Towards the development of a financial reporting framework for Sri Lankan SMEs

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ABSTRACT

The study has two objectives: to identify the users and their information needs of Sri Lankan small and medium enterprises (SMEs) financial information; and to examine the need for internationally comparable accounting information for Sri Lankan SMEs. The findings clarify issues with the current SME financial reporting standards and provide useful insights to assist in developing an appropriate reporting framework for Sri Lankan SMEs. An analysis of the literature reveals a paucity of empirical research on financial reporting by SMEs and little about the users and their financial information needs in the context of developing countries. No prior empirical research that examines the effects of adopting the International Financial Reporting Standard for Small and Medium Enterprises (*IFRS for SMEs*) in Sri Lanka was found to exist.

This thesis contributes to the literature, through applying a mixed methods approach. A questionnaire survey was used to collect data from 323 accountants and owners of SMEs. Quantitative data was analysed using a statistical package for social sciences. The responses are subdivided into three categories: small; medium and large SMEs to reveal differences according to size. Forty-one face-to-face semi-structured interviews were conducted with accountants and owners, bank lending officers, income tax officers, and representatives from government agencies, and the accounting standards setting authority of Sri Lanka. Follow-up interviews were conducted with the same group of interviewees to obtain their comments on a proposed financial reporting framework. Qualitative data was analysed using thematic analysis via the NVivo software. Institutional theory was adopted as the theoretical framework to study Sri Lanka's decision to adopt the *IFRS for SMEs*.

This decision was in response to institutional pressures rather than alleged benefits of internationally comparable financial information. Coercive institutional pressures are the most obvious which drove the adoption of *IFRS for SMEs* both at country and individual firm levels. SMEs do not see any need to provide internationally comparable accounting information due to their limited cross border activities. Many of the accounting topics included in the *IFRS for SMEs* appear to be irrelevant. The prime users of the financial information are owner-managers, banks, and the Inland Revenue Department. Government institutions are also users of financial information, particularly for the large SMEs. Users and their financial information needs vary according to the size of the SME. The results indicate that SME financial statements are unable to meet the needs of the main users. Tax oriented reporting, a lack of detail and a lack of up-to-date information are the main weaknesses in SME financial statements. Further, users indicate the existing financial reporting framework, based on general purpose financial reporting, is neither cost effective nor relevant to the diverse SME sector in Sri Lanka.

Based on the findings, a framework for Sri Lankan SME financial reporting is proposed, which includes four tiers. The proposed framework allows non-publicly accountable entities to determine the objective of their financial reporting and tailor their information to users' needs in a cost effective manner. These findings have implications, and recommendations for policy makers, and standard setters charged with developing and implementing an appropriate financial reporting framework for SMEs. The government and the local standard setters should pay greater attention to SME financial reporting and take steps to make it credible, relevant, and appropriate to the needs of users. The findings provide useful insights for developing countries, particularly the Asian countries where adoption of *IFRS for SMEs* is being considered.

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LIST OF ABBREVIATIONS

ADB	Asian Development Bank
ASEAN	Association of South East Asian Nations
CASL	Institute of Chartered Accountants of Sri Lanka
EU	European Union
FASB	Financial Accounting Standards Board (The United States)
GAAP	Generally Accepted Accounting Principles
GDP	Gross Domestic Product
IASB	International Accounting Standard Board
IASC	International Accounting Standard Committee
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
IFRS for SMEs	International Financial Reporting Standards for Small and Medium sized Entities
IMF	International Monetary Fund
LKR	Sri Lankan rupee
POBA	Professional Oversight Board For Accountancy
SD	Standard deviation
SLFRS for SMEs	Sri Lanka Accounting Standards for Small and Medium sized Entities
SME/SMEs	Small and Medium Enterprise(s)
SPSS	Statistical Package for Social Sciences
UK	United Kingdom
USA	United States of America
USD	US Dollar

CHAPTER ONE

RESEARCH INTRODUCTION

1.1 Introduction

This thesis develops a financial reporting framework for Sri Lankan small and medium sized entities (SMEs) by identifying users and their financial information needs and examining the need of internationally comparable financial information. SMEs play an economically significant role in most countries (Isaga, Masurel, & Van Montfort, 2015). For instance, within the European Union (EU), over 99 per cent of enterprises belong to the SME category (Kaya & Koch, 2015). Further, the economic importance of SMEs, especially in developing countries,[1] is widely documented (Islam, Rahman, & Ali, 2011; Rasool, Dars, & Shah, 2013).

In Sri Lanka, SMEs account for more than 90 per cent of the total number of industrial establishments (Department of Census and Statistics, 2013) and contribute 30 per cent to the country's Gross Domestic Product (GDP) (Ministry of Finance and Planning, 2013). In South Africa another developing country, Ramukumba (2014) estimates over 90 per cent of formal business entities are SMEs, and they account for over 50 per cent of GDP and 55 per cent of jobs. Similarly, in Pakistan and Bangladesh the SME sector comprises of more than 90 per cent of business entities (Islam et al., 2011; Rasool et al., 2013). Given the important role of SMEs in economic development, the survival and growth of SMEs is vital to the overall health of an economy. Any change in the financial reporting standards for SMEs could impose additional reporting burdens as many SMEs lack the capacity or resources to meet the requirements. Any financial reporting framework for SMEs therefore, needs to strike an appropriate balance between satisfying the information users' needs and reducing the reporting burden for SMEs.

[1] World Bank defines developing countries as those with "low income and middle income economies" (World Bank, 2015). The term *country*, is used interchangeably with *economy*. The term *developing country* is used interchangeably with *emerging country.*

This chapter is organised as follows: Section 1.2 presents a brief background to the thesis. Section 1.3 describes the research problem and the motivation for this research. Section 1.4 discusses the objectives and research questions of the thesis. Section 1.5 introduces the research methodology and methods adopted in this research. Section 1.6 describes the research contribution. Section 1.7 outlines the structure of the thesis and section 1.8 concludes the chapter.

1.2 Background of the thesis

It is claimed that SMEs require a simplified/differential accounting and financial reporting framework to alleviate unnecessary reporting burdens (Busuioc, 2011). This reporting framework should be appropriate for the size and types of transactions conducted by the SME, and the limited range of financial information required by users. The main argument for simplifying financial reporting requirements is because they are disproportionately affected by the costs resulting from requiring them to comply with the same financial reporting regulations as large entities (Eierle, 2008). Financial statements prepared under the full application of generally accepted accounting principles (GAAP) are suitable for the users of large companies whose shares are publicly traded and they are not appropriate for financial statement users of SMEs (Rennie & Senkow, 2009).

In their efforts to ease the financial reporting burden on SMEs, and to address the need for international comparability in the financial reporting of SMEs, the International Accounting Standard Board (IASB) [2] issued the International Financial Reporting Standards for Small and Medium-sized Entities (*IFRS for SMEs*) on July 9, 2009 (International Accounting Standards Board, 2009a). The accounting standard *IFRS for SMEs* is aimed at entities that publish general purpose financial reports and are not publicly accountable (International Accounting Standards Board, 2009b). The standard was developed as an alternative to the full

[2] The IASB was founded in 2001 and was preceded by the International Accounting Standards Committee (IASC) from 1973 to 2000. In this study, both bodies will be referred to as the IASB, and the term IFRS used when referring to any standards issued by either the IASC or the IASB.

