

# Adoption of International Financial Reporting Standards in Developing Countries: The Case of Nigeria

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## Abstract

The study focused on the adoption process of International Financial Reporting Standards (IFRS) on a developing economy, with particular reference to Nigeria. The paper is based on the data obtained from literature survey and archival sources in the context of the globalization of International Financial Reporting and the adoption of International Financial Reporting Standards (IFRS). Nigeria has embraced IFRS in order to participate in the benefits it offers, including attracting foreign direct investment, reduction of the cost of doing business, and cross border listing. In implementing IFRS Nigeria will face challenges including the development of a legal and regulatory framework, awareness campaign, and training of personnel. Recommendations were made to forestall such challenges which include strengthening education and training, establishment of an independent body to monitor and enforce accounting and auditing standards.

**Keywords:** Financial reporting, Adoption, Accounting standard and Developing countries

## 1. Introduction

Globalization of capital markets is an irreversible process, and there are many potential benefits to be gained from mutually recognized and respected international accounting standards. The adoption of uniform standards cut the costs of doing business across borders by reducing the need for supplementary information. They make information more comparable, thereby enhancing evaluation and analysis by users of financial statements (Adekoye, 2011). Users become more confident of the information they are provided with and presumably, this reduces uncertainty, promotes an efficient allocation of resources and reduces capital costs (Ahmed, 2011). To bridge the gap between accounting standards among countries, the International Accounting Standards Committee (IASC) was founded in 1973 by a group of professional accounting practitioners. The IASC was to formulate uniform and global accounting standards aimed at reducing the discrepancies in international accounting principles and reporting practices. In this light, the International Accounting Standards Committee (IASC) was established. Since its establishment the IASC has actively been championing the uniformity and standardization of accounting principles for over two decades (Carlson, 1997). In April 2001, the International Accounting Standards Board (IASB) took over the setting of International Accounting Standards from the International Accounting Standards Committee (IASC). Thenceforth, the IASB updated the already existing International Accounting Standards and referred to them as International Financial Reporting Standards (IFRS).

In Nigeria, adoption of IFRS was launched in September 2010, by the Honorable Minister, Federal Ministry of Commerce and Industry, Senator Jubril Martins-kuye (OFR). The adoption was organized such that all stakeholders use the IFRS by January 2014. The adoption was scheduled to start with Public Listed Entities and Significant Public Interest Entities who are expected to adopt the IFRS by January 2012. All Other Public Interest Entities are expected to mandatorily adopt the IFRS for statutory purposes by January 2013, and Small and Medium-sized Entities shall mandatorily adopt IFRS by January 2014. In the light of this therefore, this study focused on the process of adopting the IFRS in Nigeria as a developing economy. Specifically, the study examined the development of the accounting profession in Nigeria, the legal and regulatory framework of accounting, IFRS adoption process, benefits and challenges of IFRS adoption. Finally, conclusions are drawn and recommendation made.

## 2. Literature Review

The expansion of International Trade and the accessibility to foreign stock and debt market has given impetus to increasing the debate on whether or not there is need to be a global set of accounting standards. As companies compete globally for scarce resources, investors and creditors as well as multinational companies are required to bear the cost of reconciling financial statements that are prepared using national standards. It was argued that a common set of practices will provide a “level playing field” for all companies worldwide (Murphy, 2000). IFRS are standards and interpretations adopted by the International Accounting Standards Board (IASB). They include: International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) and interpretation originated by the International Reporting Standards Interpretation Committee (IFRSIC) (Oyedele, 2011). IFRS represent a single set of high quality, globally accepted accounting standards that can enhance comparability of financial reporting across the globe. This increased comparability of financial information could result in better investment decisions and ensure a more optimal allocation of resources across the global economy (Jacob and Madu, 2009). Cai and Wong (2010) posited that having a single set of internationally acceptable financial reporting standards will eliminate the need for restatement of financial statements, yet ensure accounting diversity among countries, thus facilitating cross-border movement of capital and greater integration of the global financial markets.

