

# [Disadvantages of ifrs for smes](https://assignbuster.com/disadvantages-of-ifrs-for-smes/)

International Financing Reporting can be referred to as a set of accounting standards developed by the International Accounting Standards Board which is applied when preparing the Financial Statement and Balance Sheet of a company. In providing a global framework, IFRS has its own specific goals of how public companies organize and disclose their financial statements.

## Definition of Small Medium Enterprises (SMEs)

A small and medium sized enterprise (SME) is managed by self-employed people either in partnership or on their own. It tends to be companies that are independent. The definition of SME is different from one country to another, depending on how many employees that the companies have. According to Saleh (2006), Malaysia’s SME can be represented based on the turnover, size and activity of the company.

SMEs criteria in Malaysia can be divided into three categories which are micro, medium and small enterprises and it has been classified into the contributions of the sectors based on full time employees and annual sales turnover. Based on Mohammad (2012), the definitions of SMEs in Malaysia as in year 2005 are as the table below:

## Definition of IFRS for SME

IFRS for SMEs has been issued by International Accounting Standards Board (IASB) in 2009 (Goel, 2010). IFRS for a SME is based on the existing full set of IFRS, but it is customised to match the requirement of reporting and accounting in SMEs. It can also be defined as entities that publish general purpose financial statements for external users.

## The advantages and disadvantages of IFRS for SMEs

There are a number of advantages and disadvantages in adopting IFRS for SMEs. One of the advantages in adopting IFRS for SMEs is enhancing the comparability of financial statements and improving access to international funding. Under IFRS for SMEs it uses different accounting method. As stated by (KPMG, 2010) the different in accounting treatment that IFRS for SMEs have which leads to less comparable than those that applying full IFRS and it can reduce the time as more entities adopt the standard thus the interpretation of the requirement in the standard become standardised.

IFRS also can strengthen the SMEs position when negotiate with the credit institutions and when it has a positive effect that have on a credit ratings so this will reduce the cost of borrowing. For instance, the adoption of IFRS leads to an increase in equity ratio and revaluation of fixed assets. This is because IFRS information can help the SMEs in buying and selling goods or services to get new relationship with customers and suppliers in locally or internationally since the financial reporting has been standard by internationally.

Besides that, IFRS for SMEs is less complex that has been simplified from the full IFRS. According to (Jayakumar, n. a), IFRS for SMEs has been simplified through the fundamental principles of full IFRS to make the accounting requirement less complex and also reduce the effort to produce the financial statements which International Accounting Standards Board (IASB) has removed some number of accounting option that have in full IFRS.

In contrast, Accounting Standards Committee of German (2008) supported that the preparation of financial statement in IFRS for SMEs is time, effort and cost intensive that not all requirements and issues in the ED (Exposure Draft) IFRS for SMEs were carefully understood and correctly applied by the participants. This is because German is a tax driven in the financial statement rather than economically relevant values.

Furthermore, some people suggest that IFRS for SMEs is not applicable to adopt and it should be rejected. For instance, based on Samujh (2007), New Zealand is not appropriate to adopt IFRS for SMEs because of balancing principles, practicality and politics might be difficult for the country to converge the standards with the global standards. The adoption of IFRS for SMEs will affect the current reporting regulation in New Zealand.

Other than that, IFRS for SMEs especially in developing countries is difficult to manage because of some limited resources in that country. As mentioned by Bohusova et. al (2011), SMEs for developing countries is difficult to cope with typical SMEs challenges such as limited human resources and limited financial and the decision to adopt the IFRS is based on their economic growth, existence in the capital market and others.

The disadvantage of IFRS for SMEs is it can create a possible confusion in the marketplace. For instance, in adopting IFRS for SMEs there is a relevant regulation that some country must to follow before or after the adopting such as in Germany, they are using tax accounting in their financial statement prepared by German GAAP. However, as stated by Kemp (2009), in Australia there are many issues that should be considered from the lawmakers in measuring the appropriate IFRS for SMEs that create two versions of GAAP which are full IFRS and IFRS for SMEs which make additional training, and transition issues between these two versions.

Additionally, the accounting software is not consistent so the users should be educated in the new standard because it keeps changing. The financial statement must be comparable and clearly understandable so that it would be easier for the user to compare the performance. According to Miller (2010), the changes for accounting software and lending agreement will be required such as the changes in the new standard which need the users of financial statements to be educated and some company want to change their accounting firm that the company needs to find a firm that know how to apply of IFRS for SMEs.

Overall, IFRS for SMEs is easier for the user to use instead of applying full IFRS. This is because, full IFRS will give a burden for the user as IFRS has become more detail and more countries have started to use IFRS since full IFRS is too complex to use.