International Financial Reporting Standards *(IFRS)*, which was created for financial reporting by large publicly accountable entities.

The IASB applied the same conceptual framework when developing the *IFRS for SMEs* (International Accounting Standards Board, 2004). The IASB argued that the information needs of users of SME financial statements were similar in most ways to those of users of publicly accountable entities' financial statements (International Accounting Standards Board, 2004). The content of the accounting standards for SMEs was therefore extracted from the *IFRS*, employing a so-called 'top-down approach'. This involved removing topics considered irrelevant to SMEs, and reducing the accounting options available. Currently, over 70 countries apply *IFRS for SMEs* or have plans to adopt this set of accounting standards in the near future (Kaya & Koch, 2015, p. 94). Sri Lanka did not modify the *IFRS for SMEs* and adopted them as Sri Lanka Accounting Standards for Small and Medium sized Entities (*SLFRS for SMEs*) (International Financial Reporting Standards Foundation, 2016). The implications resulting from the adoption and application of *IFRS for SMEs* in Sri Lanka is significant as more than 90 per cent of business entities are SMEs.

1.3 Research problem and motivation for the thesis

How the IASB developed the standard *IFRS for SMEs* has attracted opposition. A major criticism was the 'top down' approach using a framework that is biased towards large and/or listed companies (Devi & Samujh, 2014; Di Pietra et al., 2008; Evans et al., 2005). Unlike large entities, SMEs are more likely to focus on survival than on growth and profit maximisation (Hasle, Limborg, Kallehave, Klitgaard, & Andersen, 2012; Samujh, 2011). Additionally, the separation of ownership and control is not common in the majority of SMEs (Carsberg, Page, Sindall, & Waring, 1985) and most of them are formed and operated as family businesses (Fox, Nilakant, & Hamilton, 1996; Motwani, Levenburg, Schwarz, & Blankson, 2006; Tatoglu, Kula, & Glaister, 2008). It is claimed that SMEs have fewer financial statement users with different information needs when compared to large entity information users (Di Pietra et al., 2008; Evans et al., 2005). Additionally, it is difficult to design a single standard that is useful for the heterogeneous group of

SMEs (Di Pietra et al., 2008; Eierle & Haller, 2009; Evans et al., 2005). Thus, a critical question arises: Are the primary users of SME financial information the same as the users of financial information provided by large entities?

Although most researchers identify owner-managers and taxation authorities as the main users of the financial statements of SMEs, the IASB identifies the users of SMEs' financial statements as non-manager owners, credit rating agencies, lenders, suppliers, other creditors, and employees (International Accounting Standards Board, 2009b). The list of financial statements' users identified by the IASB is consistent with its 1989 conceptual framework for the preparation and presentation of financial statements. However, the IASB's revised conceptual framework for financial reporting, issued in 2010, identifies the primary users of financial statements as capital providers, potential investors, and creditors. The users such as owner-managers and the tax authority are thereby excluded from the target audience. In this context, Schiebel (2008) argues that the IASB did not undertake worldwide empirical analyses to identify users and their SME financial reporting needs. As Schiebel (2008, p. 2) explains, "International research is essential. Otherwise it will be a matter of luck whether an *IFRS for SMEs* meets the common information needs of its targeted users".

In addition to these concerns, the IASB's project on *IFRS for SMEs* has been criticised for a lack of input from developing countries in the discussions leading to the formulation of the standard (Bohušová & Blašková, 2012; Chand & Cummings, 2008; Devi & Samujh, 2014; Singh & Newberry, 2009). The summary of submissions to the Exposure Draft on the *IFRS for SMEs* shows that a substantial number of responses were received from the United Kingdom and Germany (Bohušová & Blašková, 2012; Singh & Newberry, 2009). No responses were provided by users of SME financial information, the intended recipients of reports prepared under the *IFRS for SMEs*. Following a study of comment letters from 1995 to 2007, Jorissen, Lybaert, Orens, and van der Tas (2013) claim the opinions the IASB received were biased. They call for more research to investigate the position of the different users who are not always directly involved in formal lobby activities.

The director of the *IFRS for SME* project did however, establish an informal user panel to obtain comments from users (Ram & Newberry, 2013). The panel membership was criticised by some board members of IASB as they were investment and security analysts who dealt mostly with large entities and therefore were not appropriate individuals to comment on SMEs (Ram & Newberry, 2013). Without SME voice on the panel, particularly from developing countries, the *IFRS for SMEs* does not have representation from the international SME community and lacks input from developing countries. Its adoption therefore, could result in undesirable consequences.

Developing and developed countries are not a homogeneous group. Differences exist in, for example, legal systems, taxation, sources of finance, inflation, political ties, colonial history, and culture, shape diversity in accounting practices (Doupnik & Salter, 1995; Evans, 2004; Jaggi & Low, 2000; Nobes, 1998; Richardson, 2007). These contextual factors are deeply embedded in the accounting environment of a country. As such, they may not be simply changed. They could therefore, act as an impediment to adoption of the *IFRS* across countries (Poudel, Hellmann, & Perera, 2014). Additionally, social, political, economic, and cultural factors influence accountants' professional judgment, and these differences across countries may lead to inconsistent interpretation and application of *IFRS* (Poudel et al., 2014). The needs of users of financial statements of SMEs in developing (or emerging) economies may be very different from the needs of users in developed economies. In this context, Hussain, Chand, and Rani (2012, p. 116) argue:

> … careful consideration must be given in deciding whether the full set of IFRS for SMEs should be adopted by emerging economies, or should they use IFRS for SMEs as a reference point in developing their own standards or should such economies adopt IFRS for SMEs with modifications to suit their reporting needs. For that reason, it is advisable for regulatory bodies in emerging economies to give considerable thought to the adoption of IFRS for SMEs and engage in wider consultations before deciding on the matter.

Uyar and Güngörmüş (2013, p. 86) similarly contend:

> … more studies on *IFRS for SMEs* are needed in developing countries since they may provide different feedback for future directions. Besides, differences in the views of jurisdictions, who

> have or have not adopted, might be examined to learn their perceptions. Such studies enable voicing of satisfactions or concerns which may guide standard setters for future revisions.

Research on *IFRS for SMEs* has tended to focus on the views of SME accountants about implementation issues, knowledge of *IFRS for SMEs*, and cost benefit considerations (see for example: Aboagye-Otchere & Agbeibor, 2012; Chand, Patel, & White, 2015; Devi & Samujh, 2014, 2015; Eierle & Haller, 2009; Kiliç, Uyar, & Ataman, 2016; Laing, 2012; Neag, 2010; Perera & Chand, 2015; Uyar & Güngörmüş, 2013; Van Wyk & Rossouw, 2009). Although a number of studies have been oriented towards the issues of the adoption of *IFRS for SMEs*, there are gaps in the literature about the need of internationally comparable accounting information for SMEs. Comprehensive evidence is missing on the relevance of accounting topics included in and costs and benefits of the *IFRS for SMEs*. There appears to be a dearth of literature on the subject in developing and Asian countries and Sri Lanka in particular. Most of the existing studies surveyed a narrow range of users. They omit the views of users such as bank lending officers and income tax officers on the need for internationally comparable accounting standards for SMEs.

