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Standardization and Harmonization of Financial Statements: A Two-Format Model for International Financial Reporting Standards (IFRS)

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ABSTRACT

This study on standardization and harmonization of financial statements uses a two-format model for International Financial Reporting Standards (IFRS). The aim is to review accounting standardization and harmonization especially as they affect the reporting of businesses for international stakeholders and the need to ensure the culture and traditions of people across national borders. It is also to examine the challenges of implementing international financial reporting standards (IFRS) as they affect the customs and traditions of countries inherent in the financial reporting culture of such countries and the need to address these challenges. In response to the challenges of globalization and a need to simplify international businesses and trade across national boundaries, this study advocates a two-format model for the International Financial Reporting Standards (IFRS) for financial statements.

Keywords: *Accounting Standards, Harmonisation, Customs and Traditions*

INTRODUCTION

In accounting, there is a need to prescribe and maintain standards for reporting financial statements. The Financial Reporting Council of Nigeria (FRCN), formerly the Nigeria Accounting Standard Board (NASB), is charged with formulating accounting standards and enforcing implementation in Nigeria (Ama, 2015). Standards ensure that reporting entities disclose more accounting information than they want and consistently prepare and present financial statements. Standards provide the framework and guidelines through which accounting information is prepared and presented to the users to permit informed judgment.

Historically, countries around the world have had their national accounting standards. These countries treasure their standards and wish to be known for them as a matter of pride or national sovereignty (Asein 2011). However, accounting is the ‘language of business in the transformation the world has witnessed in the advent of globalization and the falling apart of hitherto insurmountable trade barriers between nations, and corporations across countries that cannot afford to speak different languages. Association of National Accountants of Nigeria (2020) stated that International corporations and international transaction activities generally create a situation where exchanging information and sharing results among institutional stakeholders will be cumbersome and misleading, and nations operate with varied reporting standards. It, therefore, gives rise to a need for adopting a single set of accounting standards to cater for the robust waves of globalization and the problem of diversity in accounting practices across borders. According to Ama (2015), accounting standards require high-quality, transparent and comparable information for the investors, creditors, financial analysts and other users of financial statements.

Nevertheless, a wholesale application of a single set of accounting standards across national boundaries without recourse to divergent customs and traditions poses problems. The culture and traditions of a people have a significant influence on businesses. Consequent to this, the reporting of financial statements without recourse to this has dire consequences. The paper, therefore, examines issues of standardization, harmonization, and/or the two-format model to determine the way forward for financial reporting for international stakeholders.

Standardisations

Asukwo (2017) explained that without a common set of accounting and financial reporting standards, it is difficult to compare financial information prepared by different entities. In an increasingly global economy, a single set of high-quality accounting standards facilitates investment and other economic decisions across borders, increases market efficiency, and reduces the cost of raising capital (Ama 2011). According to Olamide and Temitope (2016), the purpose of Accounting Standards is to reduce or eliminate variations in accounting practice and to introduce a degree of uniformity into financial reporting. Accounting Standards usually require recognition, measurement, presentation and disclosure of transactions and other items in financial statements. The objective of this standardization process includes a faithful representation of the financial statement of an organization over time to identify trends in financial performance and financial position. Olamide and Temitope stated that in some countries, professional bodies, governments and regulators formulate financial accounting reporting standards.

According to Josiah, Okoye and Adedifan (2013), the Institute of Chartered Accountants of Nigeria (ICAN) formed the Nigeria Accounting Standards Board, which took over the responsibility previously handled by ICAN. Asukwo (2017) argued that the Nigeria Accounting Standard Board (NASB) became a government parastatal in 1992 as a component of the then Federal Ministry of Trade and Tourism. The standards are the Statements of Accounting Standards (SAS). The Nigeria Accounting Standard Board Act 2004 provided the legal framework under which NASB set Accounting Standards. A total of thirty-two (32) Standards (SAS) were issued by (NASB).

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Adoption of International Standards

Nyor (2012) stated that the International Standards were developed and published by the International Accounting Standards Board (IASB) in 2001. The standards published by IASB are known as International Financial Reporting Standards (IFRS). In 2008, the IASB issued IFRS to adopt International Financial Reporting Standards (2003). The objective of IFRS, according to Ikpefan and Akande (2012), was to ensure that an entity's first Financial Statements, which comply with International Standards, should contain high-quality information that is transparent for users and comparable for all periods presented, provides a suitable starting point for accounting under international standards and can be generated at a cost that does not exceed the benefits to users.

Josiah Okoye and Adedefan (2013) explained that an IFRS or IAS consists of several standards. A standard may be a basis for the concluding part and the considerations when the standard is devised. IASB's conceptual framework provides a detailed explanation of the information provided in the Financial Statement. Ama (2015) argued that conceptual framework standards develop from scratch. The conceptual framework provides a sound theoretical basis for accounting standards. Nevertheless, in the last few years, the international accounting standard-setting process has been able to claim some successes in achieving greater recognition and use of IFRS.

In the words of Olamide and Temitope (2016), businesses have become more global and thus lost a significant part of national identity. Nigeria's international players are reporting to the global finance market. Therefore, it justifies the need to have a global financial reporting benchmark. The challenge, however, remains in the ability to adopt unified standards across borders without violating the culture and/ or customary peculiarities among nations. For example, religion and other socio-cultural peculiarities significantly affect business and social institutions in some countries. Accounting, therefore, is never an exception. Tradition and religion shape or enforce social behaviour. It has a significant effect on how to report finances. Islamic laws influence the conduct of businesses in a manner not accommodated by international standards, especially those drawn from assumptions based on Anglo-American practice and many Western Accounting practices (Chua and Taylor 2008). A good example is in the treatment of interest from borrowed funds. Islam's prohibition of interest affects International Accounting Standards as interest computation is a significant part of issues or principles underlying Western standards. Perhaps the option will be the harmonization of national and international accounting standards.

