
Benefits and challenges regarding the IFRS implementation: lessons from the emerging economies

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Abstract

The interest shown by the users of financial statements for the convergence or harmonization process in terms of financial reporting has increased in the last decades, not only in the case of the developed countries, but also for the emerging economies. Although analysed in publications in terms of financial reporting less than the developed countries, the emerging countries have become a point of interest, being identified by the international investors as potential areas for extending their businesses. The purpose of this article is to identify the global context regarding the adoption of the International Financial Reporting Standards (IFRS) or the alignment of the national standards with the IFRS and to establish some benefits and obstacles met during this process. The analysis focuses on several emerging countries with experience in IFRS implementation and it also brings forward the case of Romania, which is treated separately.

This paper represents a contribution to the literature in terms of IFRS implementation within the emerging countries, which is still limited, and it focuses on the case of Romania, recently affected by changes of the local regulations for the financial reporting. There are a small number of studies regarding the situation in Romania after the entering into force of the new financial reporting regulations.

The research methodology was based on literature review in order to acquire and to centralize some conclusions regarding the experience of IFRS application in several emerging countries. The focus on the case of Romania consists of collecting information using questionnaire, followed by centralizing and interpreting the results in order to outline some conclusions.

Keywords: IFRS, emerging economies, benefits, obstacles, Romania.

JEL Classification: M41, M48

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Introduction

Since the extension of the globalization process, the interest shown for the harmonization of the financial reporting process by introducing a unitary set of international financial reporting standards at global level has also increased. According to AICPA (2014) and Masoud (2014), the IFRS has become the most popular set of financial reporting standards used globally, the number of the countries which already adopted IFRS at different stages being of 120.

The speeding up of this process of convergence or harmonization of the local regulations with the IFRS was also generated by factors such as the fact that the accounting information disclosed in accordance with the local standards does not always fulfil the informational needs of the market players (Saidi, 2013), or the idea that the existing differences between the local accounting systems represent significant obstacles in the process of foreign investors' understanding of the accounting information disclosed in the financial statements of other countries (Căruntu and Lăpăduși, 2011). The article represents a preliminary stage of a study scoped for analysing the impact of the IFRS implementation in the emerging economies, with focus on the case of Romania.

1. Research methodology

The research methodology used for this article was the literature review which mainly focuses on the analysis of the benefits and obstacles met in the process of adoption of IFRS regulations or of harmonization or convergence with these international standards within the emerging economies, in order to highlight some results generated from the experience of these countries. Among the countries analysed in the studies taken into consideration, there are included: the United Arab Emirates, Turkey, China, Nigeria, Ukraine, Poland, Libya, Malaysia etc.

In order to highlight some features and some expected aspects regarding the Romanian experience in terms of IFRS implementation, the opinion of the financial professionals was reviewed. Thus, for this preliminary stage, a questionnaire was developed, based on which responses were collected from a sample of 17 professionals with higher education, with more than 3 years of professional experience in the financial area

and with relevant knowledge and experience regarding the International Financial Reporting Standards.

2. The global perspective regarding the IFRS application in emerging economies

Although still limited, the research in terms of IFRS application within the emerging countries has been recently extended together with the increase in the interest shown by the international investors for the opportunities identified in this type of economies. International sources present several opinions regarding the use of these standards within the emerging economies. As Kosonboov (2014) quoted by Alsaqqa and Sawan (2013) presents, certain needs of the developing economies may have not been considered by IASB. An example would be the use of the fair value concept which in the case of emerging economies can become difficult to establish without the existence of an active market for the corresponding elements (Alsaqqa and Sawan, 2013). Also, according to Perera (1989) quoted by the same source, the information obtained by implementing the accounting standards specific to the developed economies will not be useful within the decisional process of the emerging economies (Alsaqqa and Sawan, 2013).

Recent research is generally more focused on the positive impact generated by the application of IFRS, even within the emerging countries. Favourable reactions to the application of IFRS are encountered among the companies which were affected by the information asymmetry problem during the period before the IFRS adoption (Armstrong et al., 2008).

It is also expected that the implementation of the IFRS will provide a higher level of quality to the financial information, as opposed to the local accounting standards. In most cases, the implementation of the IFRS results in an increase in the level of comparability between the financial statements used by the investors, especially if it is considered the fact that, currently, investors are interested in the global investment opportunities and a lot of companies are extending their businesses beyond national borders (Odia and Ogiedu, 2013).

However, the number of studies published in the field of the financial reporting within the emerging economies

remains quite limited, especially when compared with the case of the developed economies. In order to successfully implement the IFRS within the emerging economies it is essential that the potential challenges and problems that may occur during and after this process be considered, and to assure that they are mitigated as much as possible.