An analysis of the literature shows a diversity of findings regarding SME users and their uses of financial information in developed countries. To date, there has been limited research on financial reporting by SMEs and even less is known about the users and their SME financial information needs in the context of developing countries. There is a lack of empirical research to ascertain who are the users of SME financial information and their information needs (Evans et al., 2005; Sian & Roberts, 2006). According to Evans et al. (2005), the main problem for regulators is the significant gap in the literature on the users of SME financial statements. Therefore, they recommended that, "before progressing with the project *IFRS for SMEs*, the IASB should initiate a research to determine to what extent the needs of owner-managers and other users of SME financial statements differ between larger versus the smallest SMEs" (Evans et al., 2005, p. 38).

1.4 Research objectives and questions

Sri Lanka adopted the accounting standard *IFRS for SMEs* without making any modifications to suit the local SME needs. Consequently, excessive reporting burdens arising from the imposition of an unmodified version of *IFRS for SMEs* could impede the growth of SMEs and in turn limit their ability to make full contributions to the country's economy. It is noted that some developed countries, such as the New Zealand and Australia, are not considering adopting the standard *IFRS for SMEs* (Devi & Samujh, 2014). Many SMEs in Australia and New Zealand are not required to prepare general purpose financial statements. Rather, they prepare special purpose financial reports that comply with taxation regulations developed locally to meet the reporting needs of SMEs in these countries (Devi & Samujh, 2014). Similarly, the formulation of a financial reporting framework that can meet the reporting needs of Sri Lankan SMEs could benefit SMEs and the Sri Lankan economy.

Therefore, the objectives of this thesis are to identify Sri Lankan SME users and their financial information needs and to examine the need for internationally comparable accounting information for SMEs. Hence, the following research questions are posed to achieve the objectives of the thesis:

1. How do Sri Lankan users and their financial information needs differ with regard to size of SMEs?
2. Do Sri Lankan SMEs need internationally comparable financial information?

Findings from these two questions are then used to develop a proposed financial reporting framework for Sri Lankan SMEs.

1.5 Research methodology, methods and theory

This thesis implements the pragmatist paradigm using a mixed method approach. It incorporates both qualitative and quantitative methods for data collection to identify the users of SME financial information and their financial information needs as well as their perceptions of the accounting standard *IFRS for SMEs*. This thesis adopts a quantitative method, using a questionnaire survey, to collect data from accountants and owners of SMEs in Sri Lanka.

Face to face semi-structured interviews, with a sample of accountants and owners of SMEs, bank lending officers, tax officers, government agencies personnel, and accounting standards setting authority representatives in Sri Lanka provide qualitative data. The interviews provided in-depth perspectives of the phenomena being studied from a sample of users not usually surveyed in studies reported in the literature. The collective outcome of both types of data (i.e. quantitative and qualitative) was used to develop a financial reporting framework for Sri Lankan SMEs. Follow-up interviews were conducted with the same groups of interviewees to obtain their comments on the proposed financial reporting framework.

The quantitative data gathered from the questionnaire survey was analysed using the statistical package for social sciences (SPSS). Qualitative data gathered from the questionnaire survey and the interviews were analysed using thematic analysis. NVivo software was used to organise and manage qualitative data. The New Institutional Sociology, provided the theoretical framework to examine the decision to adopt the accounting standard *IFRS for SMEs* in Sri Lanka.

1.6 Contributions of the thesis

The literature on users and uses of SME financial statements is informed by a small number of studies. Most of the studies (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Dang-Duc, Marriott, & Marriott, 2006; Maingot & Zeghal, 2006; Page, 1984) were undertaken more than ten years ago, thus their findings are dated. Notably, research on SME financial reporting in the developing countries is limited. In addition, Di Pietra et al. (2008), Evans et al. (2005), and Sian and Roberts (2009) identify significant gaps in the research literature on SMEs. They conclude that there is a lack of clarity about the users and uses of SME financial information. This is an under-researched area and, the views of user groups such as the bank lending officers, income tax officers, and representatives from the government institutions have largely been ignored. This thesis fills a gap by obtaining views of SME owners and accountants, bank lending officers, income tax officers, and representatives from government institutions to identify users and their financial information needs of SMEs in Sri Lanka, a developing country. The empirical research that examines the effects of adopting the *IFRS for SMEs* in developing countries in Asia is scarce. There has been no such research in Sri Lanka.

Criticisms expressed at the discussion paper and exposure draft stage included an absence of research on the suitability of the standard from a users' perspectives (see for example: Aboagye-Otchere & Agbeibor, 2012; Albu, Albu, & Fekete, 2010; Di Pietra et al., 2008; Evans et al., 2005; Schiebel, 2008). An extensive literature search has been unable to identify any studies devoted to assess the suitability of the accounting standard *IFRS for SMEs* from a users' perspectives. Therefore, this thesis will attempt to fill this gap in the literature by investigating SME users' perceptions to the accounting standard *IFRS for SMEs*, in the context of a developing country, Sri Lanka.

There are considerable gaps in the available literature regarding the *IFRS for SMEs*. First, there is a lack of empirical research concerning the need for internationally comparable financial reporting information for SMEs. Second, comprehensive evidence is missing regarding the relevance of accounting topics addressed in the *IFRS for SMEs*. Third, there is a lack of empirical evidence on the specific costs and benefits of preparing financial information in accordance with *IFRS for SMEs*. There have been calls by Chand et al. (2015), Uyar and Güngörmüş (2013), and Devi and Samujh (2015) for additional research in developing country contexts.

The thesis's findings in terms of what users require from small and medium enterprise financial information will contribute to the development of a users' need financial reporting framework for small and medium enterprises. The proposed financial reporting framework developed from the findings of this thesis would direct the Institute of Chartered Accountants of Sri Lanka (CASL) in revising current financial reporting framework for Sri Lankan SMEs. In addition, standards setters in other developing countries in general can gain useful insights into what constitutes an appropriate financial reporting framework for small and medium enterprises, based on user needs.

Findings from Sri Lankan SMEs, as a representative of developing countries, enhance the IASB's views of the effects and future revisions of the *IFRS for SMEs*. Results provide useful insight on types of SMEs that are likely to benefit from an international accounting standards. Findings of the thesis are informative to other developing countries in determining the need for a global accounting standards for

SMEs and the relevance of the content of the *IFRS for SMEs*. Further, current thesis provides empirical evidence that informs the debate regarding the relevance of international financial reporting standards for SMEs.

This thesis also provides useful material for researchers/academics with an interest in international accounting research in general, as there is a dearth of studies and research regarding the users of SME financial information and effects of *IFRS for SMEs*. Finally, as this thesis integrates both quantitative and qualitative approaches within one thesis, it provides deeper insight into SME financial reporting.

1.7 Outline of the thesis

The thesis is presented in twelve chapters as follows.

Chapter 1 introduces the background and motivation for the thesis. It is followed by an overview of the research objectives, questions, research methodology and methods and contribution of the thesis. Finally, an outline of the thesis is given.

Chapter 2 locates Sri Lanka as the research context and provides contextual understanding about the research field. It discusses the significance of SMEs in the Sri Lankan economy and describes the country's financial reporting environment.

Chapter 3 reviews and analyses the literature on financial reporting in the context of SMEs. The discussion focuses primarily on two main issues: the users and uses of SME financial information; and the current financial reporting frameworks in a selected number of jurisdictions.

Chapter 4 discusses and analyses the literature that relates to the development of the *IFRS for SMEs*, and the subsequent research literature on the *IFRS for SMEs*.

Chapter 5 conveys the theoretical lens used to analyse the research findings.

