Adopting International Financial Reporting Standards (IFRS) in Africa: benefits, prospects and challenges

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Abstract: This paper presents the findings of an empirical study on the benefits, prospects and challenges of adoption of International Financial Reporting Standards (IFRS) in some African countries. A questionnaire was administered to gather data from respondents made up of users and preparers of accounting information using the Twitter social network. The objective was to find out the perception of users and preparers about what the benefits, prospects and challenges of IFRS adoption are in African countries. The results of the study indicate that IFRS adoption in Africa will have the potential to be beneficial to a wide range of stakeholders. The benefits notwithstanding, there are however, a number of challenges to be faced in the process of adoption of the new standard including the ethical environment in Africa. The study recommends among others that a rigorous IFRS capacity building programme should be embarked upon by all regulatory bodies, firms and training institutions in order to provide the needed manpower for IFRS implementation, monitoring and compliance.

Keywords: network effects; stakeholders; Africa.

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1 Introduction

The increasing growth in international trade and investment has brought to the fore the craze for adoption of International Financial Reporting Standards (IFRS) by both the developed and developing countries. A number of African countries including Nigeria, Ghana, Sierra Leone, South Africa, Kenya, Zimbabwe, Tunisia among others, have adopted or declared intentions to adopt the standard. This is a welcome development considering the fact that the quality of financial reporting is essential to the needs of users who require useful accounting information for investment and other decision-making purposes. Information emanating from financial reporting is regarded as useful when it faithfully represents the 'economic substance' of an organisation in terms of relevance, reliability and comparability [Spiceland et al., (2001), p.36]. Thus, high-quality financial reports which IFRSs have the potential to support should produce financial information that report events timely and faithfully in the period in which they occur.

It is in recognition of the need to have quality financial reports that the adoption of IFRS is becoming the vogue among countries. The process of adoption received a significant boost when in 2002 the European Union (EU) adopted a regulation requiring public companies to convert to IFRSs beginning in 2005. The major objective of the requirement to adopt IFRSs' is the harmonisation of accounting standards for listed companies in Europe. Most of the publicly traded companies reported their financial statements based on standards set in their individual countries which made interpretation of the financial statements difficult beyond their boundaries. While IFRS adoption may well suit the purposes of the countries in the EU, the story may not be the same for African countries in which the adoption could be catastrophic.

Though the relevance of adoption of international accounting standards have always been a subject of intense controversy, yet, a number of countries in Africa have adopted or plan to adopt IFRS. However, there are many questions which relate to whether the adoption will be beneficial to the countries involved in terms of enhancing transparency in financial reporting that require to be answered. IFRS is more principled-based and does not provide issuers with the same degree of detailed guidance for the preparation of financial statements, as it is for instance, under Nigerian or the US GAAP.

The objective of this study is therefore to address, from the perspective of users and preparers of financial reports, the questions: What are the perceived benefits and challenges of the adoption of IFRS to the wide range of interest group in financial reporting in Africa? Do African countries have the required accounting infrastructure and ethical environment to make the transition to a more conceptual approach to financial reporting effective and rewarding? These questions are pertinent following previous observations made by scholars concerning the accounting and auditing environment in some African countries. For instance, Owolabi (2011) noted that the accounting and auditing practices in majority of African countries, suffer from institutional weaknesses in 'regulation, compliance and enforcement' of standards and rules and also that audit committees of some Nigerian companies have been implicated in contributing to the corporate scandals by not performing their roles effectively (ROSC, 2004; Okike, 2007; Bakre, 2007).

To answer the questions raised, Section 2 of this study examines extant literature on the benefits, challenges and requirements of IFRS adoption in selected African countries. Section 3 explains the research methods used in this study and Section 4 reports the result of the study, while Section 5 is conclusions and recommendations.

2 Review of related literature

The wide spread adoption of IFRS has been promoted by the arguments that the benefits outweigh the costs. It however remains an empirical question if this is the case for all countries whether developed or developing. While opponents of the adoption of IFRS, for instance, Armstrong et al. (2007) argue that one single set of accounting standards cannot reflect the differences in national business practices arising from differences in institutions and cultures, proponents argue that substantial benefits can be reaped from greater cross-country comparability of firms' financial reports. Barth (2007), for instance, argues that by adopting a common body of international standards, countries can expect to lower the cost of information processing and auditors of financial reports can be expected to become familiar with one common set of international accounting standards than with various local accounting standards.

