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INTERNATIONAL FINANCIAL REPORTING STANDARDS AND MICRO, SMALL AND MEDIUM ENTERPRISES

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Abstract

Nigeria adopted International Financial Reporting Standards (IFRS) on a three-year phase approach effective January 1, 2012. While the listed companies and other public interest entities adopted January 1, 2012 and January 1, 2013 respectively, those SMEs had their effective date of adoption as January 1, 2014. According to the roadmap for IFRS adoption in Nigeria, this phase of the adoption statutorily requires SMEs to issue financial statements based on the framework of IFRS for SMEs at the end of 31st December 2014. The IFRS for SMEs is a stand-alone document that is organized based on topic quite unlike the full IFRS. It does not follow the numbering of full IFRS and does not also contain references to full IFRS, except for a single reference to IAS 39 Financial Instruments: Recognition and Measurement. In adopting IFRS, various countries use different approaches based on peculiarities and exigencies. For instance European Union (EU) required listed companies to use IFRS in the preparation of consolidated financial statements. While non-listed companies in the EU are permitted in some cases to file financial statements prepared in accordance with the local GAAP applicable in their respective jurisdictions. This, however does not preclude non-listed companies from being allowed to file financial statements prepared based on IFRS. It was in line with the above practice which is prevalent in United Kingdom, Australia, Ireland, Slovenia and France that one wonders if SMEs in Nigeria can cope with the challenges of preparing financial statements using IFRS for SMEs. This paper therefore, intends to examine the challenges confronting SMEs in the adoption of IFRS for SMEs and proffer solutions that would enable effective and credible financial reporting practices by SMEs under IFRS regime.

1. Introduction

Mobilization of domestic and international investments thrives on high-quality and credible corporate reporting. The various users of financial reports need such statements for making business and economic decisions. Investors need information to help them determine whether they should buy, hold or sell shares. Shareholders are also interested in information which enables them to assess the ability of the enterprises to pay dividends. Employees are interested in information which enables them to assess the ability of the enterprises to pay remuneration, retirement benefits and provide employment opportunities. Lenders are interested in information

that enables them to determine whether their loans, and interest attaching to them, are recoverable as and when due. Governments and their agencies require information to regulate the activities of enterprises, reappraise policies and as the basis for national income and similar statistics.
Agreements in the literature supported by several empirical evidences allude to the significance of Micro, Small and Medium-sized Enterprises (MSME) to the development of any economy (see Etim 2010, Jimah 2011, Akugri, Bagah and Wulifan 2015, Onugu 2005, Udechukwu 2003. In Jimah(2011) opinion, the role of small and medium scale enterprises (SMEs) cannot be overemphasized given its relevance's in resource mobilization, utilization and overall contribution to gross domestic product (GDP) of a nation. It serves as the engine of rapid economic growth and development as it respond to the macro economic problems militating against developing nations like Nigeria. In addition, Etim (2010) reportsthat SMEs have been fully recognized by government and development experts as the main engine of economic growth and a major factor by extension in promoting the realization of the financial systems strategy 2020. Udechukwu (2003) opined that SMEs are increasingly recognized as the principal catalysts for achieving equitable and sustainable industrial diversification and dispersal and in most countries SMEs account for well over half of the total share of employment, sales and value added.Obviously, MSMEs have been identified as the bedrocks for the development of nations, asthey are responsible for generating the largest employments in several economies all over the world.

2. Definition of MSME

While writers are in agreement as to the relevance of MSME to the development of any economy, there is however no agreement on the definition of MSME as they have been defined in several forms by different writers. However, the United Nations UN and Organisation for Economic Cooperation and Development (OECD) criteria on the classification of business as MSME based on turnover, asset base and number of employees remain the platform on which the various definitions spring. Therefore, the definition of MSME becomes a jurisdictional issue which hinges on the level of economic development especially currency convertibility.

In the US, for instance, the Small Business Administration defines a small business concern as one that is "… independently owned and operated, is organized for profit, and is not dominant in its field. Depending on the industry, size standard eligibility is based on the average number of employees for the preceding twelve months or on sales volume averaged over a three-year period…" It furthers defines micro, small and medium-size enterprises as made up of enterprises which employ fewer than 500 persons for manufacturing businesses and which have an annual turnover not exceeding $7.5 million for most non-manufacturing businesses.

