.5 billion Baht. The Total Access Communication Public Company Limited also recognized the effect of the amendment as expense in their 2018 income statement. Siam Cement Public Company Limited recognized the effect of the amendment as an expense in its first half-year of their 2019 income statement amounting to 2.5 billion Baht with the result that its net profit decreased approximately 2.0 billion Baht.

Accounting Conservatism and Timely Loss Recognition

Accounting conservatism has had a different degree of influence in financial reporting around the world according to each country's institutional factors (e.g., legal system) (Ball et al., 2000). Gilman (1939, p. 130) indicates that accounting conservatism is a tendency which does not comply with the accounting concept of the matching between revenues and costs. Revenues have yet to be recognized until there is a clear warrant for their recognition. However, costs, losses and expenses are recognized in income statements as they were incurred even when their uncertainty about the recognition still exists. According to Watts and Zimmerman (1986, p. 205-206), under the concept of accounting conservatism, assets should be recognized with the lowest value whilst liabilities should be recognized with the highest value. The recognition of revenues should be later instead of sooner whilst the recognition of expenses should be sooner instead of later. Accounting conservatism is interpreted by Basu (1997) as accounting income which is reflected in more timely reporting loss than gain. In other words, loss is recognized quicker than gain. Lafond and Roychowdhury (2008) view that accounting conservatism is to use the stricter standards to recognize bad news than to recognize good news. Accounting conservatism, according to Penman and Zhang (2002), refers to accounting methods and reasoning that result in low net

asset book values. Such practices and justifications are, for example, choosing LIFO inventory accounting over FIFO inventory accounting, expensing research and development expenditure rather of capitalizing and amortizing them, using short estimated assets useful lives and overestimating allowance for bad debt, sales returns or warranty liabilities.

Accounting conservatism is expected to alleviate agency costs (Watts & Zimmerman, 1986) arising from agency problems by improving the efficiency of the contract between managers and shareholders (Shuto & Takada, 2010), by reducing information symmetry (Hu et al., 2014; LaFond & Watts, 2008) and by taking the key role in monitoring managers' investment decisions (Ball, 2001). Ball (2001) underscores that the managers intend to postpone terminating their negative-NPV projects if they derive private benefits and the projects generate positive current earnings. However, timely loss recognition under accounting conservatism brings those losses into the shareholders' attention and scrutiny. As a result of this, the managers are unable to delay the termination. Watts (2003) also indicates that timely loss recognition provides the shareholders and the firm's board of directors with evidence required further investigation of the reasons behind those losses. Ball and Shivakumar (2005) point out that by timely recognizing loss the managers are refrained from deferring loss recognition of ex post negative-NPV projects to later periods. They also have more incentive to continue running the ex post negative-NPV projects and respond quickly to losses.

Client and Auditor Conservatism and Our Hypotheses

Client conservatism reduces audit risk by decreasing inherent risk and audit (DeFond et al., 2016). Clients with a high level of conservatism have less incentive to hide bad news, withhold private information such as R&D investment, and disclose financial information strategically; therefore, there is the low degree of information symmetry between clients and their auditors (J.B. Kim & Zhang, 2016). In addition, they often have a strong corporate governance by having low managerial ownership measured by managers' compensations and the number of shares held by their CEO (Lafond & Roychowdhury, 2008), high takeover protection and low CEO influence on board's decisions (Lara et al., 2009) and strong internal control (Goh & Li, 2011). Conservatism curbs management's risk-taking behaviors (Ahmed & Duellman, 2013) which may lead to the high earnings management (Gao et al., 2019) and a low quality of financial reporting (DeFond et al., 2012). As a result of their high degree of conservatism, these clients are less likely to receive going concern audit reports and their financial statements are less likely to be restated subsequently (DeFond et al., 2016).

The amendment of the Thai Labor Protection Act in 2018 and the TFAC's resolution of the recognition of the effect of the amendment led to the difference in timely loss recognition of past service cost of the post-employment benefits. Such difference may be due

to the extent of client conservatism. Clients with adherence more on the culture of strong uncertainty avoidance, more collectivism, high power distance, more femininity, more long-term orientation (Hofstede et al., 2010), are more conservative. A less conservative accounting practices may lead to a negative market reaction (Y. Kim et al., 2013). We then suggest the following hypotheses.

H_1: Conservative clients are more likely to recognize the effect of the amendment of the Thai Labor Protection Act in their 2018 income statements.

H_2: Conservative clients are more likely to recognize/disclose the greater estimated amounts of the effect of the amendment of the Thai Labor Protection Act in their 2018 financial statements.

H_3: Conservative clients better estimate the amounts of the effect of the amendment of the Thai Labor Protection Act disclosed in their 2018 financial statements.

Being more conservative helps auditors to protect their reputation (Clarkson et al., 2003; DeFond et al., 2012) and generate high-quality audits (Clarkson et al., 2003). More conservative auditors force their clients to adopt more conservative accounting practices (Chung et al., 2002) and also encourage them to have a high level of voluntary disclosures in their annual reports (Clarkson et al., 2003). Auditors are conservative more in determining the last quarter's significant reported losses and earnings decreases than in that of reported gains and earnings increases. This is because reported losses and earnings decrease seem to be more transitionary (Basu et al., 2005) and pose a greater risk to auditors (Cahan & Zhang, 2006; Lennox & Kausar, 2017; Lu & Sapra, 2009). Their behaviors are more conservative when the mass media and the public pay more attention to the profession (Feldmann & Read, 2010), for example, when audit failures were spotlighted (Fafatas, 2010), during the financial crisis (Beams & Yan, 2015), or after stricter laws were enforced (e.g., Sarbanes-Oxley, SEC enforcement actions) (Bannister & Wiest, 2001; Fafatas, 2010).

Listed companies' differences in timely loss recognition of past service cost of the post-employment benefits, which was affected by the amendment of the Thai Labor Protection Act in 2018, may also vary in the degree to which auditors of listed companies in Thailand reacted conservatively to their clients. Auditors are expected to be more conservative because of their motivation to protect their reputation (Clarkson et al., 2003;

DeFond et al., 2012) and to reduce litigation risk (Cahan & Zhang, 2006). We therefore state the following hypotheses.