If adopting IFRS is expected to lower such costs, then it will be beneficial to African countries because of their significant reliance on inflows of foreign capital to finance economic and industrial developments. The argument here is that countries choose to adopt IFRS when they expect to increase the share of foreign capital and trade in their economy. In this sense, even countries with low levels of foreign capital and trade can choose to adopt IFRS if they are expecting growth in those factors.

None-the-less, the decision to adopt IFRS by some countries arises from the understanding that it (IFRS) is a product with network effect. Network effect is said to exist where users find a product or service more valuable as additional users use the same product or service. As more and more countries adopt IFRS, it becomes more appealing to others that are yet to consider the adoption. This position cannot be generalised especially in the case of some developed countries such as the USA that is yet to adopt the standard.

In countries where the quality of governance institutions is relatively high, IFRS adoption is likely to be less attractive as high quality institutions represent high opportunity and switching costs to adopting international accounting standards. The opportunity costs arise because in adopting IFRS, countries forgo the benefits of any past and potential future innovations in local reporting standards specific to their economies.

However, in many developing countries, the quality of local governance institutions are low and thus are important determinants of the decision to adopt IFRS (Ball et al., 2000; Leuz et al., 2003; Ball, 2006). Such countries are likely to suffer from corrupt, slow-moving, or ineffectual governments that are resistant to or incapable of change (La Porta et al., 1999). In these countries, the opportunity and switching costs are lower and thus, the chance to adopt an externally developed body of accounting standards presents an advantage. Thus, among countries with less developed institutions like Nigeria, the decision to adopt IFRS is likely to be driven by lower opportunity and switching costs.

3 Research method

This is a pilot and a descriptive study in which questionnaire was used to collect data from two main groups, one representing the preparers of annual reports and the other representing users of annual reports, using Twitter network. To qualify to respond to the questionnaire, the respondent should be a user or a preparer of financial reports and familiar with financial reporting issues in Africa. The questionnaire attempted to probe the preparers' and users' perceptions on the usefulness of the adoption of IFRS in different areas of operations of organisations.

The questions required the respondents to answer on a five-point Likert-scale anchored by (5) indicating very strong and (1) very weak. On this scale, a score of 5 or 4 indicates that the item is perceived to be essential while a score of 3 or 2 indicates that the item is perceived to be fairly important, but not essential, while a score of 1 indicates that the item could be disregarded for being unimportant. Similar scales have been used by Firer and Meth (1986), Courtis (1992) and Myburgh (2001) and were found suitable. To obtain a score for these questions, the mean score was calculated. A total number of 55 responses were received from preparers in ten countries out of which 38, representing 69% were useable. For the users, 83 responses were received from ten countries out of which 64, representing 77% were found useable. The list of the countries is shown in the appendix. Though not much significant statistical inference can be made with regard to the size of the respondents, however, the response rates are considered adequate for the purpose of the study. Only countries where both users and preparers responded were considered.

4 Survey results

The first question sought to ascertain the perception of the preparers and users with respect to the importance of the factors that could make the adoption of IFRS successful in African countries. Seven factors which could potentially lead to successful adoption of IFRS were considered and the results are shown in Table 1.

From the results presented in Table 1, preparers and users are not unanimous in their rankings. The preparers ranked quality of accounting education as the most important factor while the users ranked it as the second. This is closely followed by the need to have professional base of accountants as the second for the preparers, whereas the users consider it as the most important. Overall, the mean scores for each of the factors and for both the preparers and users are quite above the average suggesting that they are positive that the factors listed have potential to lead to successful adoption of IFRS.

Table 1 Key success factors for IFRS adoption

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Professional base of accountants	4.66	2	4.77	1
2	Monitoring and enforcement of reporting requirements	4.50	5	4.55	3
3	Legal mandate to align with IFRS	3.80	7	4.05	7
4	Existence of competent oversight bodies	4.56	4	4.32	6
5	Quality of accounting education and training	4.78	1	4.64	2
6	Sound ethical environment	4.58	3	4.53	5
7	Strong legal framework for supporting accounting practice	4.00	6	4.54	4

The second question probed the current state of key success factors and the results are presented in Table 2.

