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# The Significance of International Financial Reporting Standards to Emerging Economy of Nigeria

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## Author's contribution

The sole author designed, analyzed and interpreted and prepared the manuscript.

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## ABSTRACT

This paper explores the relevance of International Financial Reporting Standards (IFRS) to emerging economies in general and Nigeria in particular. The research uses evidence from interviews conducted with senior officers from two Big Four accountancy firms in Nigeria and prior studies exploring IFRS implementation of IFRS in emerging economies to shed light on the influence of complex economic, institutional, cultural and social factors influencing accounting. The findings suggest that accounting practices in Nigeria are dominated by the historically inherited institutionalized accounting system of the old Nigerian era, when accounting information was primarily geared towards meeting the needs of government agencies such as Statistics Committee and tax authorities. The main problems of implementing IFRS in Nigeria were pressures to comply with tax codes, too much power vested in government organizations as opposed to accounting profession, lack of IFRS expertise, deficient enforcement mechanisms and expectation of tax authorities that accounting standards should mimic tax codes. The findings are limited to questioning the relevance of IFRS to emerging economies and have implications for policy makers contemplating to adopt IFRS in those countries. This paper provides some insights into the benefits and drawbacks of IFRS adoption and would be of interest to those in the field.

**Keywords:** IFRS; implementation; accounting; emerging economies; Nigeria.

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## 1. INTRODUCTION

Recently, the adoption of International Financial Reporting Standards (IFRS) has been at the forefront of the agenda of a number of countries worldwide. This is partly attributable to the globalization of capital markets, increased in international trade and cooperation, and the desire to improve the transparency, quality and comparability of financial statements prepared under different Generally Accepted Accounting Principles (GAAP) [1]. However, a number of researchers have suggested that financial statements prepared on the basis of national GAAP may not meet the accounting information needs of international investors and creditors whose decisions are international in scope [2]. Chamisa [3] found that the number of professional accounting bodies from developing countries joining the IASB and adopting its standards has increased despite overwhelming academic arguments suggesting that the IFRS are irrelevant or even harmful to these countries. Ding et al. [4] have pointed out that under the coercive power of international investors and regulators “domestic listed firms are forced to play the accounting game by global rules”. Nobes and Zeff [5] posit that “international financial reporting standards (IFRS) have been adopted in many countries, at least for the consolidated reporting of listed companies”. To date, more than 100 countries are preparing financial statements on the basis of IFRS, while a number of them have made the adoption of IFRS mandatory for publicly traded companies [6]. Moreover, the US Securities Exchange Commission (SEC) has improved the legitimacy of IFRS by allowing foreign entities trading on the US stock exchanges to issue financial statements prepared on the basis of IFRS and waving the need to reconcile with US accounting standards [7].

While a number of studies have suggested that accounting systems should reflect differences in culture, economic systems and institutional settings [8,9], few studies have explored the influence of these factors in the context of emerging economies [10]. This paper addresses this gap in the literature by exploring the adoption of IFRS in emerging economies in general and Nigeria in particular, by examining the following main research question: how relevant are IFRS to the emerging economy of Nigeria? Nigeria is an emerging economy which is undergoing rapid economic liberalization and development. It has embraced privatization and market forces by

moving away from central bureaucratic planning under the former old Nigeria, removing trade barriers, reducing the number of government-owned enterprises, and creating a financial sector to facilitate growth and the movement of private capital. Implementing IFRS is especially challenging in ex-communist countries because it requires changes not only to political institutions but also to socio cultural values and established ways of doing things. The findings of this study may be relevant to Nigeria and Communist bloc countries of Europe, and China.

The research uses evidence from interviews conducted with senior officers from two Big Four accountancy firms in Nigeria and prior studies exploring IFRS implementation of IFRS in emerging economies. The rationale for interviewing auditors is because of their expertise and knowledge regarding the implementation of IFRS by Nigerian companies in various industries. As pointed by Tyrrell et al. [10] increasing harmonization and complexity of accounting standards tend to facilitate expansion of large international accounting firms at the expense of local firms in both developing and developed countries. Moreover, Perera [9] states that international accounting firms have also been an important vehicle for transferring Western-style accounting to developing countries.

The remainder of this paper is organized as follows. Section two draws from the literature to discuss the influence of environmental and cultural factors on accounting and some of the problems faced by emerging economies when implementing IFRS. Section three discusses the research methods used to gather empirical data. Section four presents the findings by discussing auditors' perception of the relevance of IFRS to Nigeria. The final section discusses the main findings and concludes the paper.