H_4: Conservative auditors are more likely to force their clients to recognize the effect of the amendment of the Thai Labor Protection Act in their 2018 income statements

H_5: Conservative auditors are more likely to encourage their clients to recognize/disclose the greater amounts of the effect of the amendment of the Thai Labor Protection Act in their 2018 financial statements.

H_6: Conservatism auditors are more likely to encourage their clients to better estimate the amounts of the effect of the amendment of the Thai Labor Protection Act disclosed in their 2018 financial statements.

Thailand's Institutional Settings and Accounting Conservatism

Accounting conservatism varies from country to country (Ball et al., 2008; Ball & Shivakumar, 2005; Chi & Wang, 2010) because of different institutional settings (LaFond & Watts, 2008), e.g., different legal systems (Chi & Wang, 2010), accounting standards (Ball & Shivakumar, 2005), auditing and financial reporting requirements (Ball et al., 2008) and levels of investor protection (Brown Jr, He, & Teitel, 2006). The presupposition that accounting conservatism mitigates information asymmetry (Hu et al., 2014; LaFond & Watts, 2008) might not be globally generalizable (Chi & Wang, 2010). LaFond and Watts (2008) found that the asymmetry of gain and loss recognition, which leads earnings to contain more information about bad news than good news, strengthens information asymmetry between insiders and outsiders. In the US, a common law country with high investor protection, accounting conservatism limits information asymmetry.

Previous studies have observed accounting conservatism outside the US. For example, Chi and Wang (2010) used a sample from Taiwan, a country that has weak investor protection and a code law system. They found that accounting conservatism reduces information asymmetry in countries with a civil or common law like the US only in cases of bad news. Shuto and Takada (2010) studied accounting conservatism in Japan which is a common law country with a unique shareholder structure (cross-shareholding and bank ownership) and a low demand for accounting conservatism. They found that accounting conservatism addresses the agency problem. Firth, Mo, and Wong (2012) provided evidence from China, a country with a low litigation risk. They found that audit firm type affects auditor conservatism. Those from a partnership audit firm are more likely to be conservative than

those from a limited liability audit firm. André, Filip, and Paugam (2015) examined accounting conservatism in 16 European countries. They found that accounting conservatism has profound impact on financial reporting in countries with stringent enforcement on accounting standards compliance and those with high-quality audit settings.

There is a limited number of recent studies of accounting conservatism focusing only on Thailand. For example, Herrmann et al. (2008) investigated accounting conservatism after the financial crisis in 1997). They found that clients but not auditors were more conservative after the financial crisis. Kiatapiwat (2010) found that firms with shareholder concentration exhibit less accounting conservatism. Shareholder concentration may lead controlling shareholders to behave opportunistically to expropriate benefits from minority shareholders. Bangmek et al. (2016) found that conservative managers provide more reliable information on earnings forecasts.

We therefore contribute to the literature on accounting conservatism and timely loss recognition from Thailand which has a unique institutional settings. Thailand is a civil law country influenced by a common law (Central of Intelligence Agency, 2020) with weak investor protection and presence of earnings management (Leuz et al., 2003), strong secrecy culture (Hope et al., 2008), and strong religiosity (André et al., 2015). Its culture has a high level of uncertainty avoidance, collectivism, power distance, femininity, and long-term orientation (Hofstede et al., 2010). It also has a strong "Krengjai" norm. The Thai word "Krengjai" is defined as being "instrumental to all behaviors concerning the attempts to maintain social harmony in terms of smooth social (Tangruenrat, 2014, p. 93)". The Krengjai norm significantly influences Thais' behaviors (Komin, 1990). With Krengjai mentality, a Thai easily agrees to another person's requests and avoids disagreements (Holmes et al., 1995). Thais prefer to maintain a good relationship with other people if they derive benefits form those people (Runglertkrengkrai & Engkaninan, 1987).

Research Design

Client Conservatism

To measure client conservatism, we follow Basu (1997) who proposed to capture the asymmetry between timely recognition of good news and bad news by the following regression model:

$EPS_{it}/_{P_{it-1}} = \alpha_0 + \alpha_1 DR_{it} + \beta_0 R_{it} + \beta_1 R_{it} * DR_{it} + \varepsilon_{it}$, where EPS is earnings per share of company i in year i, P is market price per share of company i in year $i-1$, R is buy-and-hold stock return and similar to Raonic, McLeay, and Asimakopoulos (2004) is computed by $(^{P_t}/_{P_{t-1}}) - 1$, DR is a dummy variable and equals 1 if R < 0, 0 otherwise. We estimate the coefficients for each company using panel data of four years covering 2015-2018.

According to Basu (1997), good news and bad news are reflected in stock return. Good news is reflected in positive stock returns whilst bad news is reflected in negative stock return. If there is the asymmetric verification of good news and bad news for their recognition, bad news is lesser verified and is sooner recognized than good news. Raonic et al. (2004) draw the model of Basu (1997) simply as $EPS_{it}/P_{it-1} = \alpha_0 + \beta_0 R_{it} + \varepsilon_{it}$. They explain that coefficient β_0 is the indicator of timeliness of the recognition of good news and bad news. By assuming α_0 = 0, β_0= 1, earnings per share equals the change in market price. Reported earnings are unbiased and the asymmetry of timely recognition of good news and bad news does not exist. However, β_0<1 indicates that the asymmetry exists and market information influences reported earnings. α_1 captures the degree to which reported earnings respond to good news (positive stock returns) whilst β_1 captures the degree to which reported earnings respond to bad news (negative stock returns). By adapting the interpretation of conservative accounting of Raonic et al. (2004), clients exhibit their conservatism if β_1 is positive and the ratio of $(\alpha_1 + \beta_1)/\alpha_1$ is greater than one.