Table 2 Current state of key success factors for IFRS adoption in Africa

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Professional base of accountants	2.66	2	2.51	5
2	Monitoring and enforcement of reporting requirements	2.50	5	2.55	3
3	Legal mandate to align with IFRS	2.80	7	2.05	7
4	Existence of competent oversight bodies	2.56	4	2.32	6
5	Quality of accounting education and training	2.78	1	2.64	2
6	Sound ethical environment	2.58	3	2.53	4
7	Strong legal framework for supporting accounting practice	2.00	6	2.78	1

The responses in Table 2 show that respondents agree that the current state of the key factors that could make IFRS adoption succeed in African countries are low in quality. The results confirm earlier observations that the accounting and auditing environment in Africa is bedevilled with institutional weaknesses in regulation, compliance and enforcement of standards and rules (Owolabi, 2011), resulting in situations, for instance, where audit committees of some Nigerian companies have been implicated in contributing to the corporate scandals by not performing their roles effectively (ROSC, 2004; Okike, 2007; Bakre, 2007).

The third question probed the benefits which preparers and users consider companies will derive from the adoption of IFRS in their various countries. The results for this question are shown in Table 3.

Table 3 Benefits of adoption of IFRS to companies

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Improved management information for decision-making.	3.69	3	3.60	4
2	Better access to capital, including from foreign sources	3.20	5	3.58	5
3	Reduced cost of capital	3.47	4	3.86	2
4	Facilitating mergers and acquisitions	3.87	2	3.76	3
5	Enhanced competitiveness	3.10	7	2.68	8
6	Ease of using one consistent reporting standard in subsidiaries from different countries	4.35	1	4.45	1
7	Greater effectiveness of the internal audit	2.86	8	2.56	9
8	Lower cost of audit fees	3.15	6	3.45	6
9	Better risk management	2.40	9	3.26	7

The preparers and the users both agree that ease of using one consistent reporting in subsidiaries from different countries is the most useful benefit of IFRS. They also agree on the benefits of better access to capital and lower cost of audit fees which ranked fifth and sixth among the nine variables respectively. They however differ in their ranking of the other factors. The preparers and users consider better risk management and effectiveness of internal audit as the least benefit to be derived from adoption of IFRS.

The fourth question probed the benefits to investors of the adoption of IFRS by African countries from the perception of both preparers and users of financial reports. These results are shown in Table 4.

Table 4 Benefits for investors

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Better information for decision-making	3.43	5	3.69	4
2	More confidence in the information presented	4.16	1	4.15	2
3	Better understanding of risk and return	3.69	3	3.26	5
4	Companies can be compared to a peer group of companies	4.02	2	4.39	1
5	More timely financial reports	3.35	6	3.20	6
6	Easier access to financial reporting	3.44	4	4.10	3

From Table 4, it is observed that preparers chose confidence in the information presented in the financial reports as the most important benefit, followed by comparability of companies by peer group of companies, which users also ranked as the most beneficial.

This is followed by confidence in the information presented. The preparers and users ranked timely financial reports as the least benefit to be derived from the adoption of IFRS. This is not surprising considering the fact that there is nothing in the IFRS framework that relates to timeliness of financial reporting. The overall results however show that the preparers and users are quite positive that IFRS adoption in Africa will be beneficial to the investors.

The fifth question sought to ascertain the benefits of IFRS adoption to policy makers from the stand point of the preparers and users of financial reports. The results are shown in Table 5.

Table 5 Benefits for policy makers (management)

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Strengthened and more effective capital market.	3.20	3	3.40	3
2	Better access to the global capital markets	4.52	1	4.02	2
3	Promotion of cross-border investment	3.56	2	4.18	1
4	Better information for control and decision-making purposes	2.58	4	3.14	4
5	More realistic planning experiences	2.53	5	2.67	5

The preparers ranked better access to global capital market as the greatest benefits policy makers will derive from the adoption of IFRS while for the users it is ranked second. Similarly, the preparers ranked promotion of cross-border investment as the second most important benefit while the users ranked the same factor as the most important. For the other benefits, both the preparers and users are unanimous in their rankings. However, the users are slightly more positive in their perception of IFRS being beneficial in terms of better decision-making purposes and realistic planning experiences.

