



Challenges of Implementing IFRS in Kosovo

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Abstract

Purpose: This research aims to present the process of adoption of International Financial Reporting Standards (IFRS) by large enterprises in Kosovo and main challenges faced during the implementation.

Methodology: We conducted a quantitative research through a customized questionnaire regarding the challenges presented during the implementation period, which was addressed to 138 companies which are required by law to report under IFRS of which 100 valid for research, which were completed by the accountants of those companies.

Findings: Based on data analysis, we have identified that the main challenges faced during this process are related to the lack of knowledge of accountants and no continues professional development as well as lack of training and it is evident that the process of implementing IFRS is complex.

Originality/Value: The findings of the study provide empirical evidence in the application of IFRS from development countries as well as challenges during adaption phase of IFRS.

1. Introduction

With the advent of globalization, Kosovo's capital market has witnessed rapid expansion, integration and diversification. Since this extension of the globalization process, there was a need for internationally understandable and uniform financial statements.

In 2012, Kosovo has announced the first time adoption of the International Financial Reporting Standards (IFRSs). Prior to acceptance of IFRSs, the financial statements in Kosovo have been prepared in accordance with the Regulation No. 2001/30 "On the establishment of the board of the financial reporting of Kosovo and the financial reporting regime of the business organizations." According to the Law in force on Financial Reporting, all large enterprises have to apply IFRSs as well as other recommendations. Additionally, as of January 2015, all SMEs must apply IFRSs for SMEs. IFRSs are accounting standards based on the principles that define accounting policies. The global adoption of IFRSs provides uniform financial reporting to the users of the financial statements by enabling the application of the same accounting principles and rules worldwide. Since 2012 in Kosovo, it has been imposed the need to eliminate national barriers to financial reporting rules in adoption of IFRSs at the international level to reduce inconsistencies and enable the comparability of financial information for economic entities regardless of their place of operation. The implementation of this legal obligation in addition to its advantages often presents numerous difficulties for entities during their practical implementation, as IASB does not provide clear guidance on how to manage the transition to the use of IFRSs from local standards. The complex and frequent changes made by the compilers of these standards are among the most significant difficulties faced by first time adapters. As a result, this paper analyzes the level of practical implementation of IFRSs, transition from Kosovo Accounting Standards (KAS) and the main challenges faced by economic entities in achieving the appropriate level of implementation. This paper will contribute to literature by providing empirical evidence in the application of IFRSs from development countries as well as challenges faced during adoption phase of IFRSs.

2. Literature Review

There are many different researches on the issues of harmonization and standardization of accounting and financial reporting across Europe and elsewhere as well as the impact on the comparability and transparency of financial statements. In pursuit of this goal, the IASB works closely with stakeholders worldwide, including investors, national standards developers, regulators, auditors, academics and others who have an interest in developing high quality global standards.

The transitional phase towards the implementation of IFRS has aroused great interest for researchers in this field. Over the last decade, various researches have been done to identify the challenges of passing and implementing IFRSs, taking into account the translation, communication and interpretation of IFRSs by the IASB (Jermakowicz, E. K., & Gornik-tomaszewski, S., 2006). Although accounting systems are similar in many different countries, it is still difficult to compare information based on different frameworks, due to differences in how these standards are implemented by entities as a result of differences in the economic and political environment of that country. The speeding up of this process of convergence or harmonization of the local regulations with the IFRS was also generated by factors such as the fact that the accounting information disclosed in accordance with the local standards does not always fulfil the informational needs of the market players (Saidi, 2013). It is also expected that the implementation of the IFRS will provide a higher level of quality to the financial information, as opposed to the local accounting standards (Bendovschi, O.S, 2016). Different studies have concluded that countries with different cultures have different accounting rules and practices. Researchers Adhikari Ajay & Rasoul H. Tondkar (1992) have reported that "Reporting, accounting and standards for the provision of information and practices do not take place in a vacuum, but reflect the specific environment in which they are developed". Accounting principles and accounting practices are generally influenced, not only by environmental factors, but also by the stage of economic development of the society and the accounting system. Other studies, suggested that compliance, applicability and legislation are among the many issues that need to be resolved in the process of

developing a single set of world standards. While another researcher of this issue has concluded that the purpose of the process of international harmonization of accounting standards is to reduce or overcome differences at the global level to achieve comparability between financial statements (Choi F.S, 2002).