3. The experience of the emerging countries in IFRS application: benefits and obstacles

For the emerging countries which are in the process of transition from the financial reporting local regulations to the IFRS it is essential to identify and analyse the potential benefits and obstacles which should be expected, in order to reduce, as much as possible, the necessary efforts to avoid the obstacles and to obtain the highest impact from the positive aspects. The experience of the emerging countries already being in the process of IFRS implementation may become an example for other countries which started or are going to start this transition process to the IFRS.

Among the benefits identified in several studies performed for the case of the emerging economies, there are:

- the increase in the level of comparability between the financial statements;
- the increase of the level of quality in terms of financial reporting;
- the improvement of the transparency level;
- benefits from using the fair value concept;
- obtaining a higher level of flexibility.

According to a research performed by Sidik and Rahim (2012), in the case of Malaysia it was noticed that most of the participants in that study consider that the local financial statements aligned with the IFRS lead to the *increase in the level of comparability* between the financial statements of several companies. A result of the IFRS implementation was also the increase in the *level of confidence* of the investors in the financial information disclosed (Sidik and Rahim, 2012). A similar impact was identified in the case of Nigeria (Ikpefan and Akande, 2012) and of Poland (Grabinski, Kedzior and Krasodomska, 2014). Based on a study performed by

Alsaqqa and Sawan (2013) in the United Arab Emirates, it was identified as an advantage the *improvement of the quality* of the financial reporting, by increasing the reliability provided by the financial reporting and by increasing the level of understandability and relevance of the financial information, resulting from the implementation of the international standards (Alsaqqa and Sawan, 2013). Relevant for this benefit is also the case of China, where among the A-share companies it was noticed the quality improvement of the financial reporting after substantial convergence with the IFRSs (Nnadi, n.d.). Similar benefits were also identified in the studies performed on the Mexican regulations adapted to the IFRSs (Palacios-Manzano and Martinez-Conesa, 2014) and also in the case of Turkey (Balsari and Varan, 2014). According to an analysis performed on the listed entities in Poland, the fact that the IFRS implementation led to the increase in the level of *reliability, usefulness* and *transparency* in the financial reporting process was noticed (Grabinski, Kedzior and Krasodomska, 2014). Similar benefits were also identified in the case of the United Arab Emirates (Alsaqqa and Sawan, 2013) and in the case of Malaysia (Sidik and Rahim, 2012). The *fair value concept* is seen as a benefit in the case of India, based on the idea that this can help in presenting the assets in the financial statements of the Indian companies at their real value (Jain, 2011). Similar implications were identified in the case of the United Arab Emirates (Alsaqqa and Sawan, 2013). Regarding the countries that prepare their financial statements in accordance with the U.S. GAAP or in accordance with the local rules-based standards (as opposed to principles-based standards), the transition to IFRSs may lead to *flexibility* in approaching and disclosing the financial elements, considering the nature of each specific transaction and its corresponding circumstances. This advantage was also identified in the case of Ukraine (Kuzina, 2014).

However, several obstacles were also met in the process of the IFRS implementation in the emerging economies, such as the following:

- the lack of relevant specific knowledge and of practical experience;
- the need of training and consultancy services;
- difficulties encountered in using the fair value concept;
- the transition costs.

The absence of the necessary abilities to implement IFRS in the emerging countries was identified as an obstacle in the study performed by Masoud (2014). This obstacle was also noticed in the case of Libya (Zakari, 2014). The absence of the specific knowledge and of the experience regarding IFRS may lead to the need of training and consultancy services provided by the professionals in this field, of which costs may be significant, as identified in the case of Libya (Zakari, 2014) and Malaysia (Sidik and Rahim, 2012). In the absence of an active market for the corresponding elements, difficulties may be encountered in establishing the fair value, as noticed in the studies performed in the cases of the United Arab Emirates (Alsaqqa and Sawan, 2013) and of the Czech Republic (Strouhal and Deari, 2009).

4. Conceptions regarding the impact of implementing IFRS in the case of Romania

In order to analyse the case of Romania regarding the conceptions and expectations in terms of benefits and obstacles generated by the IFRS implementation, the opinion of several professionals in this area was considered. Their opinions were collected using a questionnaire distributed to a sample consisting of persons with higher education, with more than 3 years of professional experience in the financial area and with relevant knowledge and skills in terms of IFRSs. The results are based on the responses collected from 17 professionals.

In order to establish a starting point for the respondents' opinions about the implications of IFRS implementation, the questionnaires also included a section that collected information related to the perceptions about the categories of users of the financial statements.

According to the results of the study, it is considered that the most important users of the financial statements on the Romanian market are the creditors (which obtained a weight of 26% of the total categories of users mentioned in the responses), followed by the local investors (23%), the Government and the fiscal authorities (21%) and the international investors (19%), the other categories mentioned obtaining weights lower than 3%.

