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Critical Success Factors Analysis on International Financial Reporting Standard Implementation in Indonesia

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ABSTRACT

In 2009 – 2012, Indonesia adopt International Financial Reporting Standard (IFRS) into its accounting standard. Indonesia accounting standard board believe that IFRS adoption will increased quality of accounting information. The convergence process face several difficulties and constraint due to several problem regarding human resource, infrastructure, and regulation. This research purpose is to describe three critical sucess factors for in Indonesia. Three critical success factors are: Human Resources Education, Business Process Infrastructure, and Regulation harmonization. Research done using qualitative descriptive method with case study approach. To assess the impact level of three critical sucess factors, researcher compare Indonesia condition with other countries adopted IFRS. The research show that all three factors affect Indonesia and other countries implemented IFRS. Researcher suggest several action to be done, so the convergence process can be done effectively

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1. INTRODUCTION

International Financial Reporting Standard is a financial accounting and reporting standards that used internationally. Along with globalization, which is characterized by the international trade, investment and barrier removal, accounting and financial reporting itself will be affected. International Financial Reporting Standard will be useful to bridging the needs of globalization, by making a world-class standard for financial statement preparation. International Financial Reporting Standard in 2013 currently used over 100 countries, either through adoption or convergence process. Benefits of using IFRS as accounting standard are:

- Improve the comparability of financial statements, since users around the world use single standard, it will become easier to compare performance of companies listed in various countries.
- Improve information quality on international capital markets, since international investor will be easier to read and understand financial statement, by using single standard. It will attract investor to invest in capital markets.
- Removing barriers to international capital flows by reducing differences in financial reporting requirements.
- Reducing financial reporting costs for multinational companies and financial cost analysis for analysts. Many countries that used to reconcile the financial statement to comply with various accounting standard, now can save the cost of reconciliation.
- Improve the quality of financial reporting, so it can be "best practice" for accounting standard.

The benefits of IFRS can't be achieved for free. To comply with IFRS, companies must incurred several compliance cost. Compliance cost of IFRS including:

- Change / improvement of information system component, include information contained and database of information, since IFRS mandated companies to disclose more information to users.
- Change / improvement of accounting policy, and for some instances, must be linked heavily with operational matters, such as impairment test.
- Change / improvement of business process, since many IFRS proposed new accounting model that differ significantly with current business model, such as leasing, revenue recognition, post retirement benefits, etc.
- Training / Learning for executives and preparers of financial statement, for executives they have to understand the key impact of IFRS, and for technical accounting staff, they have to understand how to apply recognition and measurement principle of IFRS.

Ernst and Young Global (2009), on the report published in January 2009, stated that:
"As a first step, companies will need to assess the full scope and impact of the conversion — not only on the accounting and finance functions, but also on IT, human resources, tax, contracts, and performance metrics and dashboards"

The bottom line number of financial statement - profit and loss amount- will be also affected with IFRS, the variations and fluctuations of income will be higher, since IFRS information will reflect fair value in market. It will be a challenge and consideration for countries to implement IFRS.

Indonesia already implement IFRS gradually since 2009 – 2012. Currently, Indonesia's accounting standard already converged with IFRS, although there is 3 years lag (Indonesia's accounting standard adopt IFRS/IAS effective on 1 January 2009). Indonesia also faced the same challenges, how to implement IFRS succesfully? To obtain benefit from IFRS, Indonesia

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will also incurred compliance costs. To minimize the cost, Indonesia must identify key critical success factors.

Key success factors to minimize the compliance cost of IFRS, will rely on human resources and environment. In micro level, human resource must be ready to understand and applying IFRS. Business environment must also changed, the information system and database must be improved and strengthen. In macro level, several government regulation must also considered to change/adjust to IFRS requirement. Prior studies show that the extent of political influence on accounting and the legal origin of the country affect the need for published financial information (Ball et al., 2000). Indonesia needs to adjust for regulation in order to apply IFRS sucessfully.

This research will compare Indonesia and several countries in their preparation applying IFRS. Comparation will be focused on critical success factors: Human Resources, Business Process, and Regulation.

Accounting standard is a main guideline to treat and present transaction. Accounting standards do not work automatically, but needs to be done by human resources who understand the accounting process thoroughly. Various theories and textbook show the human resource needs to be competent, so the financial statement can be prepared in a well form. Based on the theory, it is compulsory for all preparers to understand the financial statements prepared using IFRS. This is because IFRS and previous GAAP carries a different based.

Lack of understanding can lead to the financial statements are not accordance with IFRS. Auditor also needs to understand IFRS, because it is not possible to express an opinion the financial statements, without understanding the standards used to prepare financial statements.

IFRS designated to be standard that qualified for international quality, as the consequences the standard requirements will be tight and demanding.To prepare financial statement with IFRS, several change must be made to business process. IFRS require companies to present both qualitative and quantitative information. Company must strengthen infrastructure to satisfy the criteria set out in IFRS accounting standards.