Many studies have examined issues related to the possible consequences of the International Accounting and Financial Reporting Standards / IFRS rules, including the potential costs / benefits associated with adopting them. From the existing international literature, it can be seen that scholars generally agree that IFRSs represent a set of global accounting standards that affect the quality of financial statements by increasing their transparency and comparability. In most cases, the implementation of the IFRS results in an increase in the level of comparability between the financial statements used by the investors, especially if it is considered the fact that, currently, investors are interested in the global investment opportunities and a lot of companies are extending their businesses beyond national borders (Odia, J.O & Ogiedu, K.O, 2013). As the forces of globalization prompt more and more countries to open their doors to foreign investment and as businesses themselves expand across borders, both the public and private sectors are increasingly recognizing the benefits of having a commonly understood financial reporting framework supported by strong globally accepted auditing standards (Peter W., 2004). However, in a research conducted by (Lantto A, 2014) it was concluded that the preparation of financial statements by applying IFRS is more complex. According to him, IFRSs require "something" to be calculated, but does not indicate how the calculation should be done. The implementation of these standards carries with it the confrontation with many challenges, during this path of transformation. One of the most important challenges in implementing IFRSs is the complex nature of these standards. As a result of this complexity, the number of efforts by entities decreases. Many studies have been done on possible challenges, and Jermakowicz best summarizes the main challenges for the implementation of IFRS as follows: "The complex nature of IFRSs, which are designed for large companies; lack of IFRS implementation guidelines; lack of uniform interpretation of

IFRSs; impact on profit and loss account; constantly changing IFRSs; running parallel accounting systems; preparation of comparative financial statements for recent years; lack of knowledge of IFRSs among employees and auditors; training of accounting and management staff; changing the mindset of finance staff; changing the structure of IT "(Jermakowicz et al, 2006). Due to the lack of knowledge from the staff responsible for the preparation of financial statements under IFRS, auditors have a large involvement in the preparation of financial statements in accordance with IFRS, increasing the risk of self-review during the audit of financial statements as they will review their own work on preparing the financial statements (Hoogendoorn,M., 2010). Regulators expect that the use of IFRSs improves the comparability and transparency of financial statements, enhances the quality of financial reporting, and the quality of external audit, and thus benefits investors and users of the financial statements (EC Regulation No. 1606/2002). Due to the required uniformity, reliability and financial comparability, the adoption of IFRSs by 120 countries is a matter of global importance (United Nations Conference on Trade and Development, 2013). Universal financial reporting standards will increase market liquidity, decrease transaction costs for investors, lower cost of capital and facilitate international capital formation and flows (Epstein, J, Barry, 2009). The same was also argued from (Daske, H., Leuz, C., & Verdi, R. S.,2013) that the implementation of IFRSs increases liquidity and reduces the cost of capital.

Post-implementation studies of IFRSs have shown that in general the establishment of national accounting standards in accordance with IFRSs and their applicability, despite the problems encountered during implementation, has led to improved quality of financial reporting.

2.1 Implementation of IFRSs in Kosovo

There is a lack of research done related to the implementation of IFRSs in Kosovo, so this paper can serve as a starting point for more in-depth studies in the field of financial reporting by encouraging researchers to further enrich literature. Financial reporting in Kosovo from 2001 to 2012 is based on the regulation no. 2001/30 on the Establishment of the Financial Reporting Board of Kosovo and the Financial

Reporting of Business Organizations. After the approval of law no. 04 / L-014 on Accounting, Financial Reporting and Auditing, since 2012 the implementation of IFRSs has become mandatory. According to this law, one of the main functions of the Kosovo Financial Reporting Council (KCFR) is to draft and adopt accounting standards in accordance with IAS / IFRS and relevant EU directives, as well as to oversee continuing education, and the provision of quality. This law obliges large enterprises in Kosovo to implement IAS / IFRS, interpretations, recommendations and advice issued by the IASB and approved by the KCFR. As of January 2015, all SME must apply IFRS for SME.