## An arguments and debates in adopting IFRS for SMEs.

Based on IASB, there is more than 50 jurisdictions decided in full IFRS must be compulsory by all the entities in the SMEs and when the full IFRS is adequate for all entities, then the IFRS for SMEs will be appropriate. In contrast with Neag, R. et al. (2009) suggested that IFRS for SMEs is not compulsory for all entities. This has been proved by Deloitte (2013) that not all jurisdictions have adopted the full IFRS, the full IFRS is adopting only for the jurisdictions that do not have their own accounting systems.

Other than that, as stated by Reilly (2009), IFRS for SMEs has more simplified standard that is appropriate for the bigger unlisted companies to follow and by adopting IFRS for SMEs can save amount of money for those who in unlisted companies that have adopted full IFRS. He also suggest that some argue that unlisted companies that are preparing the financial statement should be applied for IFRS for SMEs and the debate on this issues is the IFRS for SMEs standard needs some cost to adopt but it is too complex for small unlisted entities. As mentioned by Stokdyk (2010), he recommended that IFRS for SMEs was best suitable for the large and medium sized entities reporting under full IFRS.

Moreover, some people argued that no one want an option in the IFRS for SMEs. This is because the countries not often to have an option in financial reporting. For instance, in German about 80 per cent German companies do not want to adopt IFRS for SMEs in their present draft form because they encountered difficulties when asked for the financial information for the German manufacturer that exports to the US and would produce information that prepared by German Commercial Code (Canham, 2008).

When a countries change the financial reporting standards it will be difficult for the company to use the new standards. There is the other debate about the differential reporting that was an important issue in Australia. According to Faux (2005), in early 1980s, the differential reporting was an importance issue that the country should be considered when the accounting regulators were developing a framework for their financial reporting. The regulators focus on financial reporting that should be provide the general purpose information to the needs of wide-ranging of users who are unable to knowledge the preparation of the financial reports that was tailored to their own needs.

As a conclusion, IFRS for SMEs is more appropriate for international demand especially for the developed and emerging economies which a common set of accounting standards in the smaller and medium sized enterprises is easier for the user to use than the full set of IFRS.

## Why choosing Malaysia in IFRS for SME?

SME companies have an important position in the economy, most importantly in developed and developing economies. Malaysia is one of an emerging economy in Asia. Thus, Malaysia want to adopt the IFRS for SMEs in order to improve confidence in the accounts of SMEs, to reduce the cost that is involved in maintaining the standards since IFRS for SMEs is more cost effective to produce, and to improve the comparability for users of accounts of financial statements across different industries.

## History and regulations of accounting for IFRS and SMEs in Malaysia.

In June 2005, the definition of SME across the economic sectors was approved by the National SME Development Council with endorsement from all the Government Ministries and Agencies as well as financial institutions that are involved in SMEs in Malaysia (National SME Development Council, 2005).

In 2006, Malaysia was introduced two-tier reporting framework issued by Malaysia Accounting Standards (MASB) for the companies in Malaysia which are MASB had approved Financial Reporting Standard (FRS) for non-private entities and the Private Entity Reporting Standards (PERs) for the private entities with the objective to reduce the burden of private entities in the financial reporting compliance.

Other than that, in August 2008, Malaysia had brought the Financial Reporting Standards (FRSs) into full conjunction with IFRS. As stated by (Malaysian Institute of Accountants, n. a), in 1 August 2008 the Financial Reporting Foundation (FRF) and MASB announced a plan to bring full convergence with the IFRS which is the full compliance with IFRS for the financial reporting system in Malaysia by 1 January 2012.

Therefore, the plan that made by MASB and FRF create an exposure draft issued by MASB. MASB Exposure Draft 75 IFRS-compliant Financial Reporting Standards that was issued by MASB on 28 June 2011 result in the Malaysian financial reporting framework being standard with IFRS-compliant financial reporting framework.

While in 2010, ED 72 FRS for SMEs has been issued by MASB. According to (MIA, n. a), MASB issued MASB ED 72 FRS for SMEs in 26 March 2010 for the SMEs in Malaysia to use by users that required to publish general financial statement purpose for the external users and do not have public accountability. Other than that, the purpose of IFRS for SMEs in Malaysia is to reduce the detailed requirements under the full IFRS for small entities since full IFRS is too complex for small entities to apply. In Malaysia, the IFRS for SMEs was issued ED 72 in March 2010 (MASB, n. a). Thus, ED 72 is identical with the IFRS for SMEs that was issued by IASB. IASB issued the IFRS for SMES in July 2009 (MASB, 2010).

Generally, Malaysia is in the process in adopting IFRS for SMEs that is expected to be issued in 2013. The revisions of the IFRS for SMEs in Malaysia will be in 2015 on the any amendments to the IFRS for SMEs. According to IFRS (2013), during the first half of year 2013, Malaysia is expected to be issued FRS for SMEs and it will be effective for annual periods on or after 1 January 2016 of the new framework for the private entities. This means that, MASB is considering replacing the PERS framework in Malaysia to IFRS for SMEs in 2016.