Auditor Conservatism

Similar to previous studies, we use the type of audit firm size to measure auditor conservatism. Theoretically, Big N is more conservative than non-Big N (Lee et al., 2006) and more risk averse (Lennox & Kausar, 2017) because they have greater motivation to maintain their reputation (Clarkson et al., 2003). Clients audited by the Big 6 were found to provide more voluntary disclosure on information about their Y2K problem in 2000 than those audited by a non-Big 6 (Lee et al., 2006). Big 4's clients are more sensitive to bad news than non-Big 4's clients (Herrmann et al., 2008) and more conservative in their financial reporting (Beekes et al., 2004). Big 4 is more likely to retain their low-risk clients after the Enron collapse (Feldmann & Read, 2010) and to issue going concern opinions (Beams & Yan, 2015). Their going concern opinions more precisely predict the future bankruptcies than those of non-Big 4 (Fafatas, 2010). Big 4 is less tolerant of their clients' misstatements (Francis & Wang, 2008) and earnings management (Beekes et al., 2004).

Model

To test our *H1* and *H4*, we use only data from 2018 when the National Legislative Assembly passed a resolution to approve the draft of the new Labor Protection Act and use three-level ordered probit model which was also used by Francis and Krishnan (1999). Francis and Krishnan (1999) study the association between accounting accruals and auditor reporting conservatism. By applying the concept of Francis and Krishnan (1999), we assume that clients (auditors) had three choices to report the effect of the amendment of the Thai Labor Protection Act in 2018. The three choices are given in ascending order of the level of

conservatism as ignoring the effect, deferring the recognition to the later year but disclosing the effect in their 2018 financial statements, and recognizing the effect in their 2018 income statements. The client (auditor)'s choice can be drawn by $z^* = X\beta + \varepsilon$, where X is a vector of client's observed characteristics and ε is a random error term. The judgement on the choice z^*varies according to threshold points μ_1 and μ_2. If a client (an auditor) is the least conservatism or sees that the effect is not material to their financial statements, z^* is below μ_1 and this can be interpreted that they tend to ignore the effect. If a client (an auditor) is somewhat conservative and views that the effect is material to financial statements, z^* is in the range of [μ_1, μ_2] and this can be interpreted that they tend to defer the recognition of the effect to the later year but disclose the effect in their 2018 financial statements. If a client (an auditor) is the most conservative and views that the effect is material to financial statements, z^* is greater than μ_2 and this can be interpreted that they tend to recognize the effect in 2018's income statements.

We further expand the simple model $z^* = X\beta + \varepsilon$ into our base model as follows:

$$ReEBP = \beta_0 + \beta_1 CCon + \beta_2 ACon + \beta_3 AvCFO + \beta_4 AvROA + \beta_5 BM + \beta_6 LogA + \beta_7 LEV + \beta_8 LogLEMP + \beta_9 FCh + \beta_{10} CEOCh + \beta_{11} Union + \varepsilon$$

.

`$ReEBP$ represents a company (an auditor)'s choice to report the effect of the amendment of the Thai Labor Protection Act in 2018. It is coded as 0 if a company (an auditor) ignored the effect, 1 if a company (an auditor) deferred the recognition of the effect to the later year but disclosed the effect in their 2018 financial statements, and 2 if a client (an auditor) recognized the effect in their 2018 income statements. $CCon$ and $ACon$ are our variable of interests. $CCon$ represents client conservatism whilst $ACon$ represents auditor conservatism. $CCon$ is a dummy variable and equals 1 if a client exhibits their conservatism as explained earlier and 0 otherwise. $ACon$ is a dummy variable and equals 1 if an auditor is part of the Big 4 and 0 otherwise.

Our control variables are adapted from the studies of Krishnan (1994), Francis and Krishnan (1999) , and Khan and Watts (2009) . Krishnan (1994) tested the association between auditor switching and conservatism. Francis and Krishnan (1999) examined the relation between accounting accruals and auditor reporting conservatism. Khan and Watts (2009) studied a company's characteristics which indicate accounting conservatism. Beaudoin, Chandar, and Werner (2010) observed the companies' judgment to freeze their defined benefit pension plan after SFAS 158.

Similar to Beaudoin et al. (2010), we control for a company's cash flow position and performance. $AvCFO$ is used to control for a company's cash flow position and is defined as the average of cash flow from operations deflated by total assets for three years before the new Labor Protection Act. $AvROA$ is used to control for a company's performance and is

defined as the average of return on assets for three years before the new Labor Protection Act. We expect a positive association between $AvCFO$ and $ReEBP$ and between $AvROA$ and $ReEBP$. We expect that a client is more likely to recognize the effect of the new Labor Protection Act in their 2018 income statements while having a healthier cash flow position and better performance. The postponement of recognition of the effect may result in the decrease in their profits and poorer performance in the later year.

We control for a company's leverage and growth as Beaudoin et al. (2010) did. LEV is the ratio of total debt to total assets while BM is the book-to-market ratio. We expect both LEV and BM to have a negative association with $ReEBP$. We expect that a company with a lot of debt and strong growth has greater motivation to defer the recognition of the effect to the later year. The company may worry that the recognition would increase their liabilities and lessen their growth.

We control for CEO changing as Beaudoin et al. (2010) found the negative association between CEO's service year and the decision to freeze their defined benefit pension plans. $CEOCh$ is a dummy variable and equals 1 if a company changed their CEO and 0 otherwise. We expect the negative association between $CEOCh$ and $ReEBP$. We expect that the new CEO may have the greater motivation to delay the recognition of the effect to the later year because the recognition would lead to the lower performance in their first year of service.

As Beaudoin et al. (2010) found that the greater balance of net assets of employee benefit leads CEOs to be unable to freeze their defined benefit pension plan, we further control for the provision of employee benefit both before and after the amendment of the Thai Labor Protection Act. $LogLEMP$ is the natural logarithm of provisions for employee benefits at the end of the year. We expect the positive association between $LogLEMP$ and $ReEBP$. We expect that a client is more likely to recognize the obligation of the effect in their 2018's financial statements if the balance of the provision of employee benefit is material to financial statements.

We control for the presence of labor union as Beaudoin et al. (2010) did. $Union$ is a dummy variable and equals 1 if a company has a labor union and 0 otherwise. We expect the positive association between $Union$ and $ReEBP$. We expect that a labor union may put pressure on their company to recognize the obligation of the effect in the company's 2018 financial statements. Presumably, the recognition may help the labor union to ensure their valid claim for benefits from their company.