The European Union defines a small business as one that has fewer than 50 employees. Meanwhile, some international organisations adopted definitions of small and medium enterprises based on the tripod criteria of employees, sales and assets. For instance, the International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA) define small enterprises as those that meet two of the following three criteria:

1. Less than 50 employees
2. Less than $3 million total assets
3. Less than $ 3 million total annual sales.

In Nigeria, currently there is no clear definition of who MSME is and thus there seem to be confusion in the exact definition of MSME and this we believe have adversely affected effective regulation and harmonization of activities of this all important sector of the economy especially in developing economies like Nigeria. The Central Bank of Nigeria (CBN), the Financial Reporting Council (FRC) of Nigeria, Federal Ministry of Industry, Trade and Investment, Nigerian Association of Small and Medium Enterprises (NASME), Small and Medium Enterprises Development Agency (SMEDAN).

The Financial Reporting Council (FRC) of Nigeria adopted similar but with added criteria as with those of MIGA and IFC in defining who MSME is thus ***Small and Medium-sized Entities*** *(SMEs) refer to entities that may not have public accountability and:*

a) their debt or equity instruments are not traded in a public market;

b) they are not in the process of issuing such instruments for trading in a public market;

c) they do not hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses.

d) the amount of its annual turnover is not more than N500 million or such amount as may be fixed by the Corporate Affairs Commission,

e) its total asset value is not more than N200 million or such amount as may be fixed by the Corporate Affairs Commission,

f) no Board members are an alien,

g) no members are a government or a government corporation or agency or its nominee, and

h) the directors among them hold not less than 51 percent of its equity share capital"

The CBN, in paragraph 6 of the guidelines under its, Small and Medium Enterprises Credit Guarantee Scheme (SMEGS) defines SME thus "…. for the purpose of this Scheme, a Small and Medium Scale Enterprise (SME) is an enterprise that has asset base (excluding land) of between N5million –N500 million and labour force of between 11 and 300". The National Council of Industry in 2001 gave asset base limit (excluding land) as N200m while employment limit was given as 300 employees.

Etuk, et al (2014) argued that that the above classification is quantitative and that using quantitative indices alone to define MSME have proven unsatisfactory in many respects. They posited that "… such indices are characterised by periodic alterations due to inflation and thus can sometimes be misleading. Noteworthy is the point that the CBN's definition of SME above may not accommodate many small businesses in Nigeria, which may be known as micro-enterprises. Also misleading is the fact that some enterprise may be labour intensive and so may be large in terms of number of workers employed, while on the other hand, a capital intensive firm may be large in terms of asset base but have fewer employees". For the above limitation of quantitative definitions, a qualitative definition based on pre-determined characteristics of SME is needful, arguedEtuk, et al (2014).

The lack of agreement in the definition of MSME especially by government agencies superintending the activities of MSME in Nigeria is very evident from the differing definitions given by the Financial Reporting Council of Nigeria in its Report of the Committee on the Adoption of International Financial Reporting Standards in Nigeria issued 2010 and CBN's on guidelines for N200 billion credit guarantee scheme also issued in 2010. Unfortunately there seem to be no concerted efforts by these government agencies to come up with a unified definition.

3. USEFULNESS OF ACCOUNTING INFORMATION SYSTEM

In the view of Salehi, Rostami and Mogadam (2010), the main objective of an accounting information system (AIS) is the collection and recording of data and information regarding events that have an economic impact upon organisations and the maintenance, processing and communication of information to internal and external stakeholders.
An entity's financial reporting is a vehicle to convey to interested and relevant stakeholders various financial information that are required to evaluate the entity's financial performance. It is a mechanism necessary for proper management of the entity's resources towards the realization of its objectives. The significance of financial reporting standards cannot be over-emphasised. Financial statements are also important to a company's managers because by publishing financial statements, management can communicate with interested outside parties about its accomplishment running the company. Different financial statements focus on different areas of financial performances.

In buttressing the relevance of accounting information to an entity irrespective of size, Ezjiofor, Ezenyirimba and Olise (2014) posit that "an accounting system records, retains and reproduces financial information relating to financial transaction flows and financial position". The place of sound accounting and internal control systems in any business, irrespective of its scale, cannot be overemphasized argued Ezejiofor, Ezenyirimba and Olise (2014).