## 2. THEORETICAL DISCUSSION OF THE RELEVANCE OF IFRS TO EMERGING ECONOMIES

### 2.1 The Influence of Environmental Factorson Accounting

A number of studies have explored the influence of economic, socio-cultural, institutional and legal factors on accounting and the information needs of users. Gray [11] and Perera [9,12] argue that international differences in accounting practices are attributable to differences in socio-economic,

historical, cultural and political contexts. Ashraf and Ghani [13] suggest that accounting practices in different parts of the world are shaped by the stage of economic development, structure of corporate ownership, financial system, legislation (code law vs. common law), tax legislation, and education, among others. Indeed, during the old Nigeria era accounting system (more specifically, uniform book-keeping) was a key administrative tool used by state enterprises for planning, target setting and controlling government and agencies. However, after the collapse of the former regimes of the pre-colonial Nigeria other countries, countries started to move towards free market economy by radically reforming their institutional structures, economic systems and accounting systems and following established Western /capitalist models and systems [14]. In short, reforms to accounting systems and institutional structures were the result of systemic turbulences.

Many researchers have expressed concerns regarding the appropriateness of Anglo-American accounting standards in less developed countries [8,9]. They suggest that developing countries should develop their own accounting standards to reflect differences in their local environment. The International Accounting Standards Board (IASB) tends to promulgate accounting standards that are relevant to developed countries with dominant private sector and developed capital markets, where the major users of accounting information are analysts, dispersed shareholders and creditors so that the conceptual framework for developing IFRS is oriented towards these major accounting information users [9]. However, in emerging countries' capital markets are relatively underdeveloped and the public sectors relatively more influential than private sectors, and the needs of users may be different. For example, Tyrrall et al. [10] suggest that in less developed countries, the primary users of financial statements are tax authorities, owners of the businesses and local lenders, and therefore IFRS tailored to the needs of developed countries may be irrelevant.

Samuels and Oliga [15] argue that imposing IAS that have been developed in an environment with a different set of economic, cultural, religious and social conditions may not only be irrelevant or dysfunctional for developing countries but could also be harmful and counterproductive. *De jure* mandatory adoption of IFRS would probably not lead to *de facto* improvement at the micro level, as actual practices are shaped by complex

economic, political, legal and institutional factors. In this respect, Ball [1] argues that China's adoption of IFRS for foreign-owned entities has neither significantly changed the actual financial reporting practices nor improved the quality of financial statements. In the case of Pakistan, Ashraf and Ghani [13] claim that the quality of accounting information has not improved as IFRS adoption was hampered by corruption, deficient judicial and legal systems which were incapable of protecting interests of shareholders and enforcing laws and regulations.

Mirghani, [16] suggests that instead of myopic adoption of accounting practices developed in other parts of the world, developing countries should consider how well these practices fit with their own indigenous accounting information needs. Perera, [9] states that accounting standards should mirror the dynamic and ever-changing social, economic, legal and cultural circumstances prevailing in those countries and cater for the ever-changing needs of users of accounting information. Whittington [17] criticizes the current conceptual framework of decision-usefulness used to develop [FRS on the grounds that its main purpose is to provide forward-looking information to predict future cash flows and is concerned with buy or hold or sell decisions of investors, whereas the stewardship functions of accounting are inadequately covered. The notion of stewardship is based on the agency theory and concerned with monitoring the actions of the agent and implies a more prudent and conservative approach to accounting such that financial statements show how the current situation had arisen due to past events and actions of the agent [17]. Thus IFRS may not be appropriate to many countries with underdeveloped capital markets, where the owners of private enterprises are not dispersed and are primarily concerned with monitoring of the actions of the agents as opposed to making buy or sell or hold decisions. In these countries a set of accounting standards developed on the basis of the stewardship conceptual framework would probably be more relevant.

Sucher and Jindrichovska [18] jargue that in the emerging economy of Czech Republic where accounting system is regulated by the Ministry of Finance, there could potentially be problems with IFRS implementation since the Ministry of Finance has vested interest in the information needs of tax authorities. Similarly, in the emerging economy of Nigeria, the Ministry of Finance which has significant influence over

accounting standard setting and adoption may place greater emphasis on legal form rather than on economic substance in financial reporting practices oriented particularly to the needs of tax authorities [10]. Thus identifying the primary users of financial statement users is an important step towards ensuring that accounting standards meet their varied and often conflicting needs [19].