## The relevance and appropriateness of IFRS for SME’s in Malaysia.

As we know that, full IFRS is too complex to apply for small entities. Therefore, to make an appropriate for smaller entities, Malaysia needs IFRS for SMEs to provide self-contained in the set of accounting principles which is based on full IFRS. Malaysia makes a modification in IFRS for SMEs from the full IFRS founded from the needs of users in SMEs financial statements which is based on the topics that are not relevant to the SMEs, hence they will eliminate the topics and remove the choices for accounting treatment to make it simple. Other than that, they are also simplifying the methods for the measurement and recognition for the IFRS for SMEs.

However, Malaysia has two frameworks which are PERs and MFRs. The problems occur when comparing these two frameworks according to current documentation and its interpretations. Since IFRS for SMEs is new to the reporting entities, the practices and interpretation of it must be develop from time to time. For example, the entities must considered for cost intensive when they want to change PERs to adopt IFRS for SMEs which they have to pay more to adopt a new standard in the entities.

As stated by Yusoff (2009), the Companies Commission will come out in advance with some of the recommendations that have been made by Company Law Reform Committee in Malaysia including the introduction of a threshold before an audit is required. Normally, most countries do not have across the board audit requirements except for Malaysia. In Malaysia, the foreign investors and inactive companies must be audited so the auditors to SMEs would be valuable because this forces them to be independent and could refuse the business advice to fulfil the professional requirements.

Other than that, SMEs have to face with tough competition in a liberalized environment and they need to produce quality goods at a competitive price in order to compete in the market. By having the changes to IFRS for SMEs would give SMEs in Malaysia to have more capabilities to face stiff competition in the market by having rational strong external financial reporting to make sure it access to capital is not compromised (Yusoff, 2009). When Malaysia’s SMEs react quickly of their global competitors, they will encourage the innovation and the regulation would change.

Furthermore, the adoption of IFRS for SMEs has been issued by MASB and IFRS for SMEs can provide growing business which they required to apply full Malaysian FRSs. However, in 2011, MASB approved another framework for accounting in IFRS for SMEs. According to Farmer (2011), Malaysia has agreed to have a new accounting framework based on the Malaysian Financial Reporting Standards (MFRS Framework) approved by MASB on 19 November 2011 and it is applicable from 1st January 2012. Hence, Malaysian SMEs can choose either to continue to apply PERS or the new MFRS Framework.

Therefore, the IFRS for SMEs in Malaysia is relevant since its accounting framework in IFRS for SMEs is separate from the full IFRS. Based on (MASB, 2010), at the international level, IFRS is separate with the accounting framework in IFRS for SMEs thus it is not affect MASB’s IFRS convergence with policy in 2012 since Malaysia have the decision on whether to adopt the standard or not.

In contrast with New Zealand, the IFRS for SMEs is uncertainty relevant in their countries because this country must bear the cost for implementing and maintaining in both full IFRS and IFRS for SMEs (Samujh, 2007).

The stability of economy and political in Malaysia has created more investors to invest in Malaysia. This has been proved by Bernama (2012), Mustapa Mohamad who is the Minister of International Trade and Industry said that there were four SMEs from Japan that want to invest in agriculture, manufacturing and green energy industry in Malaysia which is some of them have bought land to start the operation in Malaysia. Malaysia also has developed infrastructure similar with other western country which lead for Malaysia to be a host of other services that result in this country to become a good place for the investors because of Malaysia’s economic and political stability (Malaysian Dutch Business Council, n. a). When Malaysia adopts IFRS for SMEs, the standard will be the same with international. Thus, it will be easier for the investor to invest in the SMEs in Malaysia since the financial reporting has been standardised.

In Malaysia, the important contribution of SMEs is in terms of its economic growth, employment and exports. According to Ministry of International Trade and Industry (2013), SMEs contribute to the economy in terms of Gross Domestic Products GDP for 30%, for the total work force is 56. 4% and in terms of total exports is 19%. SMEs play an important role in the economy of Malaysia in generating economic growth for the country. Other than that, the SME sector contains 99. 2 per cent of all businesses in Malaysia (Ministry of International Trade and Industry, 2013).

Finally, as a conclusion IFRS for SMEs in Malaysia is appropriate to apply because it is under control by MASB. As stated by Godfrey et. al, (2007), MASB has a fully responsible for the development of the accounting standards in Malaysia. They are also having the power to issue new accounting standards, make any changes to propose the accounting standards when it is necessary to change and others. Other than that, SME Corp was established in Malaysia to monitor and evaluate the application of strategies, policies and the development in the SMEs across all economic sectors (Hashim, 2009 pp. 269-295). Besides that, currently Malaysia is an advisory for all SMEs in Malaysia and a central point as the reference information for the users in SMEs.

(Total Words Amount: 2994)