Esptein (2009), emphasized the fact that universal financial reporting standards will increase market liquidity, decrease transaction costs for investors, lower cost of capital and facilitate international capital formation and flows, various studies conducted on the adoption of IFRS at country level indicated that countries that adopted IFRS experienced huge increases in direct foreign investment (DFI) flows across countries (Irvine and Lucas, 2006). Cai & Wong (2010), in a study of global capital markets demonstrated that capital markets of countries that had adopted IFRS recorded high degree of integration among them after their IFRS adoption compared with the period before adoption. In a study on financial data of public listed companies in 15 member states of the European Union (EU) before and after full adoption of IFRS in 2005, Chai et al (2010), found that majority of accounting quality indicators improved after IFRS adoption in the EU.

In a study on the question of usefulness of IAS/IFRS for developing countries using a case study of Zimbabwe, Chamisa (2000), analyzed the impact of the adoption of IASB standards on the accounting practices of listed companies. Results of the study revealed that these standards have particular importance for developing countries with emerging financial markets. In an analysis of the IAS/IFRS implementation process in developing countries using Armenia as the analytical framework McGee (1999), showed that this process poses difficulties, which can be overcome by concerted efforts in training and information dissemination about the new standards. Alp and Ustandag (2009) studied the development process of financial reporting standards around the world and its practical results in developing countries found that Turkey had encountered several complications in the adoption of IFRS. Such complications include the complex structure of the international standards, potential knowledge shortfall and other difficulties in the application and enforcement issues.

Similarly, in a study on adoption of IFRS at firm level, Meeks and Swann (2009), demonstrated that firms adopting IFRS had exhibited higher accounting quality in the post-adoption period than they did in the pre-adoption period. In a study of financial data of firms covering 21 countries, Barth (2008), confirmed that firms applying IAS/IFRS experienced an improvement in accounting quality between the pre-adoption and post-adoption periods. Latridis (2010), concluded on the basis of data collected from firms listed on the London Stock Exchange that IFRS implementation has favorably affected the financial performance (measured by profitability and growth potentials).

There are also growing number of studies that question the relevance of IFRS in developing and emerging economies. Irvine and Lucas (2006), also reported that the development of globalized set of accounting standards provides other benefits that are not so relevant to developing and emerging nations. The adoption of IFRS will save Multinational Corporations the expense of preparing more than one set of accounts for different national jurisdictions, the professional status of accounting bodies will be enhanced and the big accounting firms will benefit in their efforts to expand the global market for their services. Perera (1989), posited that accounting information produced according to developed countries accounting system is not relevant to the decision models of less developed countries. As evident from the foregoing, a good number of studies carried out in different countries have highlighted the benefits of having single set of financial reporting standards across the globe. Few of the studies have given contradictory views questioning the relevance of IFRS adoption in developing and emerging economies.

### *2.1 Development of Accounting Profession in Nigeria : Brief Overview.*

The accounting profession in Nigeria received a formal reckoning in the mid-1960's (Chibuke; 2008). During that period, Nigerian accountants, mostly trained by professional accounting bodies in the United Kingdom came together and formed a professional accounting body that is responsible for the training of accountants in Nigeria and fostering the development of the profession in the country. Presently, however, a number of professional accounting bodies carry out such functions concurrently. These bodies pay much attention to the teaching of technical and practical aspects of accounting.

The two accounting bodies in Nigeria are the Institute of Chartered Accountants of Nigeria (ICAN) and the Association of National Accountants of Nigeria (ANAN). They are in essence self-regulating, and both membership elect governing council members. There is no separate statutory body for the audit profession. ICAN acts as an examining body for awarding Chartered Accountant Certification and as the licensing authority for members engaged in public auditing practices. Members of ICAN are recognized under the Companies and Allied Matters Act as the sole auditors of company accounts. ICAN is a member of the International Federation of Accountants (IFAC) and has strong International foundation and relationship. ICAN members dominate accounting and auditing services in the private sector while ANAN members are mostly employed in the public sector

### *2.2 Legal and Regulatory Framework of Accounting in Nigeria*

#### *The Companies and Allied Matters Act (CAMA) 1990.*

The Companies and Allied Matters Act, 1990 prescribes some format and content of company financial statements, disclosure requirements and auditing. It also requires that financial statements comply with the statement of accounting standards (SAS) issued from time to time by the Nigerian Accounting Standards Board (NASB) and that audit be carried out in accordance with generally accepted auditing standards.