## 2.2 The Influence of Culture on Accounting

Culture is often referred to as the set of values, rituals, postulates, beliefs and symbols at the collective level accepted by society at large, so that it creates an atmosphere of predetermined way of behaving with unwritten rigid codes and enables the distinction of one culture from another [20,21]. A number of studies have explored the influence of culture on accounting [12,4]. Accounting as a socio-cultural practice involves value-laden processes of interpreting and implementing accounting by human participants. The exercise of professional judgment across different countries is value laden as it depends on the beliefs of human actors interpreting and applying accounting rules. Differences in culture may explain the apparent lack of consensus among different countries on what represents proper accounting methods [12]. Whittington [17] argues that most likely different meanings will be attached to appropriate way of financial reporting, due to the differences in cultures and ways of doing things that exist in various economic, social and institutional settings. Gray [11] suggest that culture values or dimensions at the societal level such as (1) individualism vs. collectivism, (2) large vs. small power distance, (3) strong vs. weak uncertainty avoidance, and (4) masculinity vs. femininity<sup>3</sup> may be linked at the micro level with four accounting values of (1) professionalism vs. statutory control, 2) uniformity vs. flexibility<sup>5</sup>, 3) conservatism vs. optimism, (4) secrecy vs. transparency. Hofstede [22] and Gray [11] posit that external and global forces (e.g. foreign investment, international trade and globalization) can potentially affect a country's accounting values and institutional settings (e.g. financial system, structure of corporate ownership, legislation and tax system). Perera [12] suggests that high professionalism is associated with low government intervention in accounting regulation and with greater extent of professional self-regulation, while high uniformity is associated with low application of professional judgment and more emphasis on compliance with detailed,

prescribed accounting rules and legislation. Moreover, a high score for conservatism is associated with a more prudent approach to measurement and less emphasis on fair value accounting, while the extent of secrecy is directly related to disclosure practices and

1. Large vs. small power distance dimension of culture refers to the extent to which society at large tolerate unequal distribution of power within its institutional arrangements. In large power distance cultures individuals take for granted unequal distribution of power and hegemony/domination of certain individuals over others and do not attempt to equalize power In small power distance cultures members of society exert some pressure to equalize power within institutional settings, while any remaining unequal power distribution of needs justification [11,12,21].
2. Strong vs. weak uncertainty avoidance dimension of culture refers to the level of society's acceptance of unknown future, deviant ideas or people, unknown and new situations, and unpredictability of certain events. In strong uncertainty avoidance cultures members of society tend to have institutional settings and rituals creating prescribed codes of behaving in various situations creating an atmosphere of stability and predictability. In weak uncertainty avoidance cultures society members are more tolerant to ambiguous and uncertain situations, and behave in a more flexible way to adapt to situations [11,21].
3. Masculinity vs. femininity dimension of culture refers to whether society at large is more concerned with individual success, domination, competition and wellbeing as opposed to being concerned with building human relationships, preserving environment, protecting weak people and caring for others. In masculine society people value financial wellbeing and power, whereas in feminine society individuals place more importance on relations with other members of society and on solidarity [11,12,21].
4. Professionalism vs. statutory control refers to the extent to which accountants within society prefer to exercise professional judgment and have self-regulated profession instead of having rigid and prescriptive accounting rules and

government regulation of accounting practices. Professionalism is expected to be positively related with individualism and inversely related with uncertainty avoidance and power distance [11].

5. Uniformity vs. flexibility refers to the degree to which accountants prefer rigid rules and regulations so that accounting practices are uniform across firms and over time instead of having flexible accounting practices to cater for the substance of transactions [11].
6. Conservatism vs. optimism refers to the extent to which accountants prefer measuring transactions at historical costs instead of having more risky or novel approach to measurement such as fair value accounting that can increase uncertainty. According to Gray [11], conservatism is positively related to uncertainty avoidance and significantly negatively related to masculinity.
7. Gray [11] suggests that secrecy is positively related with uncertainty avoidance and power distance, and inversely related with individualism and masculinity. Attitude of profession towards less or more transparency [12]. Baydoun and Willet [23] state that "the accounting systems used in developing countries may be irrelevant" to users' needs "because they originate in Western countries with different cultural values". In this respect, Perera [9,12] found differences in the cultural dimensions of (1) individualism vs. collectivism and (2) power distance between Anglo-American countries and developing countries, which question the relevance of IFRS to developing and emerging countries. The score for individualism was much lower and power distance was much higher in the case of developing countries compared with Anglo-American countries, suggesting that from a cultural perspective more uniform accounting standards/rules as well as more active government intervention in accounting regulation is required or developing and emerging countries (ibid.). Greater uniformity of accounting rules and less flexibility decreases the scope for using discretion when making professional judgment, while high power distance indicates that uniformity will be readily accepted (ibid.). However, Carmona and Trombetta [7] state that uniformity may reduce the quality of accounting

information as firms operating in different environment may face specific circumstances requiring a more flexible approach to financial reporting as provided under principles-based IFRS.

