

THE IFRS STANDARD FOR SMALL AND MEDIUM-SIZED ENTITIES –  
ANOTHER CHALLENGE FOR THE ROMANIAN ACCOUNTING?

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**Abstract**

*In the early 2000s, the accounting has been connected to the international realities. From that moment on, we have witnessed an extraordinary dynamic of the Romanian accounting, evidenced by the many changes that have occurred in the accounting rules. Internationally, the dynamism is also the main feature of today's accounting. We witness almost annually the reconsideration of the international accounting referential. In this context of the frequent changes that occur in the accounting area, the IASB launched the International Financial Reporting Standards for Non-Publicly Accountable Entities (formerly Small and Medium-Sized Entities), a controversial approach in the international accounting. The objectives of this paper will be followed on two levels: first, we will put forth the position of different countries on this IASB initiative and second, we will show, by the means of a positive research based on an empirical study, the attitudes of professional accountants in Romania towards the possible implementation of the IFRS for NPAEs in the Romanian accounting in the next period.*

**Key words:** IFRS for NPAEs, Romania, IAS/IFRS referential

**JEL classification:** M 41

**1. Introduction**

In the current economic context, dominated by the phenomenon of the markets globalization, the IASB shows its intention to extend the accounting referential, which is promoted to all the economic entities, even to the small and medium enterprises. The supremacy of the IFRS referential against the national GAAPs is intended. A few years ago, the IFRS referential was endorsed by the need to achieve a common accounting language, essential in this new stage from the evolution of the global economy based on the markets opening and internationalization. We realised that the implementation of the IFRS referential by the large companies listed on various capital markets of the world is not a simple process. Contrary to these findings, the IASB expects to expand the application of the IFRS referential trying to impose in the following period the IFRS for NPAEs. Is it an appropriate approach, especially today, when the world economy knows a crisis without precedent? And, furthermore,

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is this approach appropriate to the Romanian accounting? Here are two questions to which we try to find an answer in the pages of this paper.

But what does the IFRS for NPAEs stand for? The standard is a stand alone document with a number of cross references to the full IFRSs. It is based on full IFRSs but removes choices for accounting treatment, eliminates topics that are not generally relevant to NPAEs and simplifies the methods of recognition and measurement. As a result it has reduced the volume of accounting guidance by 85% when compared to the full IFRSs. It is, however, still 250 long with a further 80 pages of guidance notes.

The objective of this project is to develop an IFRS expressly designed to meet the financial reporting needs of entities that do not have public accountability and publish general purpose financial statements for external users. Examples of such external users include owners who are not involved in managing the business, existing and potential creditors, and credit rating agencies.

An entity has public accountability if:

- it files, or it is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; or
- it holds assets in a fiduciary capacity for a broad group of outsiders, such as a bank, insurance company, securities broker/dealer, pension fund, mutual fund or investment banking entity.

In the autumn of 2008, Mazars, an international, integrated and independent organisation, specialising in audit, accounting, tax and advisory services, elaborated a study about the perceptions and expectations of the European countries towards the IFRS for NPAEs. The research subjects were 1.500 small and medium sized entities from France, Germany, United Kingdom, Italy, Spain and Holland. The conclusion was that “the majority of the small and medium sized European entities sustain the adoption of a common set of accounting standards either optional or mandatory. This mainly happens in the case of the entities from Italy, Spain, France and Holland”. As about a potential adoption in the European Union, Denmark decided the planning of the legislation for the allowance, while the United Kingdom has discussed “the possibility of allowing the IFRS only for the not listed companies, while the regulations for the small enterprises are still maintained”. In the meantime, most of the Bulgarian accounting professionals “firmly sustain the adoption”: “there is no doubt that our national standards will be replaced by the IFRS for the private entities. The only question is when and not if”.

The project was also exposed to the 25.000 not listed Australian entities. In Tanzania, the regulators agreed to impose the IFRS for the private entities to all the national private entities“. In South Africa, the exposure draft for the IFRS for the private entities was entirely adopted according to the SA GAAP for all the not listed companies which don't use the full IFRSs. In a published article, the executive general manager of International Federation of Accountants from South Africa said that “most of the companies will use it. It is very welcomed. The standard in its current shape already offers a great relief to the small and medium sized companies and, when it will be published in its final form, will be even better”.

The United States also show interest for this standard. There isn't any regulation regarding the statutory audit in the United States. Due to the fact that the basis of the presentation note refers to compliance with IFRS for private entities, the auditor will be able to report accordingly to this standard. The adoption of this standard is supported by the

American Institute of Certified Public Accountants (AICPA) and other similar organisations.