Ernst and Young (2012) stated that IFRS will impact the business, systems and processes, as well as the investor communications in various entities. Entities will need to evaluate these implications and plan their responses. In addition, entities should consider the timing and infrastructure for the adoption of any new standards. Thus, it can be seen in a variety of industries, such as banking, insurance, real estate, that the IFRS accounting standards may change the business processes exist within a company.

Accounting standards are not the only one rules or guidelines for the company to account for transaction or present the information. There are a lot of laws compiled by various business regulator. In conducting a business, the company is bound by many rules. For example: law regarding taxation, in which also regulate the revenue or expense recognition, central bank or financial institution regulatory body which regulated some reporting requirement for specified companies.

The rules can be overlapped or even conflicted. This is happen because the regulatory body, upon issuing the law, conduct minimum or none discussion or harmonization with other rules. It will confuse companies and create an inefficiency in producing information. With regard to IFRS, IFRS will also resulted in a number of regulatory changes, to customize the content of IFRS standards, and also to avoid confusion for the financial statement preparer.

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2. METHODS

The research use qualitative methodology. In a qualitative methodology perspective, this research can be classified as qualitative descriptive, as it aims to construct a detail description, and reveals the meaning behind the data that appears (Burhan Bungin., 2007). data collected in this research using literature study and interviews. The literature study use a textbook literature, scientific journals, and on-line documents.

Interviews will be conducted using personal interviews techniques. Iinformants' in this interview are actively involved in a IFRS convergence, and consist of practitioners and academicians. Due to personal reason, the name can't be revealed in this paper. Every respondent were given 10 questions regarding critical success factors in implementing IFRS. All the interview transcript already been recorded.

The general identity of respondent can be describe as follows:

- From the academicians, the respondent is a associate lecturer at state university in Bandung, she actively involved in IFRS convergence proccess, and used to served as technical director in accounting association.
- From the practitioner, the respondens are (1) a senior supervisor of accounting in state owned enterprise located in Jakarta (2) senior auditor in one of big 4 accounting firm in Indonesia.

3. RESULTS AND DISCUSSION

3.1 Human Resource

Human Resource gives a significant contribution for successful implementation of IFRS. Unfortunately, several difficulties face human resource. The difficulties caused by lack of understanding the IFRS, or the minimum knowledge regarding the impact of the IFRS to current accounting practice.

Ernst and Young Global (2009) conducted survey in various companies in United States of America and found out that 64% of the respondents say they have only limited knowledge of IFRS and 62% reveal they lack a preliminary understanding of the balance sheet impact of IFRS. The same situation happen in various countries, India face difficulties, especially to make stakeholder understand about the impact of IFRS and to raise commitment along convergence process (Bhaskar, Bodipatti. 2011). Indonesia situation is the same as the previous two countries. Indonesia has a basic problem regarding the lack of accountant, as stated by academician:

> *"Sometimes it quite difficult to implement accounting standard, imagine we have various multinational companies, and we only have a few accountant. Not just the accountant that understand IFRS, but all the accountant. We only have less than 100.000, compared to other countries. We lack of resources"*

In the companies, several companies already improve the knowledge of the IFRS. The improvement usually done by hosting a training and seminar regarding IFRS, or send a financial accountant to go to training, as stated by practicioners:

> *"To understand the impact on tax, we have to understand the "thing" (IFRS) is.. We collaborate with many institutions, sometimes in a form of in house, or we sent some to go to seminar, maybe not only in domestic but also abroad"*

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From the auditor's perspective, lack of understanding in IFRS is not only happen in accountant prepare the financial statement, the auditor itself need to be introduced regarding IFRS, as stated by respondent from auditor:

> *"It's the same, Accountant don't understand and so do we, I mean, we understand the technical things, but sometimes since we have different judgment and consideration, often we ended up having conflict with auditee."*

Since IFRS have a principle based nature, the standard can be multi interpreted in various way by various stakeholders, so there are some preparation to avoid confusion and also to make a better understanding, regarding IFRS. From the interview conducted, several improvements can be described as follows:

1. <u>Synchronize or change the financial accounting curricula</u>, including IFRS and teach the student how the basic ideas for professional judgment, as stated by academicians:
   "We have to teach IFRS and integrated the IFRS into the curricula, not just change the syllabi, but since the professional judgment also essential, why don't we took another approach to teach? Such as Problem Learning, it will make students think like they have to decide the outcome in financial statement."
2. <u>Conduct training for financial and accounting personnel</u>. Training should be set not only for technical staff, but for all managers and also executive. It will raise not only the understanding of technical matters in IFRS, but also to raise awareness and also commitment to implement IFRS and to analyze the implementation of IFRS by companies, as stated by auditors
   "…………… Well, I believe the training will provide not only technical knowledge, but also awareness and commitment"
3. <u>Obtain certification regarding IFRS</u>. Various certification for IFRS available in domestic (Indonesia) and through various international accounting association. Certification can solidify the knowledge of IFRS and could be a parameter for someone for understanding IFRS. As stated by auditors:
   "You can pursue many certifications, at least after you get certified; we may believe that you have that ability (IFRS understanding ability)."