In summary, from a cultural perspective IFRS may be irrelevant to the emerging economy of Nigeria which is characterized by collectivism and large power distance. If indeed the level of individualism and professionalism are low and power distance is high, then adopting principles-based IFRS may potentially be problematic and arguably uniform or rule based accounting standards maybe more relevant to Nigeria. Bloom et al. [24] found that in Armenia, one of the former Soviet Union countries, the level of individualism was low and power distance was high because under the totalitarian regime of the Soviet Union people are used to being told what to do and when to do it, and as such rule based and uniform accounting systems may be more compatible with the local culture and values.

### 2.3 IFRS Implementation Difficulties

Based on 35 responses from a survey of companies which have implemented IFRS, Tyrrell et al. [10] identified a number of issues which have hindered IFRS implementation in Nigeria. Some of these were contradictions with the Tax Code, underdeveloped capital markets, differences in financial system where banks are primary users of financial statements, inappropriate software programs which are unable to generate proper accounting information needed for more extensive IFRS based disclosures and lack of expertise to implement IFRS (see also the World Bank [25] report on accounting codes in Nigeria). However, Tyrrell et al. [10] suggest that Nigeria adopted IFRS due to the country's desire to increase and stimulate foreign investments.

The findings of IFRS implementation studies in ex communist countries such as Poland, Armenia and Czech Republic may be relevant to Nigeria as they share similar institutional framework. In the case of Polari Jaruga et al. [26] found a lack of educational support and infrastructure for implementing IFRS. Moreover, issues related to corruption, unavailability of IFRS translations. Differences between national GAAP and IFRS standards and illiquid stock exchanges created further difficulties. Sucher and Jindrichovska [18] identified that in the emerging economy of Czech Republic, where the

Ministry of Finance has considerable power over accounting and tax matters, accounting practices were more form over substance and tax-oriented since primary financial statement users were tax inspectorates. IFRS implementation problems were compounded by underdeveloped stock markets distorting fair values used under IFRS. Despite the claimed orientation towards investors and substance over form, in practice the local accounting practices were primarily form over substance with an emphasis on rigid compliance with tax and accounting legislation of tax authorities, rather than focusing on showing economic reality implying that in emerging economies tax authorities are powerful and influential. In this respect, Sucher and Bychkova [27] suggest that in Russia tax inspectorate still exercise a strong influence over enterprise's preparation of financial statements and local audit firms view the primary objective of audit as ensuring compliance with tax rules.

Legal system exerts substantial influence on accounting practices and may hinder IFRS implementation. In Common law Anglo-American countries, developed equity markets are major sources of finance, legislation system is oriented on protecting the interest of dispersed shareholders, and accounting reports are oriented towards showing economic reality (substance over form) in a transparent and reliable manner. However, in code law countries funding primarily comes from governments and banks so that financial reporting practices are less transparent, more creditor-oriented, more form over substance and aligned with tax rules [13]. Indeed, in Common law countries tax legislations do not have major influence on accounting systems/practices such that tax accounting and financial accounting are considered as separate functions, whereas in Code-law countries the influence of Tax Legislation is so pervasive that tax accounting and financial accounting are aligned as organic whole [28]. In Germany tax accounting and financial accounting were mirror image of each other and called *Massgeblichkeitsprinzip* [29], but ceased under the 4th directive of the European Union mandating IFRS compliant consolidated financial reporting to be prepared for all publicly traded companies. However, in European Union countries where tax system and accounting system are interdependent, disclosures concerning tax are allowed [28] implying that tax legislation may have a substantial influence on accounting. Variations in financial reporting were primarily explained by different levels of

interdependence between taxation and accounting [26]. Nigeria exhibits features similar to other code law countries and follows Continental model of accounting of form over substance, suggesting that tax issues may dominate accounting issues.

### 3. RESEARCH METHODS

This study is based primarily on qualitative data collected from semi-structured interviews conducted in 2011 with senior officers based in two Big Four audit firm located in Nigeria. The names of the interviewees (labeled A to J) and the names of the audit firms (labeled I and 2) are not disclosed to maintain anonymity of the respondents. Although one of the researchers works for a Big Four audit firm in Nigeria, it does not necessarily mean that some of the interviewees were from that organization. Interviews with the partners were conducted in English as they were native English speaking expatriates from UK, USA and Australia. However, interviews with two audit managers, one chief accountant and one audit senior were conducted in Nigeria based on personal preference of the interviewees who were local Nigeria nationals and could express their views better independently'. All interviews were transcribed and those conducted in English were first transcribed in Local Languages and later translated to English by one of the researchers who was fluent in the language. Table 1 provides additional detail of the interviews.

To improve the reliability of the data collected, all interviews were tape-recorded and transcribed within one week of conducting the interviews. Appendix shows some of the questions asked to guide the semi-structured interviews. These were mostly informed by the literature discussed in section two of this paper. Care was taken to identify the potential for bias when analyzing the interview transcripts, as the Big Four audit firms have an interest in the implementation of new accounting technologies.