We control for the switching of audit firms as Krishnan (1994) found that auditors are more conservative in auditing their new clients for the first year. FCh is a dummy variable and equals 1 if a company switched audit firms and 0 otherwise. We expect a positive association between FCh and $ReEBP$. We expect that successor auditors with more conservatism have

greater motivation to encourage their clients to recognize the obligation of the effect in their 2018's financial statements.

We further control for a company's size. By following Francis and Krishnan (1999), $LogA$ is used to control for a company's size and is defined as the natural logarithm of total assets at the beginning of the year. We expect the positive association between $LogA$ and $ReEBP$. We expect that a larger company may exhibit greater conservatism because they have the greater litigation risk (Khan & Watts, 2009), thereby being more likely to recognize the effect in their 2018's financial statements.

We replace $ReEBP$ with $LogEEBP$ to test our H_2 and H_5 whilst we replace $ReEBP$ with $DiffEBP$ to test our H_3 and H_6 and apply OLS regressions. We use data of 2018 for testing these hypotheses. $LogEEBP$ is used to test the association between conservatism and amounts of the effect of the amendment of the Thai Labor Protection Act recognized/disclosed in their 2018 financial statements. $LogEEBP$ is defined as the natural logarithm of the effect recognized/disclosed in their 2018 financial statements. $DiffEBP$ is used to test the association between conservatism and the difference between the actual amounts of the effect recognized in their 2019 financial statements and the estimated amounts of the effect disclosed in their 2018 financial statements. We further classify our sample into two groups: $Underestimate$ and $Overestimate$. $Underestimate$ is the group which the disclosed amounts of the effect estimated in 2018 is lesser than the amounts of the effect recognized in 2019. On the other hand, $Overestimate$ is the group which the disclosed amounts of the effect estimated in 2018 is greater than the amounts of the effect recognized in 2019. $DiffEBP$ is the natural logarithm of the absolute value of difference between the actual amounts of the effect recognized in 2019's financial statements and the estimated amounts of the effect disclosed in their 2018 financial statements. We regress $DiffEBP$ model by each group. We also code $UndEst$ which equals 1 for $Underestimate$ group and 0 for $Overestimate$ group.

Sample and Data

We begin with 28 December 2018's list of all 771 listed companies traded on the Stock Exchange of Thailand. Six companies were excluded from our sample because they were under rehabilitation. To estimate client conservatism, we collected four years of stock price data (2015-2018) from www.settrade.com. 185 companies were excluded from our sample because of insufficient data for estimating client conservatism or for our models. For our models, most data were collected from companies' financial statements and annual reports published on www.sec.or.th. We collected data until 2018 for most companies except for $AvCFO$ and $AvROA$.. For these companies we collected data from 2015-2017, and for ACh and $CEOCh$ we collected data from 2017-2018. We also collected data on companies'

actual amounts of the effect of the amendment of the Thai Labor Protection in 2018 recognized in their 2019 financial statements. The result was a sample of 580 companies. These companies provided a sufficient amount of data for our models.

Result

Descriptive Statistics

Table 1 presents descriptive statistics for our variables. Panel A shows descriptive statistics for $ReEBP$ model. 512 companies (88.3%) chose to defer the recognition of the effect of the amendment of the Thai Labor Protection in 2018 to 2019 but disclosed the effect in their 2018 financial statements. 62 companies (10.7%) ignored the effect. Only 6 companies (1.0%) recognized the effect in their 2018 income statements. Conservative clients ($CCon$) were 50.4%, 50.0% and 48.4% of companies with deferment, companies with recognition and companies with ignorance, respectively. 69.4%, 59.6%, and 16.7% of companies with ignorance, companies with deferment, and companies with recognition were audited by Big 4 ($ACon$), respectively. The average of $LogA$ ($LogLEMP$) was 22.812 (0.510), 22.342 (0.441), and 21.449 (0.408) for companies with ignorance, companies with deferment, and companies with recognition, respectively. Most of all groups did not change their CEOs and audit firms and did not have labor union.

Table 1's Panel B reports descriptive statistics for $LogEEBP$ model. We found that conservative clients disclosed lesser estimated amounts of the effect of the amendment of the Thai Labor Protection in 2018. However, clients audited by conservative auditors, who typically audit large companies, disclosed greater estimated amounts. Table 1's Panel C reports descriptive statistics for $DiffEBP$ model. 167 companies (53.7%) are in *Overestimate* group. We do not find any different characteristic of these two groups.

Table 1 Descriptive statistics

Panel A: ReEBP Model

	Ignorance (Obs = 62)				**Deferment (Obs = 512)**				**Recognition (Obs = 6)**			
Variable	**Mean**	**Std. Dev.**	**Min**	**Max**	**Mean**	**Std. Dev.**	**Min**	**Max**	**Mean**	**Std. Dev.**	**Min**	**Max**
CCon	0.484	0.504	0.000	1.000	0.504	0.500	0.000	1.000	0.500	0.548	0.000	1.000
AvCFO	0.103	0.075	0.011	0.348	0.087	0.057	0.004	0.488	0.066	0.037	0.009	0.113
AvROA	0.088	0.080	0.002	0.435	0.073	0.060	0.004	0.429	0.078	0.070	0.015	0.208
BM	0.821	0.671	0.109	4.298	1.020	0.774	0.028	7.908	1.122	0.719	0.301	2.252
LogA	22.812	2.038	18.796	28.407	22.342	1.657	19.265	28.790	21.449	0.673	20.556	22.420
LEV	0.510	0.260	0.020	0.951	0.441	0.220	0.022	1.215	0.408	0.300	0.117	0.877
LogLEMP	0.010	0.013	0.000	0.071	0.015	0.017	0.000	0.129	0.012	0.007	0.002	0.023
ACon	0.694	0.465	0.000	1.000	0.596	0.491	0.000	1.000	0.167	0.408	0.000	1.000
FCh	0.081	0.275	0.000	1.000	0.088	0.283	0.000	1.000	0.000	0.000	0.000	0.000
CEOCh	0.129	0.338	0.000	1.000	0.133	0.340	0.000	1.000	0.167	0.408	0.000	1.000
Union	0.016	0.127	0.000	1.000	0.023	0.151	0.000	1.000	0.000	0.000	0.000	0.000