Harmonization

According to Ama (2015), Harmonization of Accounting Standards can be defined as the continuous process of ensuring that the generally accepted accounting principles (GAAP) are formulated, aligned and updated to international best practices. The adoption rate of IFRS across borders will depend significantly on the extent of benefits each country will get vis-àvis compatibility, trialability, observability and complexity of its unique circumstance. According to Samusodza (2016), harmonization increases the compatibility of Accounting Practices and how the accounting standards at the country-to-country level should be different. Strategies for harmonization include mutual recognition, reconciliation and standardization.

Mutual recognition is achieved if entity financial statements prepared using different Accounting Principles are accepted in other countries. Reconciliation is achieved when foreign companies are allowed to use their home country's accounting standards when in a foreign country. However, foreign countries are further required to provide a reconciliation of critical accounting measures such as net profit where there are differences in principles used. Standardization is achieved when all the participants agree to use uniform standards. Harmonization enhances the usage of IFRS. Ama (2015) observed that over 100 countries are required to use IFRS. There are several changes in the process of harmonization of the US GAAP with IFRS. One advantage of harmonization is the removal of different countries' accounting standards when financial statements are prepared and presented to international stakeholders. Harmonized standards improve the compatibility of financial information from several countries. However, the issue with harmonization is being able to cater to the accounting needs of both developed and developing countries due to the availability (or lack) of resources and skills to undertake harmonization since the standards are sophisticated in developed countries compared to developing countries. Moreover, legal and cultural systems are not the same. In some countries, legislation exists that prescribes rules, especially in the application of standards. According to Deepa (2019), the obstacles to harmonization are:

a. ***Diverse Legal and Regulatory Framework:*** The laws regulating businesses differ from country to country. Some countries have laws requiring special treatment of certain items while other countries do not.

b. ***Cultural and Language Differences:*** Accounting Concepts and terminologies may not have the same interpretation among countries due barriers inherent in language translations thus, a common understanding is difficult to attain

c. ***Influence of Local Standards:*** National Accounting Standards such as generally accepted Accounting Principles (GAAPs) might be made mandatory for local companies to adopt and many of these are different from IFRS

d. ***National Interest and Sovereignty:*** Where international standards conflict with national interest or as a matter of national pride, a country may wish to be known for its standard

e. ***Political and Economic Factors:*** Countries with different economic systems may have divergent views on matters of accounting standards.

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f. ***Cost and Implementation Challenges:*** Harmonisation requires significant resources and efforts, especially in the area of updating systems, training of professionals, etc. most developing countries cannot afford this.

These obstacles and many others not mentioned here make harmonization not attainable. The need therefore arises as per other options. This is where suggestions on the two-format model becomes necessary.

The Two Format Model and the Way Forward

The ongoing debate on burning and contentious accounting issues requires a common standard and proper interpretation. If international standards are not applied uniformly due to interpretational differences, their effectiveness as a common medium of international financial reporting is questionable. Global comparison of financial statements is difficult when entities apply standards differently based on interpretation**.**

What set of standards would qualify as a single or common set of standards for worldwide application? Ama (2015) contended that while more than 100 countries have adopted IFRS as their national accounting standard, some jurisdictions in the financial world (such as the US) that have not accepted IFRS for the financial reporting of their domestic companies. Suggestions point to a two-format model. On 2nd June 2010, the IASB and the US Financial Accounting Standard Board announced a modified strategy for IFRS and US GAAP. In 2008, the Board updated a memorandum of understanding (MOU) earlier entered, and a very aggressive work plan was agreed to formalize the convergence by 2011 (Asein, 2011).

Harmonization tended towards IAS, catered primarily for a Western-articulated ideology and tradition. For international harmonization to succeed, the two-format approach becomes expedient. Hence, the International Accounting Standard Board should allow different nations the leverage to report their financial statement in a manner that complies with IAS and prepare another report based on their customs and traditions, with a schedule to reconcile the two. Undoubtedly, there seems to be a global preference for internationally acceptable accounting standards. IFRS has emerged as an inclusive financial reporting benchmark, and most countries have started using it for listed companies. The reach (coverage) of IFRS is further enhanced with the recent issuance of IFRs for SMEs (Josiah et al 2015).

CONCLUDING REMARKS

This paper examined standardization and harmonization using a two-format model for preparing and presenting financial statements within the context of international financial reporting of business entities. The influence of customs and culture has made the wholesale application of IFRS difficult. Harmonization increases the compatibility of accounting practices by setting limits on nations' accounting standards. The paper also looked at the application of standards across national borders to achieve the purpose of standardization

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without jeopardizing the cultural and traditional values of nations. The robust wave of globalization simplifies international businesses and trade across national boundaries. In response, the International Accounting Standard Board promulgated the International Financial Reporting Standards (IFRS) for financial statements. In response to the challenges of globalization and a need to simplify international businesses and trade across national boundaries, this study advocates a two-format model for the International Financial Reporting Standards (IFRS) for financial statements.

Nevertheless, if the international standard is not applied uniformly due to interpretational differences, it will significantly affect it effectiveness. Thus, global comparison of published financial statements of entities using IFRS becomes difficult. Therefore, it recommends a two-format model, especially among nations whose customs and cultural differences would effectively influence business relationships and financial reporting is made.

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