#### *The Nigerian Accounting Standard Board (NASB) Act 2003.*

The NASB Act, No 22 of 2003, formally created the Nigerian Accounting Standards Board and also established for it an Inspectorate Unit. NASB came into being on September 9 1982. It is the only recognized Independent body in Nigeria responsible for the development and issuance of statements of accounting standards for users and preparers of financial statements, investors, commercial enterprises and regulatory agencies of government.

## **3. Methodology**

To address the emergence of IFRS in the context of the transformation of financial reporting the article adopted a pre-dominantly review approach. The research presented here builds on an analysis of discourses within the range of archival evidence and is based upon an examination the major publications, and documentary materials emanating from the professional accounting bodies (in particular relating reporting regulation, conferences, training and education).

## **4. Key Differences between NG-GAAP and IFRS**

Nigerian public listed entities are required to present their financial statement reports in accordance with IFRS beginning January 2012. Until then, all Nigeria firms prepared their financial statements in accordance with local standards issued by the Nigeria Accounting Standard Board. The principal differences between Nigerian Accounting Standards (NG-GAAP) and IFRS are detailed in Appendix A.

As may be observed, the differences appearing in financial statement presentation such as change in equity, income statement and significant management estimates and judgments are concepts that are not addressed in the local standards. There are also significant differences in property, plant and equipment, related parties, segment reporting, leases, impairment and risk management disclosure. Finally significant differences are also found in other areas such as financial guarantees, scope of consolidation and employee benefits.

## **5. IFRS Adoption Process in Nigeria**

The adoption of IFRS in many countries requires standards setters to understand the different regulatory and commercial environments in various countries. A roadmap on the adoption of IFRS (Issued by the International Accounting Standards Board) was used as a guideline for the preparation of statutory financial statements in Nigeria. The roadmap also outlines specific milestones that if realized, could lead to the adoption of IFRS in three phases as follows: (i) Public Listed Entities and Significant Public Interest Entities in Nigeria by 2012,(ii) Other public Interest Entities by 2013, and (iii) Small and Medium-sized Entities by 2014. The Roadmap discusses various areas for consideration by stakeholders in order to ensure effective adoption of IFRS in Nigeria. The Roadmap for the adoption is as specified in figure1

Insert Figure 1 here

### 5.1 Adoption Statement

It is in the best interest of the nation to adopt the IFRS. The transition should be phased so that the objectives are achieved within the time-frame as outlined in the roadmap (figure 1). The phases are explained as follows:

#### *Phase 1: Publicly Listed Entities and Significant Public Interest Entities.*

This means government business entities, all entities that have their equities or debt instruments listed and traded in the public markets (a domestic or foreign Stock Exchange or an over-the-counter markets). Examples of entities meeting these criteria include: Nigerian National Petroleum Corporation (NNPC), banks and insurance companies.

Transition date for SPEs begins 2010, with a reporting date of 2012. Transition begins by raising awareness to educate both the users and preparers of IFRS financial statements, followed by planning, training and analyzing the impact of IFRS adoption on people, systems and processes and on business of firms. By the year 2011, SPEs will then identify the key reporting data and prepare IFRS opening Statement of Financial Position (SFP). By the year 2012 SPEs are required prepares quarterly report using IFRS rules, follow audit procedures and investor relations to educate analysts, investors and manage external stakeholders. By the year 2013, SPEs would identify the loopholes in the existing system and processes by ensuring compliance and monitoring.

#### *Phase 2: Other Public Interest Entities.*

This refers to those entities, other than listed entities (unquoted, private companies) which are of significant public interest because of their nature of business, size, number of employees or their corporate status which requires wide range of stakeholders. Examples of entities meeting these criteria are large not-for-profit entities such as Charities and Pension funds. Transition date for PIEs begins by the year 2011 with a reporting date of 2013. By which period opening SFP and comparative figures are expected to be prepared. By 2013, PIEs are required to prepare quarterly reports using IFRS, audit procedures, and investor communications.

