

Financial reporting environment in sri lanka

Business



The purpose of this report is to investigate the current financial reporting environment in Sri Lanka and its impact on the companies listed on the Colombo stock exchange. Hotel ASSURING PL has been chosen to study the financial reporting requirements, cultural impacts and the political influences on the Sri Lanka listed companies.

1. Financial Reporting Environment in Sri Lanka

1.1. Current financial reporting requirements for publicly listed companies in Sri Lanka.

In August 2007, two stages were adopted by Sri Lanka accounting standards co-ordinators to form the International Financial Reporting Standards (IFRS).

They transitioned from Stage I of IFRS Adoption to Stage III, due to the result of a "gap" between the international and national sets of standards in Sri Lanka. However, on 1 January 2012, the Institute of Chartered Accountants of Sri Lanka (ICAA) successfully adopted IFRS. (Standards Forum, 2008, p. 5).

According to the Colombo Stock Exchange (2014) a requirement for a listed entity is that it must "ensure that the annual report is issued to the Entity's shareholders and shall not exceed five (05) months from the close of the financial year of the Listed Entity when given to the Exchange".

Furthermore, publishing of the Audited Financial Statements must be in accordance with the Sri Lanka Accounting Standards. (Colombo Stock Exchange 2014 -Listing Rules s. 7.5) The Colombo Stock Exchange (2014) also requires an Interim Financial Statement prepared by the listed

entity. The Financial Statement must comply with the Sri Lankan Accounting Standards (SLAS) 35.

They must include: Any group and company results in the case of a Holding Company. The additional notes and ratios as set out in Appendix B to the Rules. Signatures of the two Directors.

And must state that the Financial Statements are not audited. (Colombo Stock Exchange Listing Rules s.

7. 5 para. 5) The preparation of a financial statement under FRS, requires the following AS 1. 8 considerations: A Statement of Financial Position as the end of the reporting period A Statement of Comprehensive Income Statement, involving a Income statement and a separate Statement of Comprehensive income A Statement of Change in Equity A Statement of Cash Flows FRS has recently undergone several modifications with the possibility of many more in the near future (FRS -Application around the world p. Recent modifications include: FRS 10 Consolidated Financial Statements: in regard to control, decision will be made upon whether the consolidated financial statement of a parent company should be included within an entity. FRS 11 Joint Arrangements.

FRS 12 Disclosure of Interests in Other Entities: disclosure will require other companies' form of interest. FRS 13 Fair Value Measurement: stipulate a more precise definition of fair value. FRS 7 Financial Instruments: Disclosures and comparisons once required relating information but as of 1 January 2013 it no longer does. 1. 2.

Cultural influences on financial reporting in Sri Lanka.

According to Oxford dictionary culture is defined as the ideas, customs and social behavior of a particular people or society. Culture has become an important notion that would be expected to impact on legal systems, tax systems, and the way businesses are formed and financed, (Descendant, up. 136). In recent decades it has also been used to explain international differences in accounting systems. As we move towards the international accounting harmonistic it is vital to understand the influence that environmental factors such as culture have on the financial reporting.

The complexity of culture encouraged Hofstede to analyse and create four dimensions of national cultures such as Individualism, power distance, uncertainty avoidance and masculinity.

However when countries are ranked on the basis of Hofstede's five dimensions of national cultures a number of countries can be clustered together. Keeping this in view Gray developed the following accounting values: 1. Professionalism versus statutory control 2. Uniformity versus flexibility 3. Conservatism versus optimism 4.

Secrecy versus transparency (Descendant, up. 140)

The following chart, Hofstede's ranking of Sri Lanka, will help us analyse the cultural influences on financial reporting in Sri Lanka: Figure Gray (1988) developed a number of hypotheses to relate Hofstede's four societal cultural dimensions to his accounting values. Looking at the above chart, Sri Lanka's ranking could be best described by Gray (1988, p. 11) fourth

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hypothesis,” The higher a country ranks in terms of uncertainty avoidance and power distance and the lower it ranks in terms of individualism and masculinity, then the more likely it is to rank highly in terms of secrecy’.

The above chart indicates that with high power distance and uncertainty avoidance rankings and low individualism and masculinity rankings, it is suggested that Sri Lanka will prefer not to disclose too much information to public as this could lead to conflict, competition and security problems but instead they tend to provide more information to the private entities such as banks and financing companies where they can maintain secure relationships.

1. 3. Political setting on accounting standard setting.

The political influence over standard setting can be defined as “ purposeful intervention in the standard-setting process by an economic entity with the goal of affecting the outcome of that process to increase that entity’s economic value or wealth or achieve some other self-interested purpose”, (Kipper. Et al, 2013, p.

4). As financial accounting affects the distribution of wealth within society it will be political, (Degas, 2014, p. 94). As an emerging and rapidly growing economy in South Asia, Sri Lanka’s financial system and accounting practice have been largely influenced by colonial economic policies.

The country accounting system is equipped by the Securities and Exchange Commission, the Companies Act, professional accounting and auditing

institutions which have played an important role in the implementation and the setting of accounting standards.

According to Snakelike (2011), the following events are crucial in the developing of accounting standards in Sri Lanka: Due to colonial economic policies, there has been substandard growth in the capital market until 1995.

Laptop, De-Silages and Shellfire (1999) stated that the governments in Sri Lanka continuously intervene in economic activities in order to pacify the diverse interests of a heterogeneous society. Snakelike (2011) indicates that due to the establishment of Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995, the accounting standards and Sri Lanka Auditing standards have been set up. Snakelike (2011) argued that " Unlike in the I-J, regulatory impact assessment studies have not been undertaken in Sri Lanka on a continuous basis (Institute of Policy Studies, 2005).