### 4. FINDINGS

#### 4.1 Perception of the Influence of Institutional and Political Context on Accounting

Accounting practices in Nigeria are influenced by the government and could be traced back to the central planning system used under the Nigerian Union. As explained by an audit partner, under

**Table 1. Details of the interviews**

Interviewee	Language	duration	Gender	Nationality	Department	Position
AI	English	1 hour 30 minutes	Female	Foreigner	Auditing	Partner
BI	English	1 hour	Male	Foreigner	Auditing	Partner
C1	English	45minutes	Male	Foreigner	Tax and Legal Consultancy	Partner
DI	Local	45 minutes	Male	Nigeria	Auditing	Manager
EI	Local	1 hour	Female	Nigeria	Accounting department	Chief accountant
FI	Nigeria	50 minutes	Female	English	Auditing	Senior
G2	English	1hour 15 minutes	Male	Foreigner	Auditing	Partner
H2	English	1 hour	Male	Foreigner	Auditing	Partner
I2	English	1 hour	Female	Foreigner	Tax and Legal Consultancy	Partner
J2	Local	1 hour	Male	Nigeria	Auditing	Manager

the totalitarian regime of the Nigerian Union tax authorities were feared and considered the main financial statement users in Nigeria:

In the past the main users have always been just the tax authorities. But as the economy opens out then the main users should become banks, suppliers, but not only the tax authorities. So the tax reporting should be really separate function and that's one of the big difficult and challenges I think Nigerian has to face. It's cultural change waiting to happen. ... It probably originates from former Nigerian times and there is still a fear factor of the tax authorities. Therefore there is a lot of resistance to actually implementing IFRS in accounting records because the accounting records are still basically viewed as primarily a tax record. Tax is God within Nigeria ... that's because of the power that the tax authorities have had over the years and still have (Interviewee AI).

As pointed by Sucher and Jindrichovska [18], in cases where the Ministry of Finance, which also regulates and collects taxes, is made responsible for overseeing the development of accounting standards, there might be concern that the Ministry of Finance would not take account of the views of all prospective users of financial statements. In the current institutional framework, the professional judgment of accountants is compromised by fear of powerful tax authorities. The interviewees were generally concerned about the fact they are personally liable and may end up in jail or pay fines if errors or omissions were found in accounting records. One of the interviewees stated that:

Before implementing any IFRS standard, accountants consider in advance all the possible

tax implications/consequences in terms of jail, penalties and fines, thus accounting practices in Nigeria is form over substance (Interviewee EI).

Similarly, interviewees pointed out that auditors' judgment are further compromised by the lack of legitimacy provided by oversight bodies such as the Nigerian Stock Exchange and the Ministry of Finance. Auditors seemed wary of issuing qualified audit reports as they, instead of the companies, face blame when they highlight problems. As suggested by an interview:

Regulatory oversight doesn't push hard enough to ensure compliance. The Ministry of Finance should make sure that companies are aware but they didn't come out and say "hey f you don't comply you shall have problems" to the companies but tended to focus on auditors. Recently they came out with a memo blaming the auditors not the company by stating audit firms issue 3 disclaimers in a year, then the audit firm could have a problem (Interviewee BI).

Although interviewees pointed out that the major users of financial statements for large organizations were banks, pension funds, shareholders, creditors, tax authorities, Ministry of Finance and foreign investors, the major users of the larger number of small businesses were perceived to be tax authorities. There was consensus among interviewees that all large-scale firms (including non listed firms), international businesses, local firms making IPO (initial public offering) abroad, financial institutions, medium-size companies should follow IFRS. However, there were some concerns regarding the relevance of IFRS to small-size businesses. As Interviewee J2 explained:

Most of the small businesses have basic/simple economic transactions and there would be no material difference under IFRS reporting to them (Interviewee J2).

The fact that financial reporting is still geared towards meeting the needs of tax authorities can be traced back to the previous financial reporting regime which was under the heavy influence of the government. Prior to adopting IFRS, companies were using Nigeria Accounting Standards (NAS) which was developed by Ministry of Finance in consultation with PricewaterhouseCoopers. NAS were similar to tax legislation, as was the case in Germany before it adopted the 4th Directive of the EU. As one of the interviewees explained:

The Nigeria Accounting Standard doesn't address anything apart from the requirement to report for tax and in my opinion reporting for tax should not color what your financial statements are. I don't think that style of reporting is much use to anyone apart from the tax authorities (Interviewee CI).

Technical assistance report of the Asian Development Bank also suggests that the problem of fully implementing IFRS is partly the result of frequent changes in tax legislation in countries using civil codes of other countries leading to high level of IFRS non-compliance even by listed companies [30,25]. To mitigate this problem, Sellhorn and Gornik-Tomaszewski [29] pointed out that in Italy the government has changed both tax legislation and civil code to facilitate IFRS adoption.

