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Shifting Towards International Financial Reporting Standards

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Abstract

"Financial reporting is essential for all organizations whether "profit organization" or "non-profit organization". It is considered as the language of the business through which the various stakeholders gets information relating to the financial performance and financial position of the company. The accounting reporting practices of different countries across the world vary significantly. This is due to the differences in the economic, political, and social values etc. There is a need to have uniformity in the world wide accounting reporting. International Accounting Standards Committee (IASC) and the International Organization of Securities Commission (IOSCO) are formed to promote some kind of accounting uniformity throughout the world. The accounting regulatory bodies across the world have called for a single set of high quality, understandable, and enforceable accounting and reporting standards. Due to the globalization of financial markets the need for single set of high quality and globally acceptable accounting and reporting standards is need of the hour. International financial reporting system was introduced in 2001, to provide the uniformity in accounting and reporting practices across the world. An effort has been made in this study to examine the reasons and extent of adoption of IFRS in different countries and to discuss the problems faced by different countries in the implementation of IFRS and brings out the ways through which these problems can be addressed."

Key Words: IFRS, IASB, GAAP, ICAI

INTRODUCTION

Earlier 1970 most of the companies have domestic investors but after the internationalization of the stock markets the problem of communicating the accounting information arises. Due to the rising number of associate companies which were operating abroad, a growing need for cross-border standards arises. Internationally adopted standards facilitate the cross-border comparison, which leads to better allocation of capital and minimize the cost of reporting. IFRS was developed in the year 2001 by the International Accounting Standards board (IASB) to provide a single set of high quality, understandable, and uniform accounting standards.

Accounting is the language of the business and to make the language convey the same meaning, accountants all over the world have developed certain rules, procedures and conventions generally referred as generally accepted accounting principles (GAAP) based on US GAAP. But there are certain Drawbacks of US GAAP like it was too complex, more relies on rules than principles and politically unacceptable in many countries.

To maintain uniformity in accounting principles across the world International Accounting Standard committee (IASC) was formed on 29th June, 1973 when 16 accounting bodies from 9 nations (i.e., U.S.A, Canada, U.K, Australia, France, Germany, Japan, Mexico and Netherlands) signed the agreement for development of international accounting standards. The committee's headquarter is at London. A revised agreement was signed in October, 1977. The committee prepares the draft of standard practice to be adopted in respect of the presentation of the financial information and the final draft approved known as standard published for adoption by the members of International Federation of Accountants (IFAC) in their respective countries. But international accounting standards do not have any statutory authority, so they don't impose any legal obligation on companies to adopt these standards. In 2001, the International Accounting Standard Board (IASB) took over the responsibility of setting accounting and reporting standards as a result IASB issues new standards known as International Financial Reporting Standards (IFRS). The main objective of IFRS is to bring about consistency and uniformity in financial reporting across the world. Globalization of capital markets is an irreversible process, and there are many potential benefits to be gained from mutually recognised international accounting standards. The adoption of uniform standards cut the costs of doing business across borders by reducing the need for supplementary information. They make information comparable, thereby enhancing evaluation and analysis by users of financial statements. Many countries, like European Union and Australia have adopted IFRS from 2005. The "Norwalk Agreement" in 2002 initiated the ongoing convergence of US GAAP with IFRS. Now, nearly 100 countries have either adopted or have policy of convergence with IFRS.

REVEIW OF LITERATURE:

Several studies have been conducted from time to time in the area of IFRS. A brief summary of these studies is presented below:

Debdas Rakshit and Chanchal Chatterjee in the paper "financial reporting based on fair value- An overveiw" outlines the various drawbacks of present reporting system and suggest the various measures which may increases the value of reporting.

FM Richard (1976) said that all international and national authors give their consent for the harmonization of accounting and auditing practices to make a common global platform for fair and common accounting practices.