Therefore, the effectiveness of the regulations is discussed with the use of reports and literature available with the limitation of having difficulties in seeing a holistic view of effectiveness. " . " Political interferences affect the implementation of the regulations in the country as found by many authors. Thus, the protection of the interests of the shareholders and the other stakeholders are at stake even though the regulatory framework is in force (Warrenton, 1995; Wisecracking, Hopper and Arthritis, 2004; Rattlesnake, 2006). 2.

Description of financial and non-financial reporting, undertaken by HOTEL ASSURING PL. 2. 1 . Annual Report. Annual reports are the key accountability <https://assignbuster.com/financial-reporting-environment-in-sri-lanka/>

documents that provide information to the stakeholders about the accomplishments, performance and the financial result of the company for the financial year. The report also consists of the views for the future direction of the company.

Users of the annual reports include the public, members of parliament, the media and other agencies (reporting systems, 2012, viva).

HOTEL ASSURING PL, being listed on Colombo stock exchange, full-fills its obligation to its stakeholders by publishing its annual report each year. In their annual report they disclose certain accounting information as per the requirement of its stakeholders and in accordance to the companies Act No. 7 of 2007(hotel assuring PL, annual report 2012/2013). HOTEL ASSURING PL usually provides the following information in their annual report: General corporate information: In this section they shed light on different aspects of the hotel.

They start by describing the mission and the core values of the company, followed by a glimpse of financial performance for the financial year.

HOTEL ASSURING PL then provides information about the company's board of directors and senior management members who are vital as some of the major shareholders might be interested in knowing the performance of these members. The management has analyses and discussed the financial performance, business environment and the operations of the company.

The company discusses corporate governance which is the system by which Companies are directed and controlled by the Board in the best interest of

the Stakeholders and others. This is important information for shareholders because shareholders' role in governance is to appoint Directors and the Auditors to satisfy themselves that an appropriate governance structure is in place (hotel assuring Pl, Annual report 2012/2013). In the last part of this section the company provides annual directors and the audit committee reports.

Financial information: In this section they provide detailed total impressive income statement, statement of financial position, statement of changes in equity and cash flow statement.

They also provide notes to financial statements which provide further information about the end of year statements e. G. A full explanation of how revenue is recognized in the statements. Independent audit report is provided which the auditor ensures that the statements are made according to the Sir Lankan accounting standards, comply with the requirements of Section 151 (2) of the Companies Act, No. 7 of 2007 and are providing a true and fair view of financial position (hotel assuring, annual report 2012/2013).

2. 2. Sustainability reporting. In addition to financial reports HOTEL ASSURING PL also produces sustainability report. A sustainability report is a report produced by the company about the impacts on economy, environment and the society caused by its everyday activities.

The purpose of producing sustainability report could be explained through different accounting theories.

With the increasing global awareness of sustainability, businesses have reacted by reporting their impacts on the economy, the environment and the society, particularly under a system-orientated perspective organizations are being viewed as operating within a wider social context as “ each entity is presumed to be influenced by, and in turn to have an influence, upon the society in which it operates” (Degas, 2002, p. 292). Central to this discussion is the organizational legitimacy theory and the notion that a social contract exists between the business and the society (Charles H, 2007).

HOTEL ASSURING PL, pioneers of eco-tourism in Sir Lankan, has led the way to develop eco-tourism in Sir Lankan (hotel assuring Pl, annual reporter's/2013).

In their sustainability report they talk about the community and their struggle to establish mutually beneficial relationships with the community by minimizing any adverse impact and by contributing towards community development, therefore we could say HOTEL ASSURING PL is in state of legitimacy as it is trying to create a social contract and operate as per the expectations of the community.

They have also discussed the way they adopted the OR method; Reduce, Reuse and Recycle, which is a comprehensive environment management system for the energy and water conservation to reduce environmental impact. 2. 3. Influence of financial environments and company's stakeholder on HOTEL ASSURING PL. As HOTEL ASSURING PL is a Sir Lankan company, it has to operate within bounds and norms of the Sir Lankan society therefore the company is obliged to produce its reports as per the Sir Lankan

accounting standards and should comply with the requirements of Section 151 (2) of the Companies Act, No.

7 of 2007. Secondly, due to cultural limitation HOTEL ASSURING PL doesn't disclose all the company's information, the main reason behind this is that Sir Lankan has a high ranking in uncertainty avoidance, and according to grays fourth hypothesis the Geiger the country ranks in terms of uncertainty avoidance the more likely it is to rank highly in terms of secrecy. Therefore HOTEL ASSURING PL chooses not to disclose all of the company information to the public just to avoid competition and security problems.

HOTEL ASSURING PL has also been influenced by its stakeholders in many ways. The communities in which the hotel operates in are significant stakeholders of business therefore one of the most important influences of the stakeholders on HOTEL ASSURING PL is the initiation of sustainability reporting by the company (Hotel Assuring Pl, annual report, 2012/2013). The hotel also produces quarterly financial report as per the expectations of the stakeholders so that they can make some financial decisions and analyses the performance of the hotel.

Conclusion To conclude, Adopting FIRS has given Sir Lankan an advantage of presenting its financial statements on the same basis as its foreign rival companies at the same time making comparison much easier, therefore it could be agreed that Sir Lankan is a good place to start a business, however we recommend Seekers Hotel to study the cultural impacts and the political pressures on the financial reporting environment of Sir Lankan before making a final decision of international expansion.