Table 1 **Descriptive statistics** (Continued)

Panel B: EEBP Model

	Client conservatism										Auditor conservatism									
	CCon = 0 (Obs.=254)				CCon = 1 (Obs.=258)				Difference		ACon = 0 (Obs.=207)				ACon = 1 (Obs.=305)				Difference	
Variable	Mean	Std. Dev.	Min	Max	Mean	Std. Dev.	Min	Max	T-test		Mean	Std. Dev.	Min	Max	Mean	Std. Dev.	Min	Max	T-test	
EEBP	15.626	1.588	11.678	21.859	15.167	1.449	11.283	21.372	0.459	***	14.862	1.431	11.283	21.372	15.756	1.500	11.408	21.859	-0.894	***
CCon											0.531	0.500	0.000	1.000	0.485	0.501	0.000	1.000	0.046	
AvCFO	0.095	0.060	0.004	0.488	0.078	0.052	0.004	0.426	0.017	***	0.083	0.058	0.004	0.488	0.090	0.056	0.004	0.426	-0.007	
AvROA	0.077	0.054	0.008	0.390	0.068	0.065	0.004	0.429	0.008		0.074	0.070	0.005	0.429	0.071	0.052	0.004	0.303	0.003	
BM	0.907	0.610	0.028	3.481	1.132	0.894	0.108	7.908	-0.224	***	1.179	0.922	0.069	7.908	0.913	0.633	0.028	4.878	0.266	***
LogA	22.587	1.738	19.831	28.780	22.100	1.538	19.265	28.790	0.486	***	21.707	1.395	19.453	28.639	22.772	1.684	19.265	28.790	-1.065	***
LEV	0.435	0.213	0.071	0.889	0.446	0.228	0.022	1.215	-0.011		0.408	0.214	0.041	0.990	0.463	0.221	0.022	1.215	-0.055	***
LogLEMP	0.015	0.017	0.001	0.116	0.014	0.016	0.000	0.129	0.001	***	0.016	0.017	0.000	0.129	0.014	0.017	0.000	0.116	0.002	
ACon	0.618	0.487	0.000	1.000	0.574	0.496	0.000	1.000	0.044											
FCh	0.079	0.270	0.000	1.000	0.097	0.296	0.000	1.000	-0.018		0.106	0.309	0.000	1.000	0.075	0.264	0.000	1.000	0.031	
CEOCh	0.118	0.323	0.000	1.000	0.147	0.355	0.000	1.000	-0.029		0.106	0.309	0.000	1.000	0.151	0.358	0.000	1.000	-0.045	
Union	0.016	0.125	0.000	1.000	0.031	0.174	0.000	1.000	-0.015		0.0241546	0.154	0.000	1.000	0.023	0.150	0.000	1.000	0.001	

*, **, and *** denote significance at 0.10, 0.05, and 0.01 levels (two-tailed), respectively.

Table 1 Descriptive statistics (Continued)

Panel C: DiffEBP Model

	Undest= 0 (Obs.=167)				Undest = 1 (Obs.=144)				Difference
Variable	**Mean**	**Std. Dev.**	**Min**	**Max**	**Mean**	**Std. Dev.**	**Min**	**Max**	**T-test**
DiffEBP	12.221	2.929	-2.408	17.479	12.217	2.633	6.908	17.315	0.990
Ccon	0.473	0.501	0.000	1.000	0.465	0.501	0.000	1.000	0.892
AvCFO	0.091	0.050	0.004	0.226	0.088	0.062	0.005	0.426	0.690
AvROA	0.075	0.053	0.006	0.336	0.074	0.060	0.004	0.429	0.876
BM	0.977	0.837	0.028	7.908	0.932	0.544	0.126	2.571	0.571
LogA	22.152	1.565	19.481	27.177	22.186	1.375	19.265	28.768	0.841
LEV	0.419	0.198	0.037	1.000	0.428	0.228	0.071	0.871	0.736
LogLEMP	0.015	0.017	0.000	0.111	0.015	0.016	0.000	0.129	0.869
ACon	0.611	0.489	0.000	1.000	0.583	0.495	0.000	1.000	0.624
FCh	0.054	0.226	0.000	1.000	0.097	0.297	0.000	1.000	0.155
CEOCh	0.126	0.333	0.000	1.000	0.118	0.324	0.000	1.000	0.837
Union	0.012	0.109	0.000	1.000	0.021	0.143	0.000	1.000	0.545

Correlations

Table 2 reports Spearman's correlations. Panel A reports the correlations of variables for $ReEBP$ model. We found no correlation between $ReEBP$ and $CCon$. However, we found negative correlations between $ReEBP$ and $ACon$, and between $ReEBP$ and $LogA$. Positive correlations were found between $ReEBP$ and BM, and between $ReEBP$ and $LogLEMP$. This is initial evidence that client conservatism is not associated with the choice to report the effect of the amendment of the Thai Labor Protection in 2018. Surprisingly, conservative auditors do not encourage their clients to recognize the effect in their 2018 income statements. Companies with higher growth or greater balance of provision for employee benefits are more likely to recognize the effect in their 2018 income statements but those with greater size are more likely to defer the recognition of the effect to the later year. The correlations between each pair of variables are small, suggesting that our $ReEBP$ model does not have a multicollinearity problem.

Table 2's Panel B reports the correlations of variables for $LogEEBP$ model. We found negative correlation between $LogEEBP$ and $CCon$ but no correlation between $LogEEBP$ and $ACon$. This initial data is surprising because it provides evidence that conservative clients reported lesser estimated amounts of the effect of the amendment of the Thai Labor Protection in 2018 disclosed in their 2018 financial statements. We also found positive correlations between $LogEEBP$ and $LogA$ and between $LogEEBP$ and $Union$. This is evidence that larger companies and the presence of labor unions have a greater estimated amounts of the effect of the amendment of the Thai Labor Protection in 2018. The correlations between each pair of variables are small except for the correlations between $LogA$ and $LogEEBP$ (coef. = 0.677, P<0.01). However, their VIFs are small 2.95 for $LogA$ and 2.44 for $LogEEBP$. This suggests that our $LogEEBP$ model does not have a multicollinearity problem.