Chapter 6 explains the research approach adopted in this thesis. It sets out the philosophical views underpinning the thesis, and provides justification for using a mixed methods research design.

Chapter 7 details the data collection methods, the sample selection strategies, and the data analysis methods.

Chapter 8 exhibits the results from the questionnaire survey of accountants and owners of SMEs. It includes the findings from the analysis of data using SPSS.

Chapter 9 presents the data analysis of the qualitative data collected through the open-ended questions in the questionnaire survey and semi-structured interviews.

Chapter 10 discusses the results from the questionnaire survey and the interviews and presents the key findings.

Chapter 11 develops a financial reporting framework for Sri Lankan SMEs incorporating the findings as discussed in chapter 10.

Chapter 12 summarises the research. The implications and limitations of the thesis are presented and directions for future research are recommended. This chapter concludes the thesis.

1.8 Summary

This chapter provided an introduction, and background to the thesis. The research problem was outlined and followed by the research objectives. The research methodology and methods were introduced. This was followed by the motivation driving the research and the contribution of the thesis were briefly discussed, relating to prior studies and Sri Lankan context. An overview of the structure of the thesis concluded the chapter. The next chapter discusses the Sri Lankan context in which financial reporting operates.

CHAPTER TWO

THE SRI LANKAN CONTEXT

2.1 Introduction

The purpose of this chapter is to provide the background necessary for understanding the characteristics of the environment in which financial reporting operates in Sri Lanka. This basic understanding is important, particularly for assessing the relevance of the accounting standard, *IFRS for SMEs* to a developing country, Sri Lanka. Given that the main objective of this thesis is to provide useful insights for developing the financial reporting framework for Sri Lankan SMEs, the contextual understanding is vital for assessing and modifying the existing financial reporting framework for Sri Lankan SMEs.

Evidence suggests that financial reporting practices are affected by and could be explained by a number of environmental factors such as: a country's particular colonial history or stage of economic development; historical; socioeconomic; legal; political; professional; cultural; language; and religious settings (Devi & Samujh, 2015; Doupnik & Richter, 2003, 2004; Doupnik & Salter, 1995; Evans, 2004; Jaggi & Low, 2000; Joshi, Yapa, & Kraal, 2016; Kiliç et al., 2016; Kraal, Yapa, & Joshi, 2015; Nobes, 1998; Poudel et al., 2014; Richardson, 2007). These environmental factors differ greatly from country to country, especially between developed and developing countries (An & Sharma, 2015; Briston, 1978; Chand et al., 2015; Perera, 1989; Samuels & Oliga, 1982). For this reason, "practises that have worked in developed countries will not necessarily work in a developing country because the culture and needs differ" (An & Sharma, 2015, p. 377). Developing countries have a much broader assortment of economic and social indicators than do developed countries (Chamisa, 2000).

It was said that "less developed countries are relatively distinctive as they have a larger residue of traditional cultures, their poverty renders them more dependent on external finance, ideologies and structural reforms, with lower institutional capacity to deliver change" (Graham, Hopper, Tsamenyi, Uddin, & Wickramasinghe, 2009, p. 496). Further, the relevance of the *IFRS* to developing countries has also been questioned on the ground that national environments in developing countries are different from those of developed countries where the *IFRS* originated (Briston, 1978; Perera, 1989; Samuels & Oliga, 1982). Samuels and Oliga (1982, p. 69) articulate this argument as follows:

> … where economic, socio-political, cultural, and contextual differences between countries, nations, or societies exist, the problem of appropriate accounting standards will assume a different conceptual meaning as well as contextual significance …. in the case of developing countries where such differences tend to be not only highly pronounced, but also in a highly dynamic and fluid state, the relevance of international accounting standards becomes even more questionable.

Similarly, Nurunnabi (2015) establishes that socio-cultural factors present a critical deterrent when implementing the *IFRS* in developing countries. Additionally, it is well documented that professional judgements are applied inconsistently across countries, particularly in countries where accounting environments differ from those in Anglo-American countries where the *IFRS* were developed (Doupnik & Richter, 2003, 2004; Poudel et al., 2014).

This chapter provides an overview of the context in which financial reporting operates in Sri Lanka. Section 2.2 provides a discussion of historical, religious, and cultural settings in Sri Lanka. Sections 2.3 and 2.4 describe Sri Lanka's legal and political environment and the economic and social environment of Sri Lanka respectively. Section 2.5 describes the SME sector in Sri Lanka. Section 2.6, explains the financial reporting environment. Section 2.7 outlines the *IFRS* adoption in Sri Lanka. Section 2.8 concludes the chapter.

2.2 Historical, religious and cultural environment in Sri Lanka

Sri Lanka is a tropical island nation with a total land area of 65,610 square kilometres. It is located in the Indian Ocean close to the southern part of India. Sri Lanka's population was 20.4 million, with a population density of 324 persons per sq km in 2012 (Central Bank of Sri Lanka, 2013). Population density in Sri Lanka is one of the highest in the world (United Nations Educational Scientific and Cultural Organisation, 2013).

Sri Lanka has a rich historical and cultural heritage covering more than 2,500 years (Daskon & Binns, 2010). The most formative event in Sri Lanka's long history was the arrival of Buddhism in the 3rd century BCE (Rajapakse, 2003). According to the Mahavamsa,[3] one of the traditional chronicles of early Sri Lankan history, Buddhism was brought by Bhikkhu Mahinda. Bhikkhu Mahinda is believed to have been the son of the Mauryan emperor Ashoka.[4] Mahinda's mission won over the Sinhalese monarch Devanampiya Tissa[5] (Rajapakse, 2003). Devanampiya Tissa embraced Buddhism and propagated it throughout the Sinhalese population (Rajapakse, 2003). He established the monastery of Mahavihara, which became the historic centre of Theravada Buddhism. The Buddhist kingdoms of Sri Lanka maintained a large number of Buddhist schools and monasteries, and supported the propagation of Buddhism into Southeast Asia. However, the Buddhist-Sinhalese civilization and institutions in Sri Lanka came under attack during the colonial eras of the Portuguese, the Dutch, and the British.

Colonial rule in Sri Lanka began with the Portuguese in 1505. They ruled the maritime provinces of the country for 153 years (Wickramasinghe, 2006). The Dutch conquered the areas that were under the Portuguese and continued colonial rule for a further 140 years (Yogasundram, 2008). In 1796, the country was taken over by the British who created the Crown Colony of Ceylon. Sri Lanka obtained political independence from the British in 1948 (De Silva, 2005). In 1972, the

[3] The Mahavamsa, the great chronicle of Sri Lanka, is the epic tale of Sri Lanka's founding and early history.

[4]Ashoka, is the last major emperor in the Mauryan dynasty of India. His patronage of Buddhism during his reign furthered the expansion of that religion throughout India. He sent his only daughter Sanghamitra and son Mahinda to spread Buddhism in Sri Lanka.

[5] King Devanampiya Tissa was one of the earliest rulers of Sri Lanka based at the ancient capital of Anuradhapura from 307 BCE to 267 BCE. His reign was notable for the arrival of Buddhism in Sri Lanka under the aegis of Mauryan Emperor Ashoka.

country became a Republic within the Commonwealth, and its name was changed to Sri Lanka.