Lingisetti Venu in the paper "shifting towards IFRS and its implications" outlines that accounting bodies across the globe called for the common set of high quality, understandable, enforceable accounting standards. According to them IFRS have all the features which can provide common standards for accounting reporting. Undoubtedly, IFRS has added greater comparability and consistency in the corporate reports across the borders. Infect various observations revealed that IFRS has brought significant amount of complexities. Thus the journey of IFRS towards a truly global financial language is entered into a crucial stage.

Horton, Joanne,George Serafeim and Ioanna Serafeimin in the journal "Does mandatory IFRS adoption improve the information environment?" states that more than 120 countries permits the use of IFRS by public limited companies. Though the adoption of IFRS the information quality increases in the capital markets and as a result firm's information environment increases by both information quality and accounting comparability.

Kamal, Yousuf and Sobhan, Abdus and Haque, Tanzina in the journal "IFRS- Advantages and challenges"- A summary of findings of some existing literature (June1, 2009), emphasis on the costs and benefits of IFRS. Principle benefit of the IFRS is that it lowered the cost of capital but there are certain challenges in proper implementation of IFRS. Thus for proper implementation of IFRS optimal harmonization is required.

OBJECTIVES:

The main objective of the paper is to focus on the adoption and application of IFRS and the problems relating thereto. The specific objectives are:

1. To find out drawbacks of different reporting practices.

2. To find out the reasons for adoption of IFRS in different countries.

3. To state the extent of application or adoption of IFRS in different countries.

4. To present some policy recommendations for adoption and implementation of IFRS for ensuring good financial reporting.

RESEARCH METHODOLOGY:

To address the emergence of IFRS in the context of the transformation of financial reporting the article adopted a pre-dominantly review approach. The study has been conducted mainly on the basis of literature survey and secondary information. Various journals and research papers, diagnostic study reports, newspaper articles and books have been surveyed in this study with respect to India, Brazil, Germany, Pakistan, South Africa, and Kenya.

DRAWBACKS OF DIFFERENT ACCOUNTING REPORTING PRACTICES:

The accounting practices adopted by different countries results in the different reporting practices also. Some of the drawbacks of accounting and reporting practices are:

1. Accounting rules and tax laws are different thus the need for adjustment in the accounting practices is required to make it suitable for tax laws, which creates complexities in accounting reporting.

2. Another problem related to accounting practices is the difference between the disclosures norms adopted by different countries which makes the comparison difficult.

3. Difference in the accounting policies also creates hurdle in making the accounting reporting effective. Because different policies depict the different results under the same situation which may mislead the investors.

4. Due to the difference in the accounting practices adopted by domestics firms and the accounting practices followed by foreign competitors, it become difficult to compare the domestic performance with the international performance.

DIFFERENCE BETWEEN GAAP ADOPTED BY DIFFERENT COUNTRIES AND IFRS:

GAAP is generally accepted accounting principles which were adopted by the countries for the preparation of financial statements. But there are certain drawbacks of the GAAP. The main differences between GAAP and IFRS are as follows:

1. Under the GAAP system LIFO method is allowed for the valuation of inventories, but under IFRS LIFO method is prohibited.

2. Revaluation of assets under the GAAP is not allowed, but revaluation of assets is regular practice under IFRS.

3. Comparative statements are not allowed under GAAP but under IFRS comparative statements of at least one year prior of the reporting year are required.

4. Any purchases in process research are valued and immediately expensed under GAAP, but under IFRS these may be capitalised and amortized.

REASONS OR OBJECTIVES BEHIND ADOPTION OF IFRS IN SELECTIVE COUNTRIES:

The reason for adoption of IFRS differs from country to country. A brief study of some selected countries is as follows:

In Brazil the main reason behind the adoption of IFRS is to facilitate the comparability of financial reports and to increase investor's confidence.

In case of Germany the main objective for the adoption of IFRS is to access the financial markets outside the Germany. Similarly in case of Kenya main reason behind the adoption of IFRS is to raise national financial reporting up to international practices.

In India the main reason for shifting towards IFRS is to harmonize and converging the Indian accounting standards, in order to raise the standard of financial reporting at global level.

In case of Pakistan and South Africa the main reasons for the adoption of IFRS is to raise their financial reporting requirements up to internationally recognized benchmark.