In the second part of our work we have achieved a positive research, its objective being found in our attempt to determine the position of the Romanian professional accountants towards the progress of the current accounting system and the perspective of some possible changes, imposed by any implementation of the IFRS for NPAEs in our country. The conclusions of the research allow us to formulate answers to questions such as:

1. Does the professional Romanian accountant continue to show significant importance to the general chart of accounts in the accounting transactions?
2. Does the fiscal reasoning continue to dominate the economic one in the recognition of transactions process, in the accounting practice in Romania?
3. Has the harmonization of the accounting rules with IFRSs occurred before the accounting professionals were prepared for this change?
4. Should the IAS / IFRS accounting referential be extended to all economic entities in our country?
5. Is the implementation of the IFRS for NPAEs in Romania appropriate in the next period?

## **2. Convergences and divergences regarding the need of implementing the IFRS for NPAEs**

The exposure draft of the IFRS for NPAEs is a controversial subject in the international media. Even the representatives of the European Parliament have challenged the efforts to launch the IFRS for NPAEs. In the following lines there are some opinions expressed on this subject by the Committee on Legal Affairs of the European Parliament meeting on 05.10.2007 [European Parliament, 2007]:

- First of all, the fact that the IASB (the Council for the International Accounting Standards) is not put to a democratic control and is not receiving information from various sources and, because of this, the decisions taken are not reflecting the actual situation of the European companies, specially the one of small and medium sized enterprises (SMEs) is disputed among European officials;
- The increasingly pronounced theoretical dimension of the IASB projects, which are already so complex and theoretical, is criticized due to the fact that the small and medium sized enterprises can not always implement them;
- The idea of convergence of accounting is supported, but this process must be based on a prior assessment of the benefits and impact of such changes for those who prepare and use financial statements in the EU, in particular for the small and medium sized enterprises;
- It is dwelled on the reality that the IASB has not received any political mandate to develop the IFRS for NPAEs and it is underlined that the procedure for adoption by the EU applies only to the international accounting standards of the listed companies and does not envisage its application to the IFRS for NPAEs;
- The Commission has expressed its distrust that the draft exposure for the IFRS for NPAEs adequately reflects the needs of the small and medium sized enterprises and the diversity of shapes and sizes in which they operate; furthermore, the project has been developed taking into account the small and medium sized enterprises of

relatively large size (more than fifty employees) and passed over the reality that most of them are of smaller size;

- Last but not least, the committee concluded that the draft exposure for the IFRS for NPAs does not take into account the fact that the users of the financial statements of the small and medium sized enterprises are mainly private shareholders, creditors, business partners, employees and anonymous investors, as in the case of the large listed companies, and that these recipients are more interested in establishing a business relationship on the long term rather than on a short term.

### **3. The results and the conclusions of the empirical positive research regarding the possibility of the IFRS for NPAs extension**

We planned through our study to bring forward the view of the Romanian professional accountants on the possibility that, in the following period, to assist at the implementation of the IFRS for NPAs, with the desire of improving the financial reporting of these entities. To achieve this goal, we developed a positive research, using an empirical study, which highlighted the view of the professional accountants in our country, both on the current accounting system and the IFRS for NPAs.

The empirical research conducted by us is based on 33 questionnaires, completed by professional accountants, which are occupying the following functions in the economic entities where they are employed: economic manager 7, accounting officer 1, economist 16, accountant 6, financial controller 1 and analyst 1. We underline that 11 respondents are employed in accountancy entities, 3 are employed in accounting and tax advisor companies, 1 answerer is an employee of a firm performing audit services, 3 answerers are employees of companies that conduct financial-accounting analysis for the economic entities and 13 of the answerers are accountants, hired by companies that have other object of activity than services and consultancy in the accounting and financial domain.

All the answerers are employees of small and medium sized enterprises. Only 12 of them activate in economic entities with more than 50 employees and have obtained a turnover of more than 1,000,000 euros at the end of 2008. After pooling the results, we found that 63.6% of the answerers are employees of economic entities that have an average number of employees under 50 persons: 8 of them are working in companies with an average number of employees between 1-10 people, 5 answerers are employees of companies with an average number of employees between 11-20 people and 8 answerers are working in entities with an average number of employees between 21-50 people.

In the following lines, we will present our research results, obtained after pooling and interpreting the responses received in the questionnaires distributed to the 33 professional accountants.

In Romania, the normalization of accounting based on the general chart of accounts has a tradition of more than 60 years. The IAS / IFRS accounting referential brings another vision of the normalization of accounting through the financial statements. In this context, it is reasonable to ask to what extent the Romanian professional accountant is prepared to meet the challenges brought about by a possible generalized reorientation of accounting towards the IFRS referential.