Table 2's Panel C reports the correlations of variables for $DiffEBP$ model. We found positive correlations between $DiffEBP$ and $ACon$ but no correlation between $LogEEBP$ and $CCon$. This is contradictory to the evidence reported in Table 2's Panel B which we observe only estimated the amount of the amendment of the Thai Labor Protection in 2018 disclosed in their 2018 financial statements. This can imply that conservative auditors are more likely to be more conservative in subsequent years when their clients have recognized the effects in their 2019 financial statements. Or alternatively, their clients may have better information for more reasonably estimating of the effect of the amendment in 2019 than that in 2018. Therefore, the 2019's recognized amounts of the effect are greater than the 2018's estimated and disclosed amounts.

We also found positive correlations between $DiffEBP$ and $LogA$ and between $DiffEBP$ and $LogLEMP$. This is evidence that larger companies and those with a greater balance of provision for employee benefits tend to have greater uncertainty about the estimates of the effect. The correlations between each pair of variables are small except for the correlations between $LogA$ and $LogEEBP$ (coef. = 0.671, P<0.01). However, their VIFs are small 2.73 for $LogA$ and 2.30 for $LogEEBP$. This suggests that our $DiffEBP$ model does not have multicollinearity problem.

Table 2 Spearman's correlations

Panel A: ReEBP Model

	(1)		(2)		(3)		(4)		(5)		(6)		(7)		(8)		(9)	(10)	(11)	(12)
(1) ReEBP	1.000																			
(2) CCon	0.012		1.000																	
(3) AvCFO	-0.061		-0.157	***	1.000															
(4) AvROA	-0.050		-0.131	***	0.480	***	1.000													
(5) BM	0.103	**	0.116	***	-0.300	***	-0.479	***	1.000											
(6) LogA	-0.082	*	-0.171	***	-0.159	***	-0.210	***	0.037		1.000									
(7) LEV	-0.093	**	0.046		-0.225	***	-0.327	***	-0.093	*	0.398	***	1.000							
(8) LogLEMP	0.105	**	-0.065		0.212	***	0.206	***	-0.069		-0.375	***	-0.297	***	1.000					
(9) ACon	-0.087	*	-0.050		0.052		0.010		-0.158	***	-0.364	***	-0.133	***	-0.288	***	1.000			
(10) FCh	-0.002		0.036		-0.068		-0.087	*	-0.082	*	-0.008		-0.041		-0.031		-0.064	1.000		
(11) CEOCh	0.007		0.034		-0.001		-0.044		0.058		0.089	*	0.064		0.071		0.069	-0.012	1.000	
(12) Union	0.010		0.034		-0.056		-0.106	**	0.089	*	0.079		0.038		0.116	***	0.004	-0.005	0.009	1.000

*, **, and *** denote significance at 0.10, 0.05, and 0.01 levels (two-tailed), respectively.

Table 2 Spearman's correlations (Continued)

Panel B: EEBP Model

	(1)		(2)		(3)		(4)		(5)		(6)		(7)		(8)		(9)		(10)	(11)	(12)
(1) ReEBP	1																				
(2) CCon	-0.149	***	1.000																		
(3) AvCFO	-0.044		-0.151	***	1.000																
(4) AvROA	-0.075		-0.148	***	0.462	***	1.000														
(5) BM	-0.017		0.126	***	-0.295	***	-0.468	***	1.000												
(6) LogA	0.709	***	-0.139	***	-0.154	***	-0.186	***	0.041		1.000										
(7) LEV	0.275		0.019		-0.214	***	-0.335	***	-0.075		0.434	***	1.000								
(8) LogLEMP	0.914		-0.203	***	-0.015		-0.057		-0.010		0.677	***	0.213	***	1.000						
(9) ACon	0.298		-0.045		0.083		0.025		-0.155	**	0.348	***	0.126	***	0.270	**	1.000				
(10) FCh	0.000		0.032		-0.095	***	-0.068		0.057		0.010		0.059		-0.002		-0.054		1.000		
(11) CEOCh	0.076		0.043		0.010		-0.063		0.070		0.090	*	0.087	*	0.056		0.064		0.001	1.000	
(12) Union	0.089	*	0.050		-0.039		-0.096	*	0.092	*	-0.067		0.024		0.107	**	-0.004		-0.003	0.016	1.000

*, **, and *** denote significance at 0.10, 0.05, and 0.01 levels (two-tailed), respectively.

Table 2 Spearman's correlations (Continued)

Panel C: DiffEBP Model

	(1)		(2)	(3)		(4)		(5)		(6)		(7)	(8)		(9)		(10)	(11)	(12)	(13)
(1) DiffEBP	1.000																			
(2) UndEst	-0.015		1.000																	
(3) CCon	-0.076		-0.008	1.000																
(4) ACon	0.138	**	-0.028	0.009		1.000														
(5) AvCFO	0.090		-0.070	-0.217	***	0.147	**	1.000												
(6) AvROA	-0.037		-0.043	-0.213	***	0.012		0.497	***	1.000										
(7) BM	0.093		0.030	0.134	**	-0.103		-0.320	***	-0.562	***	1.000								
(8) LogA	0.229	***	0.046	-0.060		0.312	***	-0.086		-0.121	*	0.067	1.000							
(9) LEV	0.055		0.012	0.088		0.105		-0.227	***	-0.334	***	-0.013	0.418	***	1.000					
(10) LogLEMP	0.365	***	0.039	-0.115	*	0.271	***	0.021		-0.032		0.041	0.671	***	0.186	***	1.000			
(11) FCh	-0.006		0.083	0.005		-0.119	*	-0.093		-0.086		0.057	0.012		0.035		0.018			
(12) CEOCh	-0.015		-0.012	0.023		0.086		0.041		-0.023		0.029	0.088		0.053		0.059	-0.068	1.000	
(13) Union	0.002		0.035	-0.018		0.001		0.015		0.024		0.087	-0.017		-0.060		0.037	-0.036	-0.048	1.000

*, **, and *** denote significance at 0.10, 0.05, and 0.01 levels (two-tailed), respectively.