The periods of colonisation impacted the Sri Lankan ethnic mix, religious mix, and cultural values. For example, during the Portuguese era, a large number of people in the coastal areas were converted to Roman Catholicism (Wickramasinghe, 2006). After the Portuguese were expelled, the Dutch encouraged conversion to Protestantism from both Roman Catholicism and the traditional religions of the island. As a result, many in the low country converted to obtain Dutch favour (Wickramasinghe, 2006). At the beginning of 19^{th} century, the British brought 900,000 Tamil labourers from South India to work the plantations (De Silva, 2005). This mass scale immigration created enormous change in the ethnic mix of the country. As a result of its history, Sri Lanka is a multi-ethnic, multi-religious, and multi-lingual country.

The main ethnic groups are the Sinhalese, Tamils and Muslims. The largest ethnic group, the Sinhalese compose 73.9 per cent of the population. The largest minority group, the Sri Lankan Tamils, compose 12.7 per cent of the population. The Indian Tamils, who were brought to Sri Lanka under British colonialism to work on the tea plantations in the central hills, comprise 5.5 per cent, and Muslims 7.1 per cent of the population. Other small communities are the Burghers, (of Portuguese and Dutch descent), and the Veddas, who were the original indigenous inhabitants of Sri Lanka who together make up 0.8 per cent of the total population (Central Bank of Sri Lanka, 2012a).

Buddhism represents the largest religious affiliation, with 69.3 per cent of the population, while Hinduism and Islam are practised by 15.5 per cent and 7.6 per cent of the population respectively. Christianity is practised by 7.6 per cent of the population (Central Bank of Sri Lanka, 2012a). Linguistically, the Sinhalese speak the Sinhala language, while Tamils and Muslims speak Tamil. English is spoken by a small percentage within most communities. Sinhala and Tamil are the official languages in Sri Lanka. The language of most of the government organisations and SMEs is Sinhala. Multinational companies and most listed companies use English, the language used by the IASB for publishing their views, declarations, decisions, discussions and standards.

Sri Lankan society is structured along steep hierarchies based on caste, class, generation, sex, as well as on wealth and power (Marecek, 1998). The society accepts hierarchy. Consequently, those at the upper levels are powerful and enjoy privileges. As a result, people do not usually question authority. Silence is a signifier of respect for one's superiors (Marecek, 1998).

2.3 Legal and political environment in Sri Lanka

The legal system of Sri Lanka is made up of English common law, Roman-Dutch law, Tesawalamai law, and Kandyan law. This complex mixture of legal systems reflects the history of the country. English principles have been adopted for criminal law, mercantile law, and the Law of Evidence (Chandrakumara & Budhwar, 2005). The Laws of Persons, Property, Succession, Contracts, and Torts are fundamentally Roman-Dutch law modified by statute and English law incorporated through judicial decisions (Chandrakumara & Budhwar, 2005). English legal principles apply to contracts, copyrights, patents and trademarks, and insurance.

Kandyan law is a system of law based on the age-old customs prevailing among the Sinhalese. Today it is the customary law applicable to Kandyan Sinhalese. The main customary areas relevant to this law are marriage, divorce, and property (Chandrakumara & Budhwar, 2005). Tesawalamai is the customary law applicable to the Tamil inhabitants of Jaffna, an administrative district in north Sri Lanka. This law have evolved from the ancient Tamil customs of India (Chandrakumara & Budhwar, 2005).

The Second Republican Constitution of 1978 broke with Westminster tradition and introduced a strong Executive Presidency. The constitution vests extensive powers in the office of the President. The President is the head of the Government and the Commander-in-Chief of Armed Forces. He appoints the prime minister, the cabinet, and personnel to staff the most important positions in the military, judiciary, and various Ministries. Both the President and Parliament are elected every six years. Two parties, the conservative United National Party and the leftist Sri Lanka

Freedom Party have alternated in government since independence in 1948. Sri Lanka's political parties are structured and managed in a top-down, hierarchical manner that does not allow party members to influence decision-making (Transparency International Sri Lanka, 2011). Rather than representing social diversity and citizens' aspirations, political parties are alliances for elite power-sharing.

Most of the important positions in the government are filled by close relatives of ministers and relatives of those in power. This is not based on merit but rather on self-interest. This may contribute to the widespread corruption and fraud which exists in Sri Lanka (Transparency International, 2013). Indeed, Sri Lanka is ranked 91 out of 175 countries on the corruption perception index in 2013 (Transparency International, 2013). According to Transparency International, corruption is a serious problem threatening democratic and economic development in Sri Lanka. High tolerance of corruption, non-sanctioning of corrupt behaviour, and a culture that tends not to question authority, provide an environment in which corruption can flourish (Transparency International Sri Lanka, 2011). This corruption in Sri Lanka is closely linked to inadequate legal and institutional frameworks (Freedom House, 2013).

2.4 Economic and social environment in Sri Lanka

Sri Lanka was mainly an agricultural country at the time of independence in 1948. The contribution of the agricultural sector to the economy and the number of people who were engaged in the agricultural sector declined only slightly between 1948 and 1977 (Kelegama, 2006). Before 1977, the economy was inward looking, with strict trade and financial sector controls that included high import restrictions and exchange controls. These controls created economic problems, such as a high budget deficit, a balance-of-payments crisis, a low economic growth rate and high unemployment levels (Kelegama, 2006).

In 1977, Sri Lanka introduced open economic policies and adopted a market oriented approach (Central Bank of Sri Lanka, 2012b). The economic policies during this period were directed towards industrialisation, private sector participation in economic activities, and institutional reforms in the public sector

(Kelegama, 2006). Textiles and apparel, food and beverages, telecommunications, insurance, and banking and other financial service sectors became the most dynamic sectors of the country's economy (Kelegama, 2006).

However, the economy of Sri Lanka and the life of its people were affected by two major events. The first event, was the prolonged civil war[6] that started in the early 1980s. According to the World Bank (2013), there were 77,832 war-related deaths between 1980 and 2008. The total economic cost of the 26-year war was estimated at US$200 billion (Athukorala, 2010). In May 2009, the Government of Sri Lanka declared victory and the civil war ended. This created hopes of peace and stability. The second event, was the Indian Ocean tsunami in December 2004. The Indian Ocean tsunami brought the largest natural disaster to the country in its recorded history (United Nations Development Programme, 2012). More than 35,000 people died, 100,000 houses were damaged, and 500,000 people were displaced (Harsha, Samarawickrama, & Imamura, 2007). The severe damage caused to the infrastructure and the environment exceeded US$900 million (Harsha et al., 2007).

In spite of these events, Sri Lanka has experienced rapid economic growth (United Nations Development Programme, 2012). The economy has seen robust annual growth of 6.4 per cent over the period 2003 to 2012. This growth is well above that of its regional peers (World Bank, 2014). The macroeconomic indicators show positive trends in economic and social performance during the last 5 years (Central Bank of Sri Lanka, 2013). Table 1 illustrates key economic indicators of the Sri Lankan economy for the period 2009 - 2013.

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[6] The civil war waged between the government of Sri Lanka and a separatist guerrilla group from 1983 to 2009. The guerrillas attempted to break off the northern and eastern regions of the country as a separate sovereign state. The terror attacks were directed towards destroying government-owned infrastructure such as roads, rail, airports, and seaports. The effect of terror activities was felt outside the north and east regions of the country, with separatist guerrillas detonating bombs in other regions of the country to destroy government-owned property and human life (Abeysekera, 2011).