The various users of financial reports need such statements for making business and economic decisions. Investors need information to help them determine whether they should buy, hold or sell shares. Shareholders are also interested in information which enables them to assess the ability of the enterprises to pay dividends. Employees are interested in information which enables them to assess the ability of the enterprises to pay remuneration, retirement benefits and provide employment opportunities. Lenders are interested in information that enables them to determine whether their loans, and interest attaching to them, are recoverable as and when due. Governments and their agencies require information to regulate the activities of enterprises, reappraise policies and as the basis for national income and similar statistics.
From the above discussion, it becomes obvious that the provision of information for decision making and regular situation appraisal is the over-riding objective of financial reporting.
Though most of us know nothing about accounting experience wise, it is virtually impossible to manage a business effectively without being able to understand financial information. Therefore, one can state categorically that financial information is the heart of business management**.**Accounting reports and financial statements are as revealing of the HEALTH OF A BUSINESS as pulse rate and blood pressure reports are in revealing the health of a person (http://faculty.valenciacollege.edu/srusso/ch18bus.htm) accessed on September 8, 2015.
Mintah et al (2014) posit that "the keeping of proper records and writing of financial statements have enormous benefits for Small Scale Enterprises. They serve as an important management tool

for every business because they provide an accurate reflection of financial performance of the business. They also serve as a means to monitor performance and measure the accuracy of income and expenses".

4. IFRS FOR SMEs

Tracing the history of IFRS for SMEs, Werner (2012) recounted how AICPA's Committee on Generally Accepted Accounting Principles (GAAP) for Smaller and/or Closely Held Businesses issued a report and achieved a breakthrough as a result of its work. FASB abolished the requirement for mandatory disclosure of earnings per share data and business segment information for privately held companies. Werner (2012).

In the views of Josiah, Okoye and Adeniran (2012) "the concepts of accounting have resulted in the evolution of a variety of practices; consequently, the lack of uniformity has made it difficult for users of financial reports to compare the results of different companies". Therefore, Glautier and Underdown (2001) argued that theneed for the imposition of standards arose because of the lack of uniformity, existing as to the manner in which periodic profit was measured and the financial position of the enterprise represented. It is in the quest uniformity and comparability in financial reporting that efforts to have a single set of high quality global accounting standards began in earnest in 1973. The journey of IFRS can be said to have begun with an agreement by professional accountancy bodies of major markets (United Kingdom and Ireland, United States, Australia, Canada, France, Germany,Japan, The Netherlands and (Mexico) to develop a set of accounting principles across the globe. This led to the formation of the international Accounting Standards Committee (IASC) in 1973.

4.1 The Norwalk agreement

In September 2002, the FASB and the IASB met jointly and agreed to work together to improve and converge US GAAP and IFRS. That partnership is described in the "The Norwalk Agreement" issued after that joint meeting. The Norwalk Agreement set out the shared goal of developing compatible, high-quality accounting standards that could be used for both domestic and cross-border financial reporting. It also established broad tactics to achieve their goal: develop standards jointly, eliminate narrow differences whenever possible, and, once converged, stay converged (Norwalk Agreement).

In July 2003, the IASB commenced deliberations on a project, carried over from the agenda of the IASC, to produce a document on accounting standards for small and medium sized entities (SME). While in July 2009, the IASB issued IFRS for SMEs, which set out a stand- alone set of principles and disclosures for SMEs.

IFRS for SMEs is a condensed form of the full IFRS as the 2,500 pages of the full IFRS were vastly summarized and simplified to 230 pages in the IFRS for SMEs. Thus, IFRS for SMEs have, in most cases, different disclosure requirements. Currently, Seventy-three of the 140 jurisdictions whose profiles are posted require or permit the *IFRS for SMEs*. It is also currentlyunder consideration in a further 14 jurisdictions. In requiring or permitting the *IFRS for SMEs*, 64 of the 73 jurisdictions made no modifications at all to its requirements.

The 73 jurisdictions that require or permit the *IFRS for SMEs* are:
Anguilla, Antigua and Barbuda, Argentina, Armenia, Azerbaijan, Bahamas, Bahrain, Bangladesh, Barbados, Belize, Bhutan, Bosnia and Herzegovina, Botswana, Brazil, Cambodia, Chile, Colombia, Costa Rica, Dominica, Dominican Republic, Ecuador, El Salvador, Fiji, Georgia, Ghana, Grenada, Guatemala, Guyana, Honduras, Hong Kong, Iraq, Ireland, Israel, Jamaica, Jordan, Kenya, Kosovo, Lesotho, Macedonia, Maldives, Mauritius, Montserrat, Myanmar, Nicaragua, Nigeria, Palestine, Panama, Peru, Philippines, Rwanda, Saint Lucia, Saudi Arabia, Serbia, Sierra Leone, Singapore, South Africa, Sri Lanka, St Kitts and Nevis, St Vincent and the Grenadines, Suriname, Swaziland, Switzerland, Tanzania, Trinidad & Tobago, Turkey, Uganda, United Arab Emirates, United Kingdom, Uruguay, Venezuela, Yemen, Zambia, and Zimbabwe.