3. Research questions and hypotheses

The research tool considered most suitable to collect data to achieve the research 3. Research questions and hypotheses

Through this research we will present the current state of financial reporting in Kosovo as well as the level of implementation of IFRSs by local enterprises. The application of IFRSs, in addition to the advantages it has for financial reporting, also has many practical problems as a result of the complexity in this area. Due to the needs of the global economy, IFRSs are changed very often, hence the need for follow-up in order to update them. Preliminary studies have shown that the main challenges for the adoption and application of IFRS were the lack of experience and adequate explanations of these standards. As Kosovo is a developing country with lack of professionally trained staff in the field of financial reporting and the frequent changes that occur in these standards, makes the application of these standards a slow and complicated process.

Based on these data, the following questions are addressed:

1. What are the main challenges that accountants in Kosovo have encountered in using IFRSs?
2. Have trainings been organized for accountants to explain and simplify IFRSs?

Based on the research questions, the research hypotheses have been drafted, which are:

H1- Frequent changes in IFRSs and lack of adequate training and explanations have made the financial reporting process complicated.

H2- The level of professional training of staff in the field of financial reporting is the main problem related to the practical implementation of IFRSs.

4. Research methodology

The methodology followed in this paper is based on two data sources: primary and secondary sources. For testing hypotheses and drawing conclusions, special attention has been paid to primary sources, which are represented by data collected through research questionnaires, addressed to professionals in the field of financial reporting. This stakeholder group has been selected in order to obtain assessments from the accounting practitioners themselves regarding the problems in practice and the level of implementation of IFRS to arrive at the necessary findings for making recommendations. Through secondary sources, a comprehensive study has been conducted in terms of research and analysis of numerous works in the implementation of IFRS. The paper is mainly based on data from the scientific literature and similar scientific publications. Theoretical content includes literature used by international scholars.

Hypothesis testing is done using the "Chi Square" test. Much of the data for this research report came from a survey questionnaire, sent to 138 companies, which are required by law to report under IFRSs. The sample includes all the main economic sectors to reflect the differences between the different sectors, not only generalizing from the experiences and situation of one sector. There were 100 valid questionnaires from research, which were completed by the accountants of those companies, given the fact that the preparers of financial statements are the main source for collecting data related to financial reporting, problems, and difficulties in implementing International Standard of Financial Reporting (IFRSs).

4.1 Empirical analysis and discussion of the results

To test the hypotheses presented in this research, the collected data were processed through which we tested the dependence of the dependent variable with the independent variables to confirm or refute these hypotheses.

Table 1. Operational variables

Dependent variable:	Implementing IFRS is a complicated process
Independent variables:	Lack of adequate knowledge by IFRS implementers
	Lack of adequate explanations and trainings for IFRS

Source: *Author*

The Chi-Square test was used to test the hypotheses, according to which the effect of variables on each other is tested.

The Chi – Square test is calculated according to the formula:

$$X^2 = \sum [(O_{r,c} - E_{r,c})^2 / E_{r,c}]$$

x^2 = chi-square statistics

$O_{r,c}$ = the frequencies observed at level r of Variable A and level c of Variable B

$E_{r,c}$ = predicted frequencies at level r of Variable A and at level c of Variable B

$$E_{r,c} = (n_r * n_c) / n$$

n_r = all frequencies observed at level r of Variable A,

n_c = all frequencies observed at level c of Variable B, and

n = sample size.

Results with a value less than $p = 0.05$, show that the tested variables are dependent and have an impact on each other, and vice versa, i.e. the results on the above value show that the variables are not dependent. The test results of the hypotheses presented are as follows.

H1- *Frequent changes in IFRSs and lack of adequate training and explanations have made the financial reporting process complicated.*

Table 2. Variables

V1. IFRS are complicated	These standards are more complicated than the previous local standards with which the financial statements were prepared in Kosovo. Knowing that IFRSs have room for professional judgment make them even more difficult to implement.
V2. IFRS are constantly updated	There is insufficient trainings to explain the change in IFRS

Source: *Author*

While the summary of responses for each variable as problems for the level of application of IFRS: "IFRS are complicated" and "IFRS are constantly updated" are presented in the following table.