These studies reveals that the main reason for the adoption of IFRS is to increase the level of financial reporting up to the international level, in order to provide a common set of standards for the preparation and presentation of financial statements.

RESPONSIBLE BODIES FOR THE ENFORCEMENT OF IFRS IN SELECTIVE COUNTRIES:

Following are the some professional bodies established in different countries, which helps in the proper implementation of IFRS in those countries:

In Germany there is a two-tier enforcement system:

a. General Financial Reporting Enforcement Panel which examines the consolidated and non-consolidated financial statements.
b. Federal Financial Supervisory Authority is the second level of enforcement, to whom case is referred in case of any violation of rules or in case of any other problem with regards to this.

In Kenya Institute of certified public accountants and in Turkey Capital Markets Board is responsible for the enforcement of IFRS.

In India Institute of Charted Accountants of India (ICAI) is responsible for the enforcement of IFRS. It established the Financial Reporting Review Board (FRRB) for the proper enforcement of IFRS.

In Pakistan Monitoring and Enforcement Department of Securities and Exchange Commission of Pakistan is responsible for the enforcement of IFRS.

In South Africa the South African Institute of Charted Accountants and Joannes burg Stock Exchange are responsible for the enforcement of IFRS.

This study shows that the IFRS is growing and emerging concept across the world. Different countries have established different responsible bodies for the proper adoption and enforcement of IFRS.

RELEVANCE OF IFRS IN GLOBAL ECONOMY

1. *Uniform business practices*: - IFRS provides common platform for the preparation of financial statements across the globe. It facilitates comparison of domestic firms with foreign competitors and also eliminates the problem of different results shown under different accounting practices. IFRS brings uniformity and consistency in the accounting practices.

2. *Increased transparency*: - IFRS provides the common base for the preparation and presentation of financial statements throughout the world. It enables the domestic firms to check the performance of its subsidiary or branch operated in other country. Earlier it was not possible because of difference in standards adopted in both the countries. Thus IFRS brings transparency in the accounting and reporting system.

3. *Increased cross-border investment*: - With the adoption of globally accepted accounting principles it becomes easier for the investors to evaluate the performance of the domestic firms with international firms and increases the confidence of the investors. Thus the adoption of globally accepted accounting principles facilitates cross border investment

4. *Problem of wrong interpretation of financial statements resolved*: - With the adoption of IFRS the problem of wrong interpretation of financial statements is resolved because it provides the common base for the preparation of financial statements across the world. It brings uniformity in the accounting practices, now financial statements of different companies operated in different countries almost gives same result.

5. *Bring down the cost and time involved in reporting system*: - Prior to the adoption of IFRS, different standards were adopted by different countries. Thus the companies operated at

international level prepare their financial statements in accordance with both the standards followed in the country where it operate and in the country where it has to report, due to difference in accounting standards adopted by different countries. But with the adoption of IFRS a common set of standards prevails across the world, which results into savings in the cost and time by elimination of duplication of work.

EXTENT OF APPLICATION AND ADOPTION OF IFRS IN SELECTIVE COUNTRIES

Extent of adoption of IFRS varies from country to country like:

In Brazil only listed companies and financial institutions are required to follow IFRS. In case of Kenya all companies whether listed or unlisted are required to adopt IFRS for consolidated and non-consolidated financial statements.

In Germany companies are required to follow IFRS for preparation of consolidated financial statements and are prohibited for the use of IFRS for the preparation of separate financial statements.

In India three-tier system is adopted for the adoption of IFRS which is as under:

Level-1 Large scale companies required to adopt IFRS.

Level-2 Small and medium enterprises required to adopt IFRS with certain simplifications.

Level-3 Small and medium enterprises required to adopt IFRS with certain exceptions.

In Pakistan, Africa, and Turkey IFRS is applicable only to listed companies whose shares are widely held and separate guidelines are issued for small and medium size enterprises for reporting.