The most popular category of users included in the responses regarding the users of the financial statements whose informational needs are best satisfied by the financial statements prepared in accordance with the IFRS was represented by the international investors (obtaining a weight of 52% of the total categories of users mentioned in the responses), 33% of the users mentioned being the creditors (banks and other similar users), while weights of below 6% were obtained by the local investors, the State's institutions and the competitors.

Also, the results of the questionnaires' analysis showed that the financial statements prepared in accordance with the local regulations best satisfy the informational needs of the Government and of the fiscal authorities (42% of the financial statements users mentioned in the responses), followed by the local investors (27%), creditors (21%), while the other categories of the users obtained weights lower than 6%.

A weight of 52.9% of the sample considers that the financial statements are easier to be prepared in accordance with the local regulations, 35.5% believe that the level of effort allocated to preparing the financial statements is similar in the case of the local regulations and the one of IFRS, while according to 11.8% of the responses, it is easier to prepare the financial statements as per IFRS than by using the local regulations in terms of financial reporting.

Regarding the auditing of the financial statements, 41.2% of the respondents considers that the level of effort involved by the auditing of the financial statements is similar in the case of financial statements prepared in accordance with the local financial reporting regulations and in the case of financial statements prepared in accordance with the IFRS. A weight of 35.3% of the sample considers that the financial statements prepared according to the local regulations are easier to audit than the ones prepared in accordance with the IFRS, while a weight of 23.5% considers that the financial statements prepared in accordance with the IFRS are easier to audit than those prepared in accordance with the local regulations.

Using these questionnaires, the professionals' opinion regarding the advantages gained from the transitions of the local financial reporting standards to the IFRS was also assessed. Thus, using the weight of the presence in the responses, the following hierarchy of the advantages was built:

- higher level of comparability between the financial statements of several international companies (29%);
- higher level of the transparency in disclosures (20%);
- flexibility generated by using a framework based on principles (16%);
- higher level of the quality of the accounting information (14%);
- benefits from using the fair value concept (13%);
- cost savings related to the reporting process (where the conformity with several frameworks is required) (9%).

Also, the professionals' opinion regarding the disadvantages incurred in this transition from the local regulations to the IFRS was assessed. They are presented in the following hierarchy, starting from the highest weight in responses:

- the lack of knowledge and experience among accounting professionals regarding IFRS application (27%);
- difficulties encountered in understanding the IFRS by the accounting professionals or by the accounting information users (20%);
- challenges in applying the fair value concept (16%);
- significant costs with consultancy services (14%);
- the update of the accounting information systems (12%);
- significant costs of training (10%).

5. Conclusions

The recent international research focuses on highlighting the favourable impact of IFRS implementation in terms of financial reporting. The experience of the emerging countries which are in the process of transition from the local regulations to the IFRS or which have already completed this process can be used as a lesson for the emerging countries which will deal with this stage in the evolution of the financial reporting. Knowing the benefits and the obstacles met in the transition process is very important for an emerging country, so that it can avoid or mitigate the impact of obstacles as much as possible and get the maximum of benefits that can be obtained from the process.

In the case of Romania, a preliminary analysis shows that the majority of respondents considers that the financial statements prepared in accordance with the IFRS best satisfy the informational needs of the international investors. On the other hand, the financial statements prepared in accordance with the local financial reporting regulations best satisfy the informational needs of the Government and of other fiscal authorities. Also, the financial statements are easier to prepare using the local regulations. The level of effort involved in auditing the financial statements is similar in the case of auditing the financial statements prepared in accordance with the local regulations than it is in the case of auditing the financial statements prepared in accordance with the IFRS.

Regarding the transition from the local financial reporting regulations to the IFRS, in the case of Romania, the most popular advantage mentioned by the respondents is the one related to the increased level of comparability between the financial statements of different international companies, while the most popular disadvantage mentioned is the one related to the absence of the knowledge and professional accountants' experience in using the IFRS.

Although the latest changes of the Romanian regulations regarding the financial statements led to the alignment of some of the aspects with the ones as per IFRS for certain types of entities, significant efforts are still needed in order to achieve a higher level of convergence or harmonization with these international standards. This fact is supported by the idea that it is likely that the IFRS implementation process in the case of Romania is the most complex process the specialists have to deal with since the beginning of the accounting reforms in 1990 (L. Feleagă and N. Feleagă, 2006).

Through this article, there were outlined some general ideas regarding the current context in terms of convergence or alignment with the IFRS in the emerging economies and especially in the case of Romania. Future research will include the focus on the case of Romania and on the impact of implementing the International Financial Reporting Standards for the preparation of financial statements of Romanian companies.

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