For the 73 jurisdictions that require or permit the *IFRS for SMEs*:

- Five jurisdictions require the *IFRS for SMEs* for all SMEs that are not required to use full IFRS;
- Fifty jurisdictions give an SME a choice to use full IFRS instead of the *IFRS for SMEs*;
- Seventeen jurisdictions give an SME a choice to use either full IFRS or local GAAP instead of the *IFRS for SMEs*; and
- One jurisdiction requires an SME to use local GAAP if it does not choose the *IFRS for SMEs*.http://www.ifrs.org/Use-around-the-world/Pages/Analysis-of-SME-profiles.aspx accessed September 10, 2015

4.2 CHALLENGES OF ADOPTION OF IFRS FOR SMEs IN NIGERIA

Prior to the adoption of IFRS in Nigeria, section 335 of the Companies and Allied Matters Act (CAMA) 1991 required that "the financial statements of a company prepared under section 334 of this Decree, shall comply with the requirements of Schedule2 to this Decree (as far as applicable) with respect to their form and content, and with the accounting standards laid down in the Statements of Accounting Standards issued from time to time by the Nigerian Accounting Standards Board…" This meant that all companies SMEs inclusive were using same accounting standards except to the extent of exclusion as contained in subsection 3 of Section 334 of CAMA 1990.

Ordinarily, with the simplification and reduction in disclosures from 2,500 pages to 230 pages, it will therefore be expected that the SMEs would find the adoption easy. However, one is yet to see if this will be an advantage considering the usual problem of lack of credible financial reporting system in these SMEs.

IFRS adoption has broad impacts on SMEs especially in the areas of data and systems, processes and control and people and performance. Though IFRS for SMEs have been greatly simplified most of SMEs lack the ability to cope with IFRS – both in their ability to collect data and the scope of internal controls over the data. New and modified processes and controls over data, transactions and reporting need to be designed, tested and implemented. While Knowledge transfer - developing and retaining IFRS competencies is virtually non -existent. The SMEs rarely have the financial muscle to acquire the necessary personnel with the requisite skills or even invest in the developing and retraining the existing personnel. The IFRS skills are at the early stage of being developed in Nigeria and are very scarce and highly competitive. It requires considerable length of time to get the required personnel.

In Nigeria, the greatest challenge facing small and medium scale enterprises is access to finance. SMEs as the engine of the economy have the full potentials to turn the economy around for the better, but their greatest challenge still remains underfinance.
With the introduction of IFRS, SMEs in Nigeria are mandated to adopt the new reporting standard from January 2014. The awareness, acceptance and implementation of the new IFRS guidelines for SMEs are challenges for many African countries (Fortuin, 2011). Many businesses still do not understand what options are available and how IFRS for SMEs interplay to their benefit (Fortuin, 2011). This is an indication of the lack of awareness of the benefits accrued through the use of IFRS for SMEs which may in turn inhibit SMEs from adopting them. The results of the survey by Deloitte in 2009 revealed that 43% of SME respondents were not aware of the IASB's standard IFRS for SMEs.
Poor financial management and book-keeping are two major barriers confronting SMEs when it comes to accessing funds from financial institutions and government agencies. A study conducted by Gono (2013) revealed that most SMEs fail due to poor financial management and reporting. So it is important for SMEs to follow the current trend of financial reporting and enjoy the full benefits that are associated.
The implementation of IFRSs will also require regulatory enforcement by relevant regulatory bodies. Cains (2000) argued that compliance and enforcement have been problematic for full IFRS.Many writers have alluded to the fact that compliance or the timelinessof compliance for SMEs may be traditionally an even greater problem in somemember states (see, e.g. Bollen, 1996, for the Netherlands; Mandler, 2003a, forGermany) and given differences in the statutory audit requirement for SMEsand effectiveness thereof, compliance, consistent application and enforcementare likely to represent even greater difficulties for SME standards.

CONCLUSION

While the adoption of IFRS for SMEs have advantages, such as comparability, reduced costs and improved management, ,we are however concerned that enlightenment on the processes of adoption is nonexistence and generalconcern of lack of enough skills to execute the adoption. We are further concerned by lack of effective regulatory mechanism of enforcing the adoption. This, we believe, may make the realization of the comparability objective a mirage.
We therefore suggest a collaborative arrangement by all the relevant regulatory bodies and professional accounting bodies to ensure a smooth and seamless transition to IFRS for SMEs. A seminar to brainstorm on the challenges and solutions to the adoption of IFRS for SMEs is inevitable. Such exercise should be all involving and presentations/resolutions published and widely circulated.
Nigeria is irrevocably committed to the adoption of IFRS for SMEs and can only strive to make it work effectively.

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