Regression Results

Table 3 shows regression results. For testing our H_1 and H_4, we found that the coefficients of $CCon$ and $ACon$ are not statistically significant. We therefore reject H_1 that conservative clients are more likely to recognize the effect of the amendment of the Thai Labor Protection Act in their 2018 income statements and H_4 that conservative auditors are more likely to force their clients to recognize the effect of the amendment of the Thai Labor Protection Act in their 2018 income statements. However, we found the negative coefficients of $AvCFO$ (coef. = -2.4422, P<0.10) and $LogA$ (coef. = -0.1582, P<0.05) are statistically significant. This is evidence that client conservatism and auditor conservatism do not influence the report on the effect of the amendment of the Thai Labor Protection in 2018. However, larger companies with a better cash flow position tended to defer the recognition of the effect to the later year but disclose the effect in their 2018 financial statements.

For testing our H_2 and H_5, we found that the positive coefficient of $CCon$ (coef. = + 0.1150, P<0.05) is statistically significant but the coefficient of $ACon$ is not statistically significant. We accept H_2 that conservative clients are more likely to disclose the greater estimated amounts of the effect of the amendment of the Thai Labor Protection Act in their 2018 financial statements. We reject H_5 that conservative auditors are more likely to encourage their clients to disclose the greater estimated amounts of the effect of the amendment of the Thai Labor Protection Act in their 2018 financial statements. We further found that the positive coefficients of $LogA$ (coef.=+0.1458, P<0.01), LEV (coef.=+0.3115, P<0.05), and $LogEEBP$ (coef.=+0.7530, P<0.01) are statistically significant. This is evidence that larger companies and those with a higher leverage and greater balance of provision for employee benefits tended to disclose the greater estimated amount of the effect.

For testing our H_3, we found that the coefficients of $CCon$ is not statistically significant for both $Underestimate$ and $Overestimate$ groups. We therefore reject H_3 that conservative clients better estimate the amounts of the effect of the amendment of the Thai Labor Protection Act disclosed in their 2018 financial statements. The approval of the draft of the new Labor Protection Act on 13 December 2018 might make it difficult for listed companies to obtain enough information to make a reasonable estimation of the effect of the amendment. Thus, client conservatism might not affect the overestimation or underestimation of the effect as of 31 December 2018.

The test of H_6 provides unexpected results. We expected the negative coefficient of $ACon$ and hypothesized that conservatism auditors are more likely to encourage their clients to better estimate the amounts of the effect of the amendment of the Thai Labor Protection

Act disclosed in their 2018 financial statements. However, we found the positive coefficient of $ACon$ (coef. = +0.8983, P<0.10) is statistically significant only for the $Underestimate$ group. We further found that the positive coefficients of $LogLEMP$ are statistically significant for both $Underestimate$ and $Overestimate$ groups. This is evidence that companies with greater balance of provision for employee benefits have greater deviation between the amounts of the effect estimated and disclosed in 2018 and the amounts of the effect recognized in 2019. This supports our explanation of the difficulty in and uncertainty of the estimations of the effect.

Table 3 Regression results

	Predicted	Order probit regression H1 and H4 ReEBP		OLS regression H2 and H5 LogEEBP		OLS regression H3 and H6 DiffEBP			
						Underestimate		Overestimate	
	Sign	Coef.	P-value	Coef.	P-value	Coef.	P-value	Coef.	P-value
CCon	+ for H_1 and H_2 /- for H_3	-0.0415	0.768	0.1150 **	0.018	0.1635	0.716	-0.5293	0.233
ACon	+ for H_4 and H_5 /- for H_6	-0.1981	0.189	0.0739	0.148	0.8983 *	0.052	0.4270	0.369
AvCFO	+	-2.4422 *	0.052	0.1303	0.789	9.1436 *	0.065	-1.9124	0.678
AvROA	+	-1.1531	0.340	0.2199	0.638	-0.2663	0.955	3.1002	0.548
BM	-	0.0721	0.477	0.0090	0.787	0.8738 ***	0.003	0.2344	0.604
LogA	+	-0.1582 **	0.021	0.1458 ***	0.000	-0.0329	0.888	-0.1223	0.619
LEV	-	-0.4209	0.193	0.3115 **	0.012	0.5915	0.609	-0.0040	0.997
LogLEMP	+	0.0941	0.134	0.7530 ***	0.000	0.7514 ***	0.001	0.7090 ***	0.003
FCh	+	-0.1378	0.564	0.0084	0.919	1.3262	0.161	-0.9019	0.232
CEOCh	+	0.1023	0.605	0.0633	0.361	-0.8861	0.154	-0.3671	0.593
Union	+	0.1193	0.804	-0.1450	0.351	0.8600	0.650	-0.4242	0.781
Constant				-1.357 ***	0.000	-2.7077	0.418	2.3701	0.558
N		580		512		167		144	
Log likelihood		-218.5		n/a		n/a		n/a	
Adj R-squared		n/a		88%		20%		6%	
Prob > F		n/a		0.000 ***		0.000 ***		0.064 *	

*, **, and *** denote significance at 0.10, 0.05, and 0.01 levels (one-tailed), respectively. The sample for testing H_3 and H_6 is reduced from 512 to 311 because 179 companies did not disclosed amount of the effect recognized in 2019, 11 companies did not have the deviation between the amount of the effect estimated and disclosed in 2018 and the amount of the effect recognized in 2019, and 9 companies are deleted because they were outlier as we winsorize variable $DiffEBP$ at 1-99%

Conclusion

Our descriptive statistics provides evidence that listed companies were more likely to opt to delay the recognition and only disclosed the effect of the amendment of the Thai Labor Protection Act in 2018 when there was the official guideline that allowed them to do so. This is because they might be aware that the sudden recognition of the effect of the amendment in the last quarter of 2018 would result in a decrease in earnings or loss, or missing earnings benchmarks. The stock market penalizes firms when reporting a decrease in earnings or loss (Biell & Muller, 2013) or when they miss an earnings benchmark (Lopez & Rees, 2002). Missing an earnings benchmark also affects management bonuses (Edmonds et al., 2013; Matsunaga & Park, 2001). In addition, there is evidence that auditor conservatism led auditors to be less tolerant towards clients' ignorance of reporting the effects in 2018. The auditors might at least challenge their clients to disclose the effect in 2018.