Perception of the influence of tax on accounting although IFRS have been officially adopted since 2007 by companies with significant public interest [25], tax issues have continued to dominate accounting. As explained by one interviewee, accounting practices in Nigeria are deeply embedded in and informed by tax considerations:

Companies are more interested in complying with what the tax requirement is. They see IFRS financial statements as auditors 'financial statements that auditors create. They are more interested in what the tax authorities want, they are more concerned about Tax Authorities coming to penalize than whether the Ministry of Finance is going to blame them for producing incorrect IFRS financials. They try to keep the tax department happy (Interviewee CI).

Tax legislation may impede IFRS implementation, as the former follows cash accounting principles. For example, according to the tax legislation and NAS, revenue should be recognized on the date of signed invoice and waybill, but not as per paragraph 14 of IFRS 18 "when the entity has transferred to the buyer the significant risks and rewards associated with ownership of the goods". The evidence suggests that accruals accounting principles may not have been strictly followed for some transactions and as such IFRS may not have been properly implemented. As pointed by an interviewee: even though Nigerian adopted IFRS, current taxation and legislation does not provide full scope for IFRS implementation since government did not link cash accounting under NAS and accruals accounting under IFRS together, and many entities still do not adopt IFRS because they do not understand how all those things will work in practice (Interviewee H2).

Legal form of transactions may also dominate substance as tax audits require retrospective adjustments of accounting records to arrive at IFRS figures, and the fear factor limits the ability to use professional judgment forcing accountants to comply with formalities of the Tax Code. Similar problem was found in another country where there is often ambiguity in the laws such that much power rests with civil servants who interpret the law in their own way [27]. One of the interviewees eloquently described that the (tax) tail should not wag the (accounting) dog as follows:

Accountants fear putting through accruals before all the tax paperwork is in place and therefore their accounting records will not include accruals, so they have to be added on separately to arrive at IFRS reporting. It is also the result of a lack of understanding of the tax legislation, which is enhanced by the heavy-handedness of the tax authorities when they go into these companies... In any country there are differences between IFRS and tax legislation but here tax legislation and tax authorities expect the accounting records to match the tax returns ... for me I expect to see accounting records when auditing together a list of adjustments but what I actually see is people 's accounting records are always bent towards the tax reporting and don 't reflect the IFRS position. Accounting records are geared towards tax legislation and not towards the economic situation. The tax tail should not wag the economic dog (Interviewee AI).



Chua and Taylor [31] argued that IFRS has diffused quickly partly because it is a principles-based set of rules that enables local customization and local translation as compared to tightly specified set of rules lacking plasticity. An interviewee noted that organizations are not changing their structure to facilitate IFRS implementation but are adapting the latter due to its plasticity:

The accounting systems, controls and organizational structure that were in place just didn't suit IFRS. So you end up with sort of! think organizations trying to change IFPS to suit them rather than change the organization to suit IFRS (Interviewee B1).

#### **4.2 Arguments for Adopting IFRS in Nigeria**

The interviewees indicated that there was a general improvement in the quality of financial reporting since IFRS implementation, primarily because cash based accounting standards (e.g. NAS) were unable to effectively meet the information needs of investors which have gained importance over the years in Nigeria. Consistent with the literature, interviewees suggested that IFRS adoption could improve trust in financial reports and increase foreign investments leading to the development of capital markets [2]. Moreover, the global financial crisis also played a role in reshaping financial reporting in Nigeria, as banks started to demand IFRS compliant financial information while previously the decisions to grant credit were primarily based on collateral and relationships. As one of the interviewees pointed out:

With the financial crisis we are getting away from collateral and relationship based lending by the banking organizations to really looking at the operations of an entity. I think this is where IFRS comes in as it enables better understanding what the real economics of the business is and that's not lending you \$ 1,000,000 based on a plant or land you have. Banks want to see a business plan, financial statements, cash flows and debt service plans, in addition to collaterals to assess creditworthiness (Interviewee C1).

The shift towards providing loans based on reliable IFRS financials was explained by high volume of bad loans arising from relationship based lending, and the fall in the value of collaterals during the financial crisis. It was also noted that IFRS provide a wealth of information,

covering gaps in both the Tax Code and NAS which are unable to keep pace with the rapidly growing economy and address complex business transactions. As noted by an interviewee:

There are a lot of details in IFRS regarding how you treat and how you determine certain derivatives or how you treat reserves or provisions for employee pensions, etc. But we have nothing in tax law governing these. Nigeria is a very quickly developing market and so are the financial instruments relating to oil and gas accounting. We see hedging transactions, puts and calls, and a lot of pretty sophisticated transactions that the tax law doesn't address, so having that underlying blanket of IFRS that does address those types of things is good. (Interviewee 12).