#### *Phase 3: Small and Medium-sized Entities (SMEs).*

Small and Medium-sized Entities (SMEs) refers to entities that may not have public accountability and their debt or equity instruments are not traded in a public market:

- they are not in the process of issuing such instruments for trading in a public market
- they do not hold assets in fiduciary capacity for a broad group of outsiders as one of their primary businesses
- the amount of their annual turnover is not more than N500 million or such amount as may be fixed by the Corporate Affairs Commission
- their total assets value is not more than N200 million or such amount as may be fixed by the Corporate Affairs Commission
- no Board members are foreigners
- no members are a government or a government corporation or agency or its nominee
- the directors among them hold not less than 51 percent of its equity share capital

Entities that do not meet the IFRS for SME's criteria shall report using Small and Medium-sized Entities Guidelines on Accounting (SMEGA) Level 3 issued by the United Nations Conference on Trade and Development (UNCTAD).

Transition date for SMEs begins by 2012 with a reporting date of 2014. SMEs commence transition to IFRS by 2012, preparing opening SFP and comparative figures and investor communications by 2013, adopting IFRS reporting standards, and ensuring compliance and monitoring by 2014.

### 5.2 Benefits of Adopting IFRS in Nigeria

The adoption of IFRS has several benefits as evidenced by previous studies carried out by several scholars some of which include the following: (Leuz and Verrecchia, 2000): decreased cost of capital, (Bushman and Piotroski, 2006): efficiency of capital allocation, (Young and Guenther, 2008): international capital mobility, (Ahmed, 2011): capital market development (Adekoya, 2011): increased market liquidity and value (Okere, 2009): enhanced comparability (Bhattacharjee and Hossain 2010): cross border movement of capital, (Mike, 2009): improved transparency of results. The potential benefits that Nigeria stands to gain after IFRS adoption are seen in the light of:

- (i) Promotion of the compilation of meaningful data on the performance of various reporting entities at both public and private levels in Nigeria thereby encouraging comparability, transparency, efficiency and reliability of financial reporting in Nigeria.
- (ii) Assurance of useful and meaningful decisions on investment portfolio in Nigeria. Investors can easily compare financial results of corporation and make investment decisions.
- (iii) Attraction of direct foreign investment. Countries attract investment through greater transparency and a lower cost of capital for potential investors. For example, cross-border listing is greatly facilitated by the use of IFRS.
- (iv) Assurance of easier access to external capital for local companies.
- (v) Reduction of the cost of doing business across borders by eliminating the need for supplementary information from Nigerian companies.
- (vi) Facilitation or easy consolidation of financial information of the same company with offices in different countries. Multinationals companies avoid the hassle of restating their accounts in local GAAPs to meet the requirements of national stock exchange and regulators, making the consolidation of accounts of foreign subsidiaries easier and lowering overall cost of financial reporting.
- (vii) Easier regulation of financial information of entities in Nigeria.
- (viii) Enhanced knowledge of global financial reporting standards by tertiary institutions in Nigeria.
- (ix) Additional and better quality financial information for shareholders and supervisory authorities.
- (x) Government to be able to better access the tax liabilities of multinational companies.

### 5.3 Challenges to IFRS Adoption in Nigeria

The practical challenges that may be faced in Nigeria as a result of implementing the IFRS need to be identified and addressed in order to benefit fully from the introduction of IFRS.

These challenges have been evidenced by previous studies conducted by scholars such as: (Alp and Ustundag, 2009): potential knowledge shortfall, (Li and Meeks, 2006): legal system effect, (Shleifer and Vishny, 2003): tax system effect, (Irvine and Lucas, 2006): education and training, (Martins, 2011): enforcement and compliance mechanism. The challenges are discussed as follows:

#### 5.3.1 Level of Awareness

The transition plan to IFRS and its implications for preparers and users of financial statements, regulators, educators and other stakeholders have to be effectively coordinated and communicated. This should include raising awareness on the potential impact of the conversion, identifying regulatory synergies to be derived and communicating the temporary impact of the transition on business performance and financial position. The implementation of IFRS requires considerable preparation both at the country and entity levels to ensure coherence and provide clarity on the authority that IFRS will have in relation to other existing national laws.