Table 3. Implementation of IFRSs in relation to the independent variables for H1

Implementation of IFRS complex process	V1	V 2	%
Very high	10	14	12 %
High	19	24	21.5 %
Medium	27	36	31.5 %
Low	29	18	23.5 %
Very low	15	8	11.5 %
Total	100	100	100%

Source: *Author*

Whereas, the results of the Chi-square test are presented summarized in the following table:

Table 4. Chi-square test results for H1

RESULTS		
	V1	V2
Chi - Square statistic	39.3815	24.8348
p - value	.000091	.015625
Result at p<0.05	Significant- the variables are dependent and have an impact on each other	Significant- the variables are dependent and have an impact on each other

Source: *Author*

The testing of the dependence of the variables from the table above done through the Chi - Square test, shows that the level of implementation of IFRSs in Kosovo and the variables "IFRSs are complicated" and "IFRSs are frequently updated and there is no training sufficient" are interdependent and their dependence is also concluded through the result of the Chi-Square test, since the value of $p < 0.05$ in both cases.

From the achieved results, which are based on the answers received from the research questionnaire, we conclude that the H1 hypothesis has been confirmed "Frequent changes in IFRSs and lack of adequate training and explanations has made the financial reporting process complicated", as only 23% of respondents consider the implementation of IFRSs as a non-complex process and this is mainly due to the part of respondents who belonged to the profession of Auditor, in which case they are the only profession that has higher knowledge about IFRSs from their practice in previous work experiences.

H2- *The level of professional training of staff in the field of financial reporting is the main problem related to the implementation of IFRS.*

Table 5. Variables

V1 Education of accountants	Level of continuing professional education of accountants and lack of professional certifications
V2 The experience of accountants	Lack of work experience related to the application of IFRS

Source: *Author*

The summary of responses for each variable is presented in the table below:

Table 6. Implementation of IFRS in relation to the independent variables for H2

Implementation of IFRS complex process	V 1	V 2	%
Very high	26	28	27%
High	37	38	38%
Medium	18	16	17%
Low	13	13	13%
Very low	6	5	6%
Total	100	100	100%

Source: *Author*

The results of the Chi-square test are presented summarize in the following table:

Table 7. Chi-square test results for H2

	V1	V2
Chi - square statistic	77.2213	63.1591
p - value	.00001	.00001
Result at p<0.05	Significant- the variables are dependent and have an impact on each other	Significant- the variables are dependent and have an impact on each other

Source: *Author*

Testing the dependence of the variables from the above table done through the Chi - Square test shows that the dependent variable, is influenced by the "Level of Education" of the respondents, as well as the "interest and support of management for their implementation" and from this it can be concluded that there is dependence between variables since the value of $p < 0.05$ in both cases.

From the achieved results, which are based on the answers received from the research questionnaire, we conclude that hypothesis H2 has been confirmed "The level of professional training of staff in the field of financial reporting is the main problem in the implementation of IFRS in Kosovo", as over 65% of respondents rate professional trainings in relation to the level of implementation of IFRSs as a high problem.

5. Conclusion and recommendations

This transition from an accounting system based on local rules and practices to standards based on principles was a significant change but not a simple process for both professionals and regulators. The results of the work show that IFRS are complex, voluminous, not simple to practice, and their implementation requires certain knowledge by professionals and constant monitoring of their updating or changes. The findings of the paper show for some standards there is not enough knowledge on the part of professionals in this field and moreover there is a lack of specified training to explain and simplify these standards and accountants have nowhere to go to seek professional advice. From the data analysis it is concluded that the level of continuing professional education of accountants, lack of professional certification and lack of work experience related to the application of IFRS, staff in the field of accounting and financial reporting, were the main factors that have made the implementation of IFRS, a complex process. Regarding the lack of adequate training and explanations and simplifications of IFRS, we can say that it is an important factor in the implementation of IFRS, but not in level as high as the above factors.

5.1 Recommendations

The results of the paper can give some recommendations, which can serve professionals in the field of accounting and finance. The following recommendations may be used to facilitate the IFRS application process:

- The Kosovo Council for Financial Reporting (KCFR) as the responsible institution in this field together with professional associations should organize trainings and meetings with economic entities, in order to raise their awareness about the importance and benefits arising from the implementation of these standards.
- Organize regular and frequent trainings for professionals in the field of finance to facilitate the implementation of these standards and continuous professional development in this field.
- Universities and other educational institutions belonging to this field to start making agreements with economic units for the engagement of students for internships to see closely the implementation of IFRS so that the same professionals are ready for the market after graduation and to ease implementation of these standards, combining the theoretical part gained by the educational institution together with the necessary knowledge gained from practice.

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