The sixth question probed the perception of preparers and users concerning the benefits of IFRS adoption to national regulatory bodies. This question is particularly important because IFRS monitoring and compliance enforcement is a national issue. The results are shown in Table 6.

Table 6 Benefits for national regulatory bodies

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Improved regulatory oversight and enforcement	3.13	3	3.07	4
2	A higher standard of financial disclosure	3.47	1	3.50	3
3	Better information for market participants	2.43	4	4.50	1
4	Better ability to attract and monitor listings by foreign companies	3.29	2	3.65	2

Though the preparers and users are unanimous in their ranking that the adoption of IFRS will lead to better ability of regulatory bodies to attract and monitor listings of foreign companies, they however differ in respect of other benefits. Whereas the preparers ranked higher standard of disclosure as the greatest benefit, for the users, better information for market participants ranked first. These rankings are not unexpected because accounting regulation in Africa has traditionally been very prescriptive and thus invites a *form* over *substance* approach. With IFRS, this trend has the potential to reverse.

The curious and interesting issue about the results presented in the above table is that while the preparers ranked better information for market participants as the least beneficial, the users ranked it the most beneficial. Also, the mean scores of the preparers for three of the factors are lower than those of the users. This creates the impression that the preparers are more knowledgeable about what goes in to financial statements than the users. This could be perceived as 'insider' knowledge which only the preparers are exposed to.

The seventh question probed the perception of preparers and users in terms of the challenges of the adoption of IFRS. The results are as presented in Table 7.

Table 7 Challenges of IFRS adoption

		Preparers (n = 38)		*Users (n = 64)*	
		Mean	*Rank*	*Mean*	*Rank*
1	Training of relevant professionals	3.59	6	3.45	6
2	Funding of conversion	4.00	5	3.25	5
3	Compliance and enforcement	4.36	3	4.30	2
4	Complexity of conversion	4.12	4	3.89	4
5	Retention of key employees	4.35	2	4.13	3
6	Ethical environment	4.70	1	4.55	1

The results presented in Table 7 show that the preparers and users only differ in their ranking of the challenges of the adoption of IFRS in two out of six issues raised. They are unanimous that the ethical environment is the most important challenge for the successful adoption of IFRS. This should not be surprising because corporate transparency is a particularly important component of good governance as it ensures the protection of parties (both individual and institutional) who have operational interest in financial reporting in terms of accurate and reliable information which are needed in order to take well-considered economic decisions.

Interestingly, preparers and users are both unanimous that training will be the least challenge. This is curious especially that African countries do not have enough trained and professional accountants. One would have expected training to create the greatest obstacle especially in the issue of first time adoption of IFRS. The result also shows that retention of qualified employees will be a challenge as it is ranked second and third respectively by the preparers and users. In this early stage of adoption of IFRS, poaching of staff, especially accounting personnel might be pronounced due to the dearth of such personnel.

5 Conclusions

This study has provided evidence of the potential benefits and challenges of the adoption of IFRS in Africa. The results show that the introduction of IFRS in Africa will result in a number of important benefits for a wide range of stakeholders. The benefits of ease of using one consistent reporting standard in subsidiaries from different countries will accrue to companies while investors will develop, amongst others, more confidence in the information presented in financial statements which they can understand and use. For policy makers (management), the adoption of IFRS will create better access to the global capital markets and a higher standard of financial disclosure for national regulatory bodies.

The benefits will be largely driven by a number of potential success factors. The benefits and potential success factors notwithstanding, there are a number of challenges to be faced in the process of adoption of the new standard. These among others include ethical environment and the ability to protect qualified and competent employees from being poached by other companies.

Against the backdrop of the objectives of this paper, the following recommendations are hereby suggested: The education, sensitisation, and communication to stakeholders of issues associated with IFRS should commence in earnest. A rigorous IFRS capacity building programme should be embarked upon by all regulatory bodies, firms and training institutions in order to provide the needed manpower for IFRS implementation.

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Appendix

Countries and number of respondents

S/N	*Country*	*Preparers (no.)*	*Users (no.)*
1	Nigeria	8	12
2	Ghana	3	6
3	Cameroun	2	4
4	South Africa	14	20
5	Kenya	10	13
6	Zimbabwe	4	6
7	Egypt	3	5
8	Tunisia	2	5
9	Uganda	5	7
10	Tanzania	4	5
	Total	55	83

Source: Field survey