#### 5.3.2 Accounting Education and Training

Practical implementation of IFRS requires adequate technical capacity among preparers and users of financial statements, auditors and regulatory authorities. Countries that implemented IFRS faced a variety of capacity-related issues, depending on the approach they took. One of the principal challenges Nigeria may encounter in the practical implementation process, shall be the shortage of accountants and auditors who are technically competent in implementing IFRS. Usually, the time lag between decision date and the actual implementation date is not sufficiently long to train a good number of professionals who could competently apply international standards.

#### 5.3.3 Training Resources

Professional accountants are looked upon to ensure successful implementation of IFRS. Along with these accountants, government officials, financial analysts, auditors, tax practitioners, regulators, accounting lecturers, stock-brokers, preparers of financial statements and information officers are all responsible for smooth adoption process. Training materials on IFRS are not readily available at affordable costs in Nigeria to train such a large group which poses a great challenge to IFRS adoption.

#### 5.3.4 Tax Reporting

The tax considerations associated with the conversion to IFRS, like other aspects of a conversion, are complex. IFRS conversion calls for a detailed review of tax laws and tax administration. Specific taxation rules would

have to be redefined to accommodate these adjustments. For instance, tax laws which limit relief of tax losses to four years should be reviewed. This is because transition adjustments may result in huge losses that may not be recoverable in four years. Accounting issues that may present significant tax burden on adoption of IFRS, include determination of Impairment, Loan loss provisioning and Investment in Securities/Financial Instruments.

### 5.3.5 Amendment to Existing Laws

In Nigeria, accounting practices are governed by the Companies and Allied Matters Act (CAMA) 1990, and the Statement of Accounting Standards (SAS) issued by the Nigerian Accounting Standards Board (NASB) and other existing laws such as Nigerian Stock Exchange Act 1961, Nigerian Deposit Insurance Act 2006, Banks and Other Financial Institution Act 1991, Investment and Securities Act 2007, Companies Income Tax Act 2004, Federal Inland Revenue Services Act 2007. All these provide some guidelines on preparation of financial statements in Nigeria. IFRS does not recognize the presence of these laws and the accountants have to follow the IFRS fully with no overriding provisions from these laws. Nigerian law makers have to make necessary amendments to ensure a smooth transition to IFRS.

## 6. Conclusions and Recommendations

IFRS is driving the revolutionary world of accounting with over 120 countries either requiring or permitting its use. There is no doubt that conversion to IFRS in Nigeria is a huge task and a big challenge; its revolutionary impact requiring a great deal of decisiveness and commitment. It is in the best interest of Nigeria to adopt IFRS. A countrywide intensive capacity building program to facilitate and sustain the process of adoption is needed as early as possible. The IFRS ship is already making its way around the world as a single set of high quality global accounting standards.

Based on the study undertaken on IFRS adoption in Nigeria the following recommendations are hereby advanced. These recommendations may serve as useful inputs for adopting and implementing a country action plan for accounting reforms in Nigeria.

- (i) Raise awareness of professionals, regulators and preparers to improve the knowledge gap. Issues to be addressed include the importance of financial statements prepared under IFRS framework and importance of compliance with accounting and auditing requirements.
- (ii) Improve the statutory framework of accounting and auditing to protect the public interest. This recommendation might necessitate amending the Nigerian Accounting Standards Board Act (2003) into Financial Reporting Act. Various laws and regulations should be revised to conform to the proposed act.
- (iii) Establish an independent body to set monitor and enforce accounting and auditing standards and codes. The proposed body should be empowered to monitor and enforce accounting and auditing requirements with respect to general purpose financial statements.
- (iv) Strengthen professional education and training. The professional accountancy bodies should align their continuing professional education requirements with IFAC guidelines. Business ethics should be taught as a separate subject in undergraduate accounting and business programs and revision to university accounting curricula should enable students to gain exposure to practical IFRS application.
- (v) Strengthen capacity of the regulatory bodies and review adequacy of statutory enforcement provisions. Take necessary steps to strengthen capacity of regulators including Corporate Affairs Commission, Securities and Exchange Commission, National Insurance Commission, Central Bank of Nigeria that enable them to effectively deal with accounting and financial reporting practices of the regulated entities.
- (vi) NASB should set up a committee charged with the responsibility to ensure that this project is not derailed.