Table 1: Key economic indicators of the Sri Lankan economy for the period 2009-2013

Economic indicator	**2009**	**2010**	**2011**	**2012**	**2013**
Real GDP growth (%)	3.5	8.0	8.2	6.3	7.3
GDP by sectors (%)					
Agriculture	12.0	11.9	11.2	11.1	10.8
Industry	28.6	28.7	29.3	30.4	31.1
Services	59.3	59.3	59.5	58.6	58.1
Per capita GDP (US $)	2,057	2,400	2,836	2,922	3,280
Unemployment as a % of labour force	5.8	4.9	4.2	4.0	4.4
Inflation rate	3.5	6.2	6.7	7.6	6.9
Export (US $ Mn)	7,085	8,626	10,559	9,774	10,394
Imports (US$ Mn)	10,207	13,451	20,269	19,190	18,003
Public debt as a % of GDP	86.2	81.9	78.5	79.2	78.3

Source: Central Bank of Sri Lanka (2013)

Sri Lanka has Gross Domestic Product (GDP) of US$67.2 billion (Central Bank of Sri Lanka, 2013). The GDP growth rate has averaged close to 7 per cent per annum over the past 5 years. In 2011, Sri Lanka recorded its highest growth rate since independence of 8.2 per cent with the major contribution coming from an increase in the industry and service sectors (Central Bank of Sri Lanka, 2013). The industrial sector's total contribution to the GDP was 31.1 per cent in 2013. The services sector, where wholesale and retail trade, transport and communication and banking, insurance and real estate play a major role, contributed 58.1 per cent of GDP in 2013. Agriculture, which was the mainstay of the economy when the country gained its independence and accounted for 40 per cent of GDP, has decreased in relative importance over the years. By 2013, the agriculture sector accounted for only 10.8 per cent of GDP.

Between 2009 and 2013, the per capita income of the country increased from US$2,057 to US$3,280. This growing trend in per capita income supports the country's rising economic status as a middle-income country (Dutz & O'Connell, 2013). As a result the World Bank has listed Sri Lanka as a lower-middle income developing country (World Bank, 2014). Other economic indicators such as a one-digit inflation rate and a low unemployment rate over the past 5 years are also favourable (Central Bank of Sri Lanka, 2013). However, the exchange rate continues to show an unstable continuous decline due to a negative foreign trade balance, unfavourable world economic conditions, and continuous increases in the price of crude oil (Central Bank of Sri Lanka, 2013). Rising oil prices and the 30-year long civil war have also contributed to Sri Lanka's high public debt (78 per cent of GDP in 2013).

Sri Lanka is a recipient of large amounts of foreign assistance from the World Bank, the International Monetary Fund (IMF), the Asian Development Bank, China and Japan (U.S. Department of State, 2011). The World Bank has been providing financial assistance to Sri Lanka for close on six decades (World Bank, 2005, 2017). The current active World Bank portfolio comprises of 18 projects with a total net commitment value of US$2.1 billion (World Bank, 2017). Sri Lanka has a 3-year Extended Fund Facility program with the IMF, which is primarily focused on reducing fiscal deficit, rebuilding foreign exchange reserves, and introducing a simpler, more equitable tax system to restore macroeconomic stability and promote inclusive growth (International Monetary Fund, 2017). These financial aid packages however, come with conditions as requirements of the loans. For example, the IMF announced that the second review reached a staff-level agreement with Sri Lankan authorities subject to submission of a new Inland Revenue Act to the Parliament by June 2017 (World Bank, 2017). The United States of America, United Kingdom, other European countries (Germany, Italy, Belgium, Netherland and France), and India are the main destinations for Sri Lankan exports. China, India, Singapore, United Arab Emirates and Japan are the main origins of Sri Lanka imports (Central Bank of Sri Lanka, 2017).

Sri Lanka ranks high on the Physical Quality of Life Index and the Human Development Index. In 2012, Sri Lanka was ranked 92 in the Human Development Index[7] and grouped in the high human development category (United Nations Development Programme, 2013). In comparison with other developing countries, Sri Lanka had a literacy rate of 95.6 per cent and a high life expectancy of 75.1 years in 2012 (Central Bank of Sri Lanka, 2013). These quality of life indices reflect

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[7] This classification is based upon the island's indicators of life expectancy (75.1 years); mean years of schooling (9.3) in association with expected years of schooling (12.7); and its per capita gross national income at purchasing power parity (US$5,170).

sustained government intervention in the health and the education sectors (Wijewardena & Yapa, 1998).

2.5 SME sector in Sri Lanka

SMEs make up a large part of the Sri Lankan economy (Wickramasinghe, 2015). The SME sector is recognised as an important sector in the country for generating high economic growth, and reducing unemployment, inequity, and poverty (Department of Census and Statistics, 2015). Sri Lankan SMEs are engaged in a wide range of business activities in agriculture, mining, fisheries, industry/manufacturing, construction, tourism and services in rural, urban and estate settings (Department of Census and Statistics, 2015). Most Sri Lankan SMEs are one-person entities or are run by a family, with friends or a business partner (Dasanayaka, 2011). Sole ownership is the dominant legal status in SMEs in Sri Lanka (Department of Census and Statistics, 2015).

SMEs contribute 30 per cent to the GDP, 35 per cent of employment, 30 per cent of manufacturing activities, and 20 per cent of exports (Ministry of Finance and Planning, 2013). The most recent industrial survey statistics on industrial survey dates back to 2010. This offers a useful framework for analysing the contribution of industrial enterprises to the national economy in Sri Lanka. Table 2 shows the principal indicators of industrial activity, classified by the major industry division. The scope of this annual industrial survey is to categorise all activities under three industry divisions of the international standard industrial classification of the United Nations (Department of Census and Statistics, 2013), namely, Mining and Quarrying, Manufacturing and Generation and Distribution of Electricity, Gas and water.

Table 2: Principal indicators of industrial activity classified by major industry division

Industry Sector and Persons engaged size class		Number of Establishments		Number of Employees		Value of Output	
		No.	%	No.	%	Rs. '000	%
Mining & Quarrying	5 to 9	1,666	84	11,632	57	3,571,207	41
	10 to 19	266	13	3,248	16	1,097,591	13
	20 to 39	24	1	573	3	244,982	3
	40 to 99	16	1	808	4	980,994	11
	100 & above	10	1	4,268	21	2,814,228	32
	Group Total	**1,982**	**100**	**20,529**	**100**	**8,709,002**	**100**
Manufacturing	5 to 9	10,484	64	70,770	11	109,503,604	7
	10 to 19	2,732	17	36,292	5	49,757,205	3
	20 to 39	885	5	24,481	4	63,740,871	4
	40 to 99	1,192	7	77,232	11	220,214,928	14
	100 & above	1,022	6	464,573	69	1,180,588,617	73
	Group Total	**16,315**	**100**	**673,348**	**100**	**1,623,805,225**	**100**
Electricity, Gas and Water	5 to 9	17	37	109	0.4	82,115	0.1
	10 to 19	13	28	167	0.7	541,648	0.4
	20 to 39	7	15	191	0.8	800,503	0.6
	40 to 99	6	13	353	1.4	1,930,071	1.4
	100 & above	3	7	24,627	96.8	133,493,313	97.5
	Group Total	**46**	**100**	**25,447**	**100**	**136,847,650**	**100**
Total		**18,343**		**719,324**		**1,769,361,877**	

Source: Department of Census and Statistics (2013)

The industrial survey does not include establishments with fewer than five employees. This is in line with the definition[8] adopted for this study, all industrial establishments with more than four and fewer than 100 employees, are categorised as SMEs. They account for more than 90 per cent of the total number of industrial establishments in all three industry divisions. However, their contribution to employment and value of output is low in the categories of Manufacturing, and Electricity, Gas, and Water. For Mining and Quarrying, the SME sector accounts for 99 per cent of the total number of establishments, which in turn, contribute to 79 per cent of total employment and 68 per cent of total value of output.