PRACTICAL CHALLENGES OR PROBLEMS FACED BY SELECTIVE COUNTRIES IN IMPLEMENTATION OF IFRS:

Following are the certain problems which are faced by different countries in the proper implementation of IFRS:

1. *Difference in existing country laws and IFRS*: - Due to the difference between the laws applicable in different countries it becomes difficult to implement the IFRS. These laws have different requirements regarding the disclosures and formats for the presentation of financial statements. Different laws prevail in different countries are as follows:

India - Companies Act, 2013.

Pakistan - Companies Ordinance, 1984.

South Africa - Companies Act, 1973.

Turkey - Commercial Code, 1957.

2. *Difficulty in enforcement of IFRS*: - Different countries have set up different responsible bodies for the adoption and implementation of IFRS. It also creates problem in the proper implementation of IFRS. For example in Germany two-tier system is adopted for the implementation of IFRS and in India three-tier system is adopted for the implementation of IFRS. Due to these differences it becomes difficult to implement the IFRS.

3. *Time gap between adoption and implementation of IFRS*: - Usually there is a long time gap between the decision taken for the adoption of IFRS and its actual implementation of IFRS is too large. This is another barrier in the proper implementation of IFRS. For example in case of Kenya decision for implementation of IFRS was taken in 1998 but actually implemented in 1999.

4. *Technical challenges in the implementation of IFRS*: - This is the principle difficulty faced in the proper implementation of IFRS. Practical implementation of IFRS requires adequate technical capacity among preparers, auditors, regulatory authorities, and users of financial statements. But due to the lack of sufficient number of accountants and auditors who are technically qualified it becomes difficult to implement IFRS properly.

5. *Difficulty in coping with rapid changes in IFRS*: - More frequent changes in IFRS creates problem for the quick adoption and implementation of IFRS in different countries. It is because of the non availability of sufficient structure for the proper implementation of IFRS.

RECOMMENDATIONS OR SUGGESTIONS FOR THE PROPER IMPLEMENTATION OF IFRS

On the basis of study of different problems faced in different countries in the implementation of IFRS, some measures to overcome these problems are recommended as under:

1. Preparers, users, regulators, professional bodies should be involved in the planning as well as in the implementation stage of IFRS.
2. Define the scope and applicability of IFRS in respect of type of entity to which it is applicable, because IFRS cannot be implemented in full at a time. For example some exceptions must be given to small and medium size enterprises regarding the adoption of IFRS.
3. The government should introduce an awareness program for the proper implementation of IFRS and for improving the degree of compliance with accounting requirements by specified business enterprises.

2. To encourage the companies for the adoption of IFRS, significant incentives monetary or non- monetary must be given for reporting regularly complying IFRS and other necessary requirements.
3. Special considerations must be given to the countries which are under the trend of inflation.
4. The professional bodies responsible for the adoption and implementation of IFRS must conduct various IFRS training programmes from time to time as there is a gap between the trained professionals required and trained professionals available.

5. Full support and strong commitment is necessary on the part of different professional accountancy bodies for the quick implementation of IFRS.
6. In order to upgrade the accounting education and to ensure a minimum quality standard, it must be part of the curriculum in the universities and colleges.

CONCLUSION:

An effective control and enforcement mechanism is one of the essential requirement for the implementation of IFRS. Each interested party, like directors, auditors, accountants, and various professional bodies have to come together and work as a team for the proper implementation of IFRS. To make the present reporting system in accordance with IFRS, the lawmakers have to make necessary changes in existing laws i.e. Companies Act, tax laws etc. Various professional bodies have taken the necessary step in regard with implementation of IFRS. But these steps are not enough to ensure the full compliance with IFRS. Only enforcement mechanism is not enough but self regulation, awareness and proper training is necessary for the smooth adoption of IFRS.

SCOPE FOR FUTURE RESEARCH:

This study is based on the analyses of secondary information and provides the fundamental base for the future research. This is a comprehensive study of different countries regarding the adoption and implementation process of IFRS. It helps in understanding the reasons, extent of adoption and problems faced in the implementation of IFRS in different countries. On the basis of the information contained in this article further research can also be done in the area of IFRS and information contained in this article may be helpful for various researchers.

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