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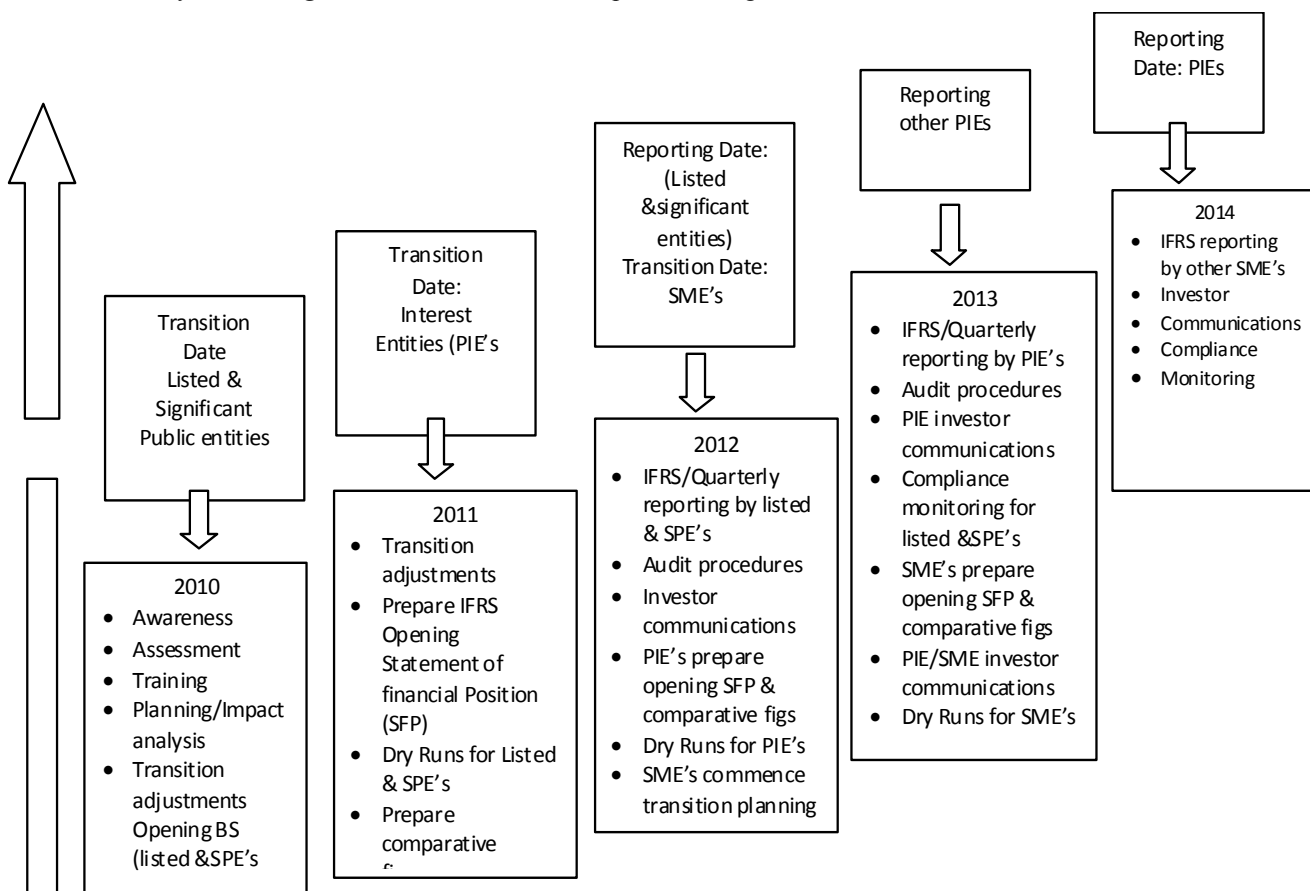


Figure 1. The Roadmap for the adoption  
 Source: Report of the Committee on Roadmap (2010)