[8] For the data collection purposes of this study, SMEs have been defined as entities that employed between 5-99 employees.

The majority of establishments in the manufacturing sector fall under the category of SMEs (94%). However, their contribution to the value of output is low (about 27%). Conversely, the large establishments in the category of Manufacturing account for more than 73 per cent of value of output. For Electricity, Gas and Water, a similar conclusion can be drawn. Although there are a significant number of SMEs in Sri Lanka, the contributions from Manufacturing and Electricity, and Gas and Water to the national economy, in terms of output and share in employment, has been low.

Recognising the importance of the SME sector, the Sri Lankan government formulated a national policy framework for SME development in 2015 (Ministry of Industry and Commerce, 2015). This policy framework sets out the direction, the challenges to be addressed, and the broad intervention strategies. The major policy intervention areas are identified in six core areas namely: environment, modern appropriate technology, entrepreneurial culture and skills development, access to finance, market facilitation and research and development (Ministry of Industry and Commerce, 2015).

The institutional support for SMEs in Sri Lanka is mainly provided by the public sector, financial institutions, Chambers of Commerce, non-government organisations (NGOs), and multilateral and bilateral donor agencies. SMEs fall under the responsibility of the Ministry of Industry and Commerce while other ministries such as, the Ministry of Finance and the Ministry of Economic Development, directly or indirectly, engage in policy formulation, regulatory functions, support services, and coordination of SME development works. Government departments carry out regulatory functions and provide support services for R&D, enterprise development, skills development, investment promotion, and trade promotion (Ministry of Traditional Industries & Small Enterprise Development, 2012)

Both state and private banks are the main capital providers to SMEs in Sri Lanka (Ministry of Finance and Planning, 2013). These banks have established loan schemes and projects to help SMEs. In 2013 the total loan disbursements to SMEs by the state banks amounted to Rs.168,409 million (approximately US$1,276 million) (Ministry of Finance and Planning, 2013). However, SMEs in Sri Lanka face significant constraints to access bank finance (Gamage, 2015). Access to bank financing is the biggest barrier faced by SMEs in most developing countries (Wang, 2016). The credit culture in the Sri Lankan banking industry shows that banks predicate their decisions not on cash flows but on collateral when making lending decisions to the SME sector (Gamage, 2015). Therefore, for example, being able to offer a clear title to land can be critical to qualify for a loan.

The multilateral and bilateral donor agencies such as the World Bank, the IMF, the Asian Development Bank, the Japan International Cooperation Agency, and the United States Agency for International Development also play an important role in promoting the SME sector activities. They supply of low cost credit, and they have been actively involved in capacity building policy reform initiatives jointly with government and private sector organisations (Ministry of Enterprise Development, 2012).

2.6 Financial reporting environment in Sri Lanka

The history of financial reporting in Sri Lanka can be traced back to the ninth and tenth centuries (Liyanarachchi, 2009). Archival evidence shows that Buddhist monasteries were required to maintain accounting records and to read these records aloud annually and publicly (Liyanarachchi, 2009). Buddhist monasteries had wealth to maintain in the form of land and money received from the king, officials, and private individuals. Liyanarachchi (2009) notes rock inscriptions were relied upon to limit the misappropriation of monastic property and to improve openness and accountability. Thus, the accounting records helped to maintain the reputation of a monastery as well as the relationship between monastery, rulers, and the general public.

The British colonial period is seen to be the most significant in influencing Sri Lankan accounting practises (Narayan, Lakshman, & Reid, 2002). During this period, locals who could afford a British education were able to obtain accounting qualifications from the Institute of Chartered Accountants in England & Wales or from any other British body (Wijewardena & Yapa, 1998). The British motive was to provide some education to locals in order to obtain assistance for their administration processes (Perera, 1975). Most of those who went to the United Kingdom to study were from the elite Colombo family members. This tradition continued for many years as British-owned mercantile companies operated in Sri Lanka gave priority to British-qualified professionals (Wijewardena & Yapa, 1998). Wijewardena and Yapa (1998, p. 269) explain:

> … during the early years of the colonial period, most of the sizable businesses in these countries (Sri Lanka as example) were set up by British investors. The managerial personnel, including accountants, for these enterprises were generally brought from the UK. At that time a person could obtain the status of professional accountant only by admission to one of the British professional accounting bodies. Only the small number of local people who could bear the cost of education and training abroad proceeded to England to obtain professional qualifications.

Until 1970, Sri Lankan financial reporting requirements were largely based upon British legislation and professional promulgations (Narayan et al., 2002). Thereafter, the accounting laws and regulations related to financial reporting of business entities in Sri Lanka were developed in response to changes in the business and economic environments of the country such as the *Companies Act No 7 of 2007*.

2.6.1 Companies Act No. 7 of 2007

Sri Lanka's *Companies Act No.7 of 2007* (the Act), replacing the 25-year old Act of 1982, come into legal force with effect from 3 May 2007. The Act is based largely on the New Zealand company law (Sunday Island, 2007). The Act contains the current rules, procedures, and accounting and reporting requirements for Sri Lankan incorporated or registered companies. Company registrations, financial statements, and annual returns are lodged with the Registrar of companies. The Act sets out the requirements to prepare company and group financial statements. However, the Act does not clearly classify companies into different categories. Further, it does not specify the financial reporting and auditing requirements or which standards are applicable for each category (Wickramasinghe, 2015). Under the Act public company financial statements are open for public inspection, but private company financial statements are not. The Registrar may, by notice in writing require a private company to deliver to the Registrar, the financial statements of the company together with copies of any auditor's report on those statements (Companies Act, 2007). The Act specifies that an auditor must be a member of the Institute of Chartered Accountants of Sri Lanka (CASL) to carry out audits of Specified Business Enterprises.[9]

2.6.2 Institute of Chartered Accountants of Sri Lanka

The main professional accounting body CASL, was established in 1959. It is responsible for overseeing the accounting and auditing profession in Sri Lanka. Prior to 1959, the only authoritative body of accountancy in Sri Lanka was the Accountancy Board (Perera, 1975). Accountants who became qualified under the Accountancy Board were called Ceylon Registered Accountants. The examinations conducted by the Accountancy Board were similar to those of the British professional accounting bodies (Yapa, 2006).

Since its establishment, the CASL has provided the opportunity for prospective accountants to become qualified as chartered accountants within the country (Perera, 1975). The CASL acts as an examining body for certifying chartered accountant qualifications. It is the only body issuing “practicing certificates” to its members and they are the only members eligible to carry out audits of Specified Business Enterprises (Wickramasinghe, 2015; Yapa, Jalathge, & Siriwardhane, 2017). CASL members pay annual subscription fees and have to submit a self-declaration of Continuous Professional Development (CPD) to renew their annual practicing certificate (Yapa et al., 2017). There is no separate registration process for audit-firms, although “approved Employer Certificates” are issued to firms but not in the name of individual partners (Yapa et al., 2017, p. 505). Table 3 shows the number of audit firms operating in Sri Lanka as of 2014.