Interviewees generally concurred that IFRS can better show economic reality and is more comprehensive compared with NAS. For example. Interviewee J2 explained the limitations of NAS vis a vis IFRS as follows:

NAS compliant financial statements do not disclose and recognize all the future liabilities (e.g. Asset retirement obligation related to subsoil-use contracts and social obligations). There is no guidance in NAS concerning allowances/provisions on bad debts. Indeed, there are substantial gaps in NAS which comprise of a total number of 209 pages compared with IFRS which comprise of more than 2000 pages. NAS are cash-based accounting standards as compared to IFRS.

#### **4.3 Some IFRS Implementation Challenges**

Because of the problems of determining fair values in imperfect or underdeveloped markets, interviewees were concerned that models may be used by managers to manipulate accounting information to create a reality that suits their interest when preparing IFRS financial statements. An interviewee explained that fair value accounting is fundamentally flawed due to the subjectivity involved in determining fair values in illiquid capital markets as follows:

fair value accounting is fundamentally flawed. It has been fundamentally flawed ever since it was first mooted... fair value accounting to me is just another name for putting whatever you want on something. Because the valuation models companies use can be so different making

nothing comparable. ... If you have illiquid capital market, is it better to use model to count for (he fair value or is it better to use cost? At least everyone understands what cost is and how flawed it is (interviewee B1).

However, all interviewees agreed that IFRS implementation should have a positive effect in the long-run on the development of capital markets in Nigeria, as one of the determinants of efficient capital markets is reliable accounting information. Although to some extent the problem may be mitigated by the use of independent valuation experts, an interviewee pointed out that there was a lack of valuation expertise in Nigeria as follows:

There is a limited poor of Nigerian licensed valuation experts and firms. And the issue you also run into is disparity between certain valuations depending on other influential factors. There is always I think a pot entails for bias given the somewhat limited market of valuation services in Nigeria (Interviewee C1).

Interviewees generally perceived the institutional and political frameworks in Nigeria as obstacles to implementing IFRS. Where tax rules conflict with accounting regulations, the former may prevail if the accounting profession is not well developed or has not fully gained societal legitimacy. Accounting in Nigeria is still governed by the provisions of the Law on Accounting and Financial Reporting of 1995 (the "Accounting Law,"), as amended by Parliament and endorsed by the Ministry of Finance in 2007 to incorporate IFRS and portray Nigeria as a modern, organized and well-regulated place to conduct business. The World Bank [25] report pointed out that IFRS implementation and enforcement is also hampered by a lack of IFRS qualified staff, which makes the specific task of monitoring compliance with IFRS extremely difficult.

Interviewees revealed that there was a lack of official IFRS translations and guidance in Nigerian languages leading to interpretation problem. As noted by an interviewee: there is a non-official publication of IFRS in Nigerian, but it doesn't actually have the guidance and interpretations. So we often have a disagreement with a client where we say well the standard needs to be interpreted in this way and they say they disagree because ... The IFRS translation is in Nigeria. We understand the client's view but you check the English interpretation it becomes very clear that the IFRS was not meant to be

applied in the way interpreted by the client (Interviewee H2).

High power distance, low individualism [22,11] and the personal liability of accountants may be obstacles to implementing IFRS and using professional judgment effectively. There is some evidence to suggest that the uniform accounting rules of the old regime may be more relevant to Nigeria than imposing or paying lip service to IFRS implementation, although there are potential benefits to implementing IFRS in the longer term.

## 5. DISCUSSION AND CONCLUSION

The current accounting practices in Nigeria were partially shaped by the historically inherited institutionalized accounting system of the colonial era, when accounting information was primarily prepared to meet the needs of various government agencies such as Statistics Committee and/or tax authorities. Whilst undoubtedly the adoption of IFRS brings the benefit of improved transparency and accountability [1,26], the literature and the preliminary findings presented in this paper casts doubt on its suitability to emerging economies [10]. Prior to adopting a set of financial reporting standards in other countries, greater thought is required as to whether accounting information should serve its current or traditional purpose of reflecting the legal form of transactions or whether accounting should reflect the economic substance of transactions, or alternatively, whether accounting should be tailored to meet the needs and expectations of specific stakeholder groups. Jaruga et al. [26] for example compared financial statements of English companies prepared under IFRS with those prepared under English GAAP, and found that financial statements prepared under IFRS showed net value of assets closer to market values due to the revaluation of fixed assets, but these assets were fully depreciated under English GAAP because capital allowances were fully claimed under tax rules. Thus whilst IFRS have the ability to better portray economic reality or profit earning capacity of the resources of an enterprise to suit the needs of investors, local GAAP may serve the purpose of meeting the information needs of tax authorities.