**Appendix A: Key Differences between NG-GAAP and IFRS**

<b>TOPIC</b>	<b>NG-GAAP</b>	<b>IFRS</b>
<b>Financial statement presentation</b>	Income statement Balance sheet Cash flow statement Value added statement Accounting policies Notes	-Statement of comprehensive income (including income statement). - Statement of financial position (balance sheet) - Statement of changes in equity - Statement of cash flows - Accounting policies - Notes -Significant management estimates and judgments
<b>Property plant and Equipment</b>	Measured using cost model	Measured using cost model with detailed guidance regarding: - Componentization - Useful lives - Residual values -Impairment calculations and identifying cash generating units.
<b>Related parties</b>	Limited disclosure but expected	Detailed guidance on identification of related parties and detailed disclosure of related parties and transactions
<b>Segment reporting</b>	More on geography	- Operation segments based on management's view. - Threshold for reportable segments is results or assets of an individual segment should be 10% or more of all segments. - If the aggregate revenue of all reported segments on this basis less than 75% of total, then more segments required until 75% threshold is reached.
<b>IFRS 1- First time adoption of IFRS</b>	Not applicable	Provides guidance and requirements on the transition to IFRS. Also provides relief for certain items in the preparation of the opening balance sheet.
<b>Financial guarantees</b>	Disclosed as contingent liabilities	Requires financial guarantees to be recognized at their fair value
<b>Scope of consolidation</b>	General principles	Investment under control are consolidated. SPEs are potentially also consolidated
<b>Employee benefits</b>	General expense and disclosures on pensions	-Complex criteria of accounting -Recognize the undiscounted amount of short-term employee benefits
<b>Risk management disclosures</b>	Limited disclosure of foreign exchange and credit risk	Disclosure required for: - Credit risk and - Liquidity risk - Price risk - Capital risk management - Risk management
<b>Leases</b>	Based on general guidelines – operating and finance leases	-Currently similar but updates to IFRSS e.g. IFRIC 4 will lead to only finance leases hence more items coming unto balance sheet. - Fair value and amortized costs used in valuations -Certain transactions/contracts containing hidden leases which needed to be accounted for
<b>Impairments</b>	- No specific standard	- Carry out impairment test based on trigger vent - IFRS 36 – impairment on non – financial assets - IAS 39 – impairment on financial assets
<b>Financial asset classification and valuation</b>	Classification include: - Cost - Amortized cost	Classification include: - Amortized cost - Fair value This is driven by the business model and nature of the instrument.

Source: Oyedele, T. (2011)

## Appendix B

### Other Relevant Laws that Regulate Financial Reporting in Nigeria

- i. The Central Bank of Nigeria is the main statutory regulator of banks and non-banking financial institutions under the terms of the Banks and other financial institution Act (1991). The Banks and other financial institutions Act contains provisions on financial reporting by banks in addition to CAMA requirements. The Banks Act requires Banks to submit audited financial statements to the Central Bank of Nigeria for approval before publication in a national daily newspaper within four months from the year end.
- ii. The National Insurance Commission regulates financial reporting practices of insurance companies under the National Insurance Act, 2003. Audited financial statement are submitted to the National Insurance Commission within 6 months of the year- end and published in newspapers.
- iii. The Investment and Securities Act, 2007. The Act amongst other things, provides for:
  - a. The establishment of securities and exchange commission
  - b. The repeal of the investment and securities Act 1999.
  - c. The enlarged powers and functions of the commission over the capital market; and
  - d. A set of new market infrastructure and wide-ranging system of regulation of investment and securities business in Nigeria, especially in the area of mergers, acquisition and take over and collective investment schemes.
  - e. A stock Exchange, which is a self-regulating organization established by the Nigerian Stock Exchange Act.
- iv. The Nigeria Stock Exchange Act of 1961, supports the Securities and Exchange Commission, supervises the securities market operations and regulates the secondary market. Audited Financial statements of all quoted firms on the floor of the Stock exchange and the Corporate Affairs Commissions must be approved by the Stock Exchange before publication in newspaper within three month after the year- end.
- v. Companies Income Tax Act 2004 (as amended); one of the Act regulating the taxation practices relating to companies income in Nigeria is the Companies Income Tax Act formally Companies Income Tax Act 1979.).