Since 1949, in the Romanian accounting there was the practice of recording the economic and financial transactions starting from the compliance with an accurate set of instructions developed by the Ministry of Finance.

From the research accomplished by us, we found that in the process of accounting for economic and financial transactions the Romanian professional accountant continues to give importance to the usage instructions of the general chart of accounts elaborated by the Ministry of Finances: 57.6 % of the answerers give a great importance to these instructions, while 39.4% of the respondents consider that the compliance with these instructions in the recognition of the economic and financial events is the most important. One answerer from a total of 33 grants a limited significance to the usage instructions of the chart of accounts.

This result demonstrates very clearly that the Romanian professional accountant is not yet ready to accept the IFRS philosophy, based on respecting the principles of accounting and on the appliance of the "professional reasoning for finding the best solutions in solving the accounting problems".

The opening of the Romanian accounting towards the international realities in the early 2000's influenced to a large extent the position of the professional accountants with regard to the role of accounting. We began to understand that, when an accounting transaction is recorded, we must not focus strictly on the technical part, but bear in mind the impact which that transaction has on the information to be published in the financial statements for a wide range of users. Most of the answerers, 87.9%, consider that, when recording an economic-financial transaction, the professional accountant should give the same importance to the accounting technique and to the information which will be published in the financial statements. One answerer of the 33 respondents attaches greater importance to the issues related to the accounting technique.

For fifty years, in Romania, due to the economic and political context, the professional accountant was taught to obtain accounting information for a single user - the state. After 1990, the state still was the main user of the accounting information, its great interest being the taxes, fees and the various contributions to be calculated, paid and accounted for to consolidated state budget by economic entities. Today, the same concern of the taxpayers in their relationship with the taxation is expected to be maintained, because a generalized and maintained mentality for decades can not be quickly changed. This hypothesis is validated by our research result that 75.7% of the answerers recognize that they give great importance to the fiscal implications of the economic and financial transactions recording. We found interesting the fact that the answerers do not attribute a reduced importance to the fiscal implications that are generated by the economic events when they are recognized.

Such a position of the professional accounting related to the taxation-accounting relation shows that in the Romanian accounting it is difficult to accept the idea that accounting could be disconnected from taxation in the next period.

Moreover, only 51.5% of answerers support the IFRS philosophy in the sense that, in the next period a greater importance should be given to the economic reasoning in the detriment of the fiscal reasoning on the occasion of the economic and financial transactions recognition.

Here is something that comes and proves once again that the Romanian professional accountants are not prepared, at least for now, to make the transition from one accounting model, based on European accounting directives to another model that has its pillars in the IFRS referential.

Most of the answerers - 84.8% consider that the harmonization of the accounting regulations in Romania with the IAS / IFRS for large firms during the period 2000-2005 has been dictated purely by political decisions. Only 12.1% of the answerer see in the harmonization of the Romanian accounting regulations process with the IAS / IFRS

referential a necessity imposed by the development and the globalization of the capital markets.

The following distribution of responses was received to our question referring to shaping the application area of the IAS / IFRS referential in the Romanian accounting:

- 45.4% of the answerers consider that the IAS / IFRS referential should be applied by all the economic entities;
- 15.1% of the answerers consider that the IAS / IFRS referential should be applied only by the listed entities, both consolidated and individual;
- 15.1% of the answerers consider that the IAS / IFRS referential should be applied only to large companies and public interest entities;
- 12.1% of the respondents considered that the IAS / IFRS referential should be applied only to companies that choose to do so;
- The rest believes that of this accounting referential is useful to the entities seeking financing on the international market.

More than half of those included in the sample, that is 54.5% of the answerers, would welcome the Ministry of Finance decision to extend the IAS/IFRS referential to all the entities, considering that such an approach would ensure the credibility and the comparability of the accounting information provided to Romanian and foreign investors. On the other hand, 27.3% of the answerers support the idea that the efforts to assimilate the IAS / IFRS referential is not justified in relation to the benefits, excepting the case of the listed companies and 12.1% consider that the implementation of the IAS/IFRSs is not justified because the costs of applying them exceed the benefits obtained through the submission of the financial statements in accordance with this reference.

Through the research we have done it we intend to draw a conclusion on the position of the professional accountants in our country towards the possibility that in the next period the small and medium enterprises to be required to apply the IFRS for NPAs.

In order to justify such a position, we wanted to find out which are, according to the accounting professionals, the main benefits of implementing the IAS / IFRS referential in the Romanian accounting: 51.5% of the answerers consider that the main advantage of the application of this referential is the quality of the information presented in the financial statements, while 42.4% think that the IAS / IFRS referential has the merit of ensuring the comparability of the accounting information between different countries.