The adoption of IFRS has the potential to contribute to the development of capital markets by reducing the cost of capital through providing information enabling foreign investors to better

assess the risk profile of business entities. High quality accounting information may also lead to more efficient allocation of financial resources by enabling managers to make informed decisions. IFRS's appeal has also increased due to globalization and fluidity of capital flows across borders. However, Chua and Taylor [31] found limited support to mainstream research findings that wide-spread adoption of IFRS by various countries was due to economic benefits, greater comparability, increased transparency and higher quality information. They suggest that world-wide IFRS diffusion could be explained from social and political perspective, by providing examples of how powerful international financial institutions (e.g. The International Monetary Fund and World Bank) required IFRS adoption in financially distressed countries in exchange for rescue packages. In Nigeria, the support of IFRS by political organizations such as the Ministry of Finance and professional accountancy bodies may be instrumental to the successful adoption of IFRS.

Although principles-based approach to financial reporting under IFRS requires professional judgment, it provides greater consistency and comparability of financial statement information than if rule based financial reporting (for example, under US GAAP) or other country specific rules were followed. Bhimani [32] argues that most academicians, commentators and financial regulators partly blamed the financial scan Zlals in the US such as Enron and WorldCom on the application of rigid and prescriptive US GAAP hampering auditors ability to exercise professional judgment and understand businesses' models, financial transactions and risks. One way forward for the Ministry of Finance to reconcile IFRS and differences arising from the application of rigid tax rules may be to form a joint working group comprising of accounting specialists and tax officials, but the lack of power of the accounting profession may remain a spectre haunting IFRS implementation.

The findings are relevant to emerging ex-communist countries where tax authorities and other government agencies are considered the prime users of financial statements and legal form over substance prevail [18]. Similar to Nigeria, these countries are probably characterized by the communist-mentality of accountants preferring prescriptive and more uniform rules as opposed to using professional judgment, insufficient IFRS education, historical

legacy of tax-driven accounting regime and culture, code-law system and coercive power of government agencies marginalizing the needs of other stakeholders.

Whilst from a cultural and institutional perspective IFRS may not be appropriate to Nigeria, due to institutional arrangements (enforcement mechanisms, taxation, legislation), mentality of local accountants (e.g. most of them were trained during Soviet times), high power distance (fear of government authorities) and low individualism, the economic arguments may in the long run outweigh and alleviate these concerns. Although rules-based/ uniform accounting standards may be currently more suitable given their compatibility with the current structures in place, principles based IFRS better fit with the new capitalist and free market ideals embraced by Nigeria. Changes in the socio economic, cultural and political environments are required to ease the implementation of new accounting technologies for greater compatibility and success.

## COMPETING INTERESTS

Author has declared that no competing interests exist.

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## APPENDIX

### Appendix: Some of the questions asked to guide the interviews.

- 1) Do you believe that quality of financial statements improved since IFRS was implemented in Nigeria in 2007?
- 2) Do you think that IFRS adoption in Nigeria was too early leaving auditors and audit clients not enough time to prepare to IFRS transition? Has the quality of financial statements improved from 2007 compared to 2010?
- 3) What were the main obstacles to IFRS implementation in Nigeria? Has anything changed since 2007? If yes, could you name what are the obstacles nowadays?
- 4) What are your thoughts regarding the gap between NAS and IFRS? Is the gap narrowing or widening from year to year?
- 5) In your opinion what type of entities should follow IFRS and what type of entities should follow NAS?
- 6) Do you believe that IFRS adoption should be voluntary or mandated by the government?
- 7) How are IFRS actually being implemented in practice in Nigeria (e.g. compared to the claimed or mandatory adoption)?
- 8) Are IFRSs relevant to Nigeria taking into consideration its politico-legal and socio-economic context?
- 9) What are some benefits of adopting IFRS in Nigeria?
- 10) Considering the fact that IFRS leans towards substance over form, to your knowledge are there any contradictions between IFRS and Nigeria's Tax Code? In other words, are there any problems of IFRS implementation related to Nigeria tax legislation?
- 11) Who are the primary financial statement users in Nigeria?
- 12) The conceptual framework of IFRS is based on idea that shareholders are the primary users of financial statements. How relevant is this conceptual framework to Nigeria?
- 13) Are English language and the unavailability of IFRS in Nigerian languages a problem to implementing IFRS? Please explain.
- 14) Principles-based IFRS requires using professional judgment. Do you believe that accounting professionals in Nigeria are qualified enough to exercise professional judgment?
- 15) Do you think Nigeria is ready to fully implement IFRS? Why?

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