3.2 Business Process

IFRS make an impact on business process of the company. IFRS demand extensive information either quantitative or qualitative. Various researches show that information system become major attention since the implementation of IFRS. Research conducted by Dunne et al of Institute of Chartered Accountant in Scotland (2008) shows that some companies in United Kingdom, Ireland and Italy, major changes were required to information systems, and different processes and operating modes were introduced to collect, process and disclose the extra information required under the new standards.

Indonesia also faces a problem regarding information system. Investment cost in information system increased since the implementation of IFRS, as stated by the respondent:

> *"We hire consultant to improve our system, nowadays we live in fair value era. Fair value needs reliable information, and reliable information needs expensive information system."*

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IFRS main concept is fair value. Fair value requires company to define the business model and describe the business model in recognition of an element in financial statement. It also create impact, since the previous accounting standard, doesn't rely on fair value information. The difficulties can be described by the story of the practitioners:

"In implementing PSAK 48: Impairment (IAS 36), we can't just rely on future valuation, but we need information from operation people. We have to change the procedure and also manual for impairment, because of the standard"

From the academicians, the business process change happen in almost industries around the world, as stated below"

"Banking changed due to PSAK 50, 55, and 60… It force bank to update information system, and IAI had to suspend the implementation twice. Insurance and Real Estate also feel the impact, especially in revenue recognition model. The IFRS really force company to mark with business model. Its unavoidable."

From the interviewed conducted several procedures for business process improvement can be described as follows:

1. <u>Companies must adopt or improve information system infrastructure</u>, so the information system can produce information according to IFRS requirement.
2. <u>Companies must change some business rules and procedure for implementation of IFRS</u>; it must be done to harmonize with business model.
3. <u>Companies must re-evaluate and re-design performance metrics, for performance evaluation</u>, since the IFRS had impact in some accounting numbers, as stated by academicians:
   "The IFRS will also impact Key Performance Indicator, if company not changed the KPI measurement and standard, there will be lots of item that assess as "below standard"."

3.3 Regulations

Regulations created by many institutions or regulatory body. The financial reporting regulation issued by various institutions. Some times the regulations overlapping and conflicted with IFRS. The companies often confused with the conflict.

The major overlapping is tax. Various study in several countries show that difference in tax reporting and financial reporting make inefficiency, since company has to prepared two set of financial statement. In India, the companies implementing IFRS face the issue of tax accounting that significantly differ from IFRS, which create many reconciliation and time to make corrected financial statement. (Girish K.R. 2011) stated that Convergence to IFRS was going to be a challenge with many companies having made little preparation or having understood it to relate many typical issues of the country's corporate laws and practices, particularly relating to applicability of taxation issues in IFRS.

In Indonesia, there is also a problem regarding taxation. Indonesian Tax Law still refer to US-GAAP and some old accounting standard, so many companies face difficulties and had to make several reconciliation and also two time reporting, as stated by auditors:

"Tax is confusing, our tax law required the companies to use Rupiah for currency, while some client must use non Rupiah currency as a result of PSAK 10, this is inefficiency, and can't we do something to settle the difference?

Academicians argue that source of the conflict because there are no effort to harmonize the rules between accounting standard and various rules, as stated below:

> "*When we make accounting standard, we adopt form International, without considering any difference with Indonesia's environment, although in the standard board, there are delegations from central bank or government, but they are not always the rule-maker. The rule maker often acts according to its own.*"

From the interview conducted, several improvement for regulation can be described as follows:

1. Harmonize various regulation with IFRS to avoid conflict and redundancy, for example in taxation with Directorate General of Tax, Ministry of Finance (revenue and expense recognition and also for reporting using foreign currency), with Industries regulator (for example, insurance companies, regarding the differences in estimating future claim).
2. Accounting standard due process should actively involving regulators and regulators should also invite accounting standard board when addressing some regulation matters.

4. CONCLUSION

Based on the research result, it can be concluded that the three critical factors in implementing IFRS has impact in Indonesia and several countries implemented it. To overcome the difficulties caused by the three factors, researcher suggested companies to apply the improvement as stated in the research result section.

To further strengthen the implementation, researcher suggests additional improvement as follows:

1. University and related institution design the curricula to teach IFRS to accounting students, in the financial accounting and also auditing subject, so the accounting students will get extensive knowledge regarding IFRS, it will be useful for students to prepare themselves before they go into practical world.

Auditors, Accounting Association and Regulatory Body jointly design the guidance to implement IFRS, so it will reduce conflicted items, and increase parsimony between accounting standard and regulations.

5. AUTHORS' NOTE

The authors declare that there is no conflict of interest regarding the publication of this article. Authors confirmed that the paper was free of plagiarism.

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