After pooling the results we found that, although the accounting professionals in our country recognize the benefits of an accounting based on the IFRS referential, they are unable to estimate the cost-benefit relationship from the perspective of its implementation in the Romanian accounting: 66.7% of the answerer consider that it is difficult to estimate such a relationship. Only 18.2% of the respondents considered that the benefits justify the costs of the implementation and 15.1% think that the benefits are lower than the implementation costs.

Moreover, 66.7% of the answerers accuse the fact that the harmonization of the Romanian accounting regulations with IAS/IFRSs has been done before the accounting professionals were prepared, which in our opinion was an important shortcoming of this process, which should have been differently considered by the Romanian regulators.

We believe that the Ministry of Finance should be concerned about this reality. Only 3 respondents from the total of 33 believe that nowadays, after 10 years from connecting the Romanian accounting to the international realities, the accounting professionals from our country are ready to apply the IAS / IFRS referential to the extent of 100%. Referring to this

subject, most of the answerers - 81.8%, believe that professional accountants in Romania are ready to apply the IAS / IFRS referential, but not 100%. 60% of them consider that the accounting professionals are ready to apply the IAS / IFRS only in a proportion of 50%.

Through the research we have done, we intended to learn how the Romanian professional accountants appreciate the IASB approach on the IFRS for NPAEs adoption. We were surprised by the results obtained in this direction, because 45.4% of the answerers don't know details about the approach initiated by the IASB. Only 30.3% of the answerers consider the IFRS for NPAEs very useful for enhancing the quality and comparability of the information published in the financial statements and 18.2% of respondents consider that the IASB draft is appropriate in the current economic context.

Presently, the accounting professionals in our country can not sustain the strong need to implement the IFRS for NPAEs in the Romanian accounting, because 57.6% of the answerers don't know yet if such an approach will demonstrate its value. On the other hand, 33.3% of the respondents considered necessary to implement the IFRS for NPAEs in the Romanian accounting. Only 9.1% of the answerers rejected this approach.

In the recent years, the accounting in our country has passed through a permanent change and, even so, the accounting reform seems far from being completed. Through our research we were able to find out the point of view of the professional accountants regarding this issue: 48.5% of the answerers consider that the frequent changes which took place in the national accounting rules in the recent years are justifiable, while 33.3% disagree with this.

Our research results clearly lead to the conclusion that, in Romania, by being connected to the IFRS referential, the accounting demonstrates its value leading to an increased reliability and comparability of the information. There is though a big drawback: the lack of a sufficient number of professional accountants that know and apply the IFRS referential. 63.6% of the answerers argue that this is the main drawback of an accounting based on the IFRS referential from the perspective of the Romanian reality and 24.2% of respondents require frequent changes and updates to IFRS referential, sometimes more than annually. The rest of the answerers identified another shortcoming of the accounting connected to IFRSs, which is an exaggerated theorization of accounting.

#### 4. Conclusions

The global standards of financial reporting that are consistently applied enhance the comparability of the financial information. The accounting differences may hide the comparisons done by the investors, creditors and other persons. Having as result the disclosure of some comparable financial information of high quality, the global standards of financial reporting improve the efficiency of the capital allocation and evaluation. Not only those who provide capital for debts or equity benefit of this result, but also those entities seeking capital, because it reduces their costs of compliance and it eliminates the uncertainties that affect the costs of the capital. The global standards also improve the consistency of the audit quality and facilitate the education and training.

It is appropriate to extend the IFRS referential to all the economic entities? The results of our research lead to the conclusion that the IASB's initiative is not welcomed by the international accounting. Among the representatives of the European Parliament there are many voices that challenge the value of this IASB approach resulted in the IFRS for NPAEs. Moreover, in the current international economic context, the entire attention is directed towards the professionals in overcoming the consequences of the crisis rather than

to measures for broadening the influence of the IASB referential. The interest for the survival of the companies is more important than the desire to improve the financial reporting at the level of the smaller sized economic entities.

Is it appropriate to implement the Standard IFRS in the accounting for NPAEs in Romania in the immediately following period? Our research results show that this approach has a big drawback: on one hand, the lack of a sufficient number of specialists able to know and successfully apply the IFRS referential. On the other hand, the international economic crisis is affecting the Romanian economy more than the Romanian officials' expected to, many SMEs are forced to close their doors in this difficult period and. Not the least, the IFRS for NPAEs is addressed to economic entities with an average number of employees of approximately 50 people, while in Romania the vast majority of SMEs operate with a reduced number of employees and are not conducting external transactions.

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