According to the result of the three-level probit model, H_1 and H_4 are rejected. This may be because the small proportion of conservative clients which recognized the effect of the amendment in 2018. We were thus unable to conclude that client and auditor conservatism impact reporting of the effect of the amendment of the Thai Labor Protection Act in 2018. The results of OLS regressions lead to the acceptance of H_2, the acceptance of wrong sign of H_6 and the rejections of H_3 and H_5. These indicate that client conservatism plays a crucial role in reporting the effect of the amendment of the Thai Labor Protection Act in 2018. Clients with more conservatism recognized/disclosed the greater estimated amounts of the effect of the amendment in their 2018 financial statements.

The possible explanations for the unexpected results of H_6 are at least threefold. First, conservative auditors were more conservative in 2019 and they might obtain better evidence of the estimations of the effects recognized in 2019. They tended to challenge these clients to adjust the estimations of the effect and recognize the greater amounts of the effect in 2019 than those amounts estimated and disclosed in 2018. Second, the estimation of the provision for long-term employee and post-employment benefits required the clients to exercise their judgement on key assumptions, e.g., future salary rates, mortality rates, discount rates, and employee turnover rates. For auditors, clients' underestimate of the effect of the amendments may have a severer consequence (e.g., loss of reputation) than overestimate. Therefore, conservative auditors paid more attention to their clients' underestimations because the estimation is subject to high uncertainty and is difficult to determine the value of employee benefit obligations and their clients were prone to underestimate the effect of the amendment rather than overestimate. Third, auditor conservatism may be undermined by Thailand's Krengjai norm. Owing to Thailand's Krengjai

norm and smooth interpersonal relationship orientation (Tangruenrat, 2014) auditors might compromise with their clients on the choice to recognize or to delay the recognition to the later year**.**

In sum, if the amendment of the Thai Labor Protection Act in 2018 is bad news as it results in companies' loss and liability, its effect might be theoretically recognized in 2018 under conservative accounting. However, the guideline with the free choice to recognize or to delay recognizing the effect of the amendment in 2018 led most of listed companies traded on the Stock Exchange of Thailand to opt to delay the recognition and only disclose the effect of the amendment. Nonetheless the sudden recognition of this bad news in the last quarter of 2018 might cause negative impacts. We also found some evidence that client and audit conservative existed to some extent due to Thailand's culture of strong uncertainty avoidance, collectivism, high power distance, femininity, and long-term orientation (Hofstede et al., 2010). Clients with more conservatism recognized/disclosed the greater estimated amounts of the effect of the amendment in their 2018 financial statements whilst the auditors might at least challenge their clients to disclose the effect in 2018. Interestingly, we suspected that auditor conservatism may be undermined by Thailand's Krengjai norm and smooth interpersonal relationship orientation (Tangruenrat, 2014). Auditors might compromise with their clients on the choice to recognize or to delay the recognition to the later year as the guideline allowed them to have the free choice. The compromise between auditors and their clients helps maintain the good relation between them (Gibbins et al., 2010; Herrbach, 2005) but impairs auditor independence (Ashbaugh et al., 2003).

We suggest that when there is a circumstance which causes the different accounting practices, there should be a clear guideline for it which would militate against the divergence of accounting practices and promote accounting conservatism. Nonetheless, owing to the guideline to allow financial statements preparers to have free choice for accounting practices, information asymmetry would be magnified and financial statements are unable to be comparable with each other. This may in turn impact financial statement users' decision making.

Our findings should be interpreted with care. Different measures of client and auditor conservatism may yield different findings. Importantly, with the small proportion of conservative clients which recognized the effect of the amendment in 2018, we were unable to completely conclude that client and auditor conservatism impact reporting the effect of the amendment of the Thai Labor Protection Act in 2018. Owing to the unique institutional settings of Thailand, our findings may not be applicable to other countries. We therefore suggest that future research should use other measures of client and auditor conservatism to observe the relationship between accounting conservatism and timely loss recognition, especially in counties other than the US. Observation outside the US is of interest because

the level of accounting conservatism varies from country to country (Ball et al., 2008; Ball & Shivakumar, 2005; Chi & Wang, 2010) and there is plenty of existing evidence from the US. For Thailand, it is also of interest to study the relationship between accounting conservatism and loan loss provision after the TFAC issued the accounting practice guideline for loan loss provision in response to the effects of COVID-19 in April 2019. In addition, future research should observe the impact of audit firm's specialization on auditor conservatism in timely loss recognition.

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Appendix: Definitions of the variables

Variable	Type	Description
ReEBP	Ordinal variable	0 if a company (an auditor) ignored the effect, 1 if a company (an auditor) deferred the recognition of the effect to the later year but disclosed the effect in 2018's financial statements, and 2 if a client (an auditor) recognized the effect in 2018's income statements
LogEEBP	Continuous variable	the natural logarithm of the effect recognized/disclosed in 2018's financial statements
DiffEBP	Continuous variable	the natural logarithm of the absolute value of difference between the actual amounts of the effect recognized in 2019's financial statements and the estimated amounts of the effect disclosed in 2018's financial statements
UndEst	Dummy variable	1 for *Underestimate* group and 0 for *Overestimate* group.
CCon	Dummy variable	1 if a client exhibits their conservatism as explained in 3.1 and 0 otherwise
ACon	Dummy variable	1 if an auditor is Big 4 and 0 otherwise
AvCFO	Continuous variable	the average of cash flow from operations deflated by total assets for three years before the new Labor Protection Act
AvROA	Continuous variable	the average of return on assets for three years before the new Labor Protection Act
LEV	Continuous variable	the ratio of total debt to total assets
BM	Continuous variable	the book-to-market ratio
CEOCh	Dummy variable	1 if a company changed their CEO and 0 otherwise
LogLEMP	Continuous variable	the natural logarithm of provisions for employee benefit at the end of the year
Union	Dummy variable	1 if a company has labor union and 0 otherwise

Appendix: Definitions of the variables (Continued)

Variable	Type	Description
FCh	Dummy variable	1 if a company switched audit firm and 0 otherwise
$LogA$	Continuous variable	the natural logarithm of total assets at the beginning of the year.