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[9] *The Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995* defines a class of companies as Specified Business Enterprises (SBEs). SBEs include: 1. Companies listed on a stock exchange. 2. Banks. 3. Insurance companies. 4. Factoring companies. 5. Finance companies. 6. Leasing companies. 7. Unit trusts. 8. Fund management companies. 9. Stockbrokers and stock dealers. 10. Stock exchanges. 11. Public corporations engaged in the sale of goods or the provision of services. 12. Non-listed companies that have; ─ annual turnover in excess of Rs500 million; ─ shareholders’ equity in excess of Rs100 million; ─ gross assets in excess of Rs300 million; ─ liabilities to banks and other financial institutions in excess of Rs100 million; ─ staff in excess of 1,000 persons.

Table 3 : Audit firms in Sri Lanka

Single/Type of audit firm	**No. of firms**
Sole audit practitioner	441
2 Audit partners	45
3 Audit partners	14
4-5 Audit partners	12
6-9 Audit partners	7
10-14 Audit partners	6
15-19 Audit partners	1
Overseas	6
Total	532

Source: Wickramasinghe (2015)

The four largest international accounting firms that operate in the country are KPMG, Ernst & Young, PWC, and BDO. They audit 84 per cent of the listed companies (Yapa et al., 2017). The registered auditors who operate in Sri Lanka includes: officers of the Department of Inland Revenue; holders of the Higher national Diploma in Accountancy; members of the Ceylon Audit Service who are not below the rank of Superintendent of Audit; members of the Ceylon Government Accountancy Service who are not below Class III; and a member of any other institute or society of accountants or secretaries approved by the Board of Registrar of Companies as per the Ceylon Government Gazette, September 4, 1964 (Wickramasinghe, 2015). Registered auditors and small and mid-tier audit firms carry out most of SME audits. However, registered auditors are not mandated to comply with Sri Lanka Auditing Standards, and are not required to undertake CPD. Therefore, the public perception of the value of an audit is weak (Wickramasinghe, 2015).

It is suggested that there are significant skill gaps and concerns regarding the ability of many Sri Lankan small and mid-tier audit firms to comply with the requirements of the Sri Lanka Standard on Quality Control (Wickramasinghe, 2015). A major concern of small and mid-tier Sri Lankan audit firms is the “poaching” of experienced professional staff by the Big Four audit firms (Yapa et al., 2017). It is further claimed that small and mid-tier audit firms in Sri Lanka are unable to compete effectively with registered auditors due to the absence of mandatory audit requirements set by CASL (Wickramasinghe, 2015). This has created unique tensions among small and mid-tier audit firms about their market share and survival in the profession (Yapa et al., 2017). Staff shortages, lack of regular professional development, and retention of qualified and trained staff are some of the issues faced by these smaller audit firms in general (Alam & Nandan, 2010; Ciccotosto, Nandan, & Smorfitt, 2008).

The CASL currently has 4,396 members, of which 3,461 are working in Sri Lanka (Institute of Chartered Accountants of Sri Lanka, 2014a). Therefore, for a country with about 20.4 million people, 3,461 accountants seems inadequate. As Yapa (2000, p. 298) explains:

> …although CASL was set up to improve the status of the profession and to contribute positively to the economic development of the country, analysis of Sri Lankan professional accounting education and CASL's role in producing qualified accountants during the last four decades raises serious doubts about the achievement of those objectives.

By comparison, Australia, with a similar size of population, has over 100,000 professionally qualified accountants. Furthermore, Singapore, with only 2.9 million people, has nearly 8000 professionally qualified accountants (Yapa, 2000).

2.6.3 Sri Lanka Accounting and Auditing Act No 15 of 1995

Until 1995, accounting and auditing standards in Sri Lanka served as guidelines for accountants and auditors to prepare and audit financial statements (Narayan et al., 2002). After the enactment of the *Sri Lanka Accounting and Auditing Act No 15 of 1995*, Sri Lanka Accounting Standards issued by the CASL became mandatory for all public companies. It empowers the CASL to issue suitable accounting and auditing standards from time to time. The *Sri Lanka Accounting and Auditing Act No 15 of 1995* governs the preparation, presentation, and audit of financial statements. This Act also established the Sri Lanka Accounting and Auditing Standards Monitoring Board to administer the Act as well as monitor the application of accounting and auditing standards (Sri Lanka Accounting and

Auditing Standards Monitoring Board, 2012). Other current reporting requirements are found in the *Inland Revenue Act No. 10 of 2006*.

2.6.4 Inland Revenue Act No. 10 of 2006

The *Inland Revenue Act No. 10 of 2006* requires all listed companies and companies, partnerships, and sole proprietorships, having a turnover of not less than 250 million rupees or a net profit of not less than 100 million rupees for the year, to submit their annual tax return to the Department of Inland Revenue together with audited financial statements (Inland Revenue Act, 2006). All other entities including private companies, partnerships, or any sole proprietorships are also required to submit detailed balance sheet and revenue accounts. However, a cash flow statement is not a compulsory requirement for these entities. According to the act, financial statements should be prepared and audited by an approved accountant.[10]

SMEs' financial reporting in Sri Lanka is closely linked with taxation laws (Perera, 1975). In spite of the taxation laws, it is often alleged that firms avoid taxation illegally altering business records (Perera, 1975). Therefore, the credibility of financial information provided by SMEs is questioned. As in other developing countries, tax evasion is one reason why Sri Lanka has not been successful in raising adequate tax revenue to meet its public expenditure (Jayawickrama, 2008; Pragua, 2010). The adoption of the IFRS was promoted as a way to improve the quality of financial reporting in Sri Lanka (World Bank, 2004).

[10] "Approved accountant" means
(i) An accountant who is a member of the Institute of Chartered Accountants of Sri Lanka;
(ii) An accountant who is approved by the Commissioner-General for the purpose of the definition of authorized representative;
(iii) any individual who is registered as an auditor under the Companies (Auditors) Regulations and approved by the Commissioner-General for the purpose of the definition of "authorized representative"; or
(iv) An auditor authorized to carry out audits of cooperative societies registered under the Cooperative
Societies Law, No. 5 of 1972, in relation to any such co-operative society where the turnover of such society for the year does not exceed fifty million rupees.

2.7 *IFRS* adoption in Sri Lanka

In 2004, the World Bank conducted a review of accounting and auditing practices in Sri Lanka. The objective of this review was to evaluate the weaknesses and strengths of the accounting and auditing requirements, and to compare actual practices with the reporting requirements (World Bank, 2004). The *IFRS* and International Standards on Auditing served as benchmarks for evaluating international comparability of locally applicable accounting and auditing requirements. The review identified gaps between Sri Lanka accounting standards and the *IFRS* (World Bank, 2004). According to the World Bank (World Bank, 2004, p. 11), "a gap exists between Sri Lanka Accounting Standards and International Accounting Standards mainly for two reasons: non-adoption of certain International Accounting Standards; and the introduction of an alternative method that is not permitted by International Accounting Standards".

Following its evaluation of the Sri Lanka accounting and auditing standards, the World Bank made recommendations through their Report on the Observance of Standards and Codes. The World Bank mandated the use of the *IFRS* in Sri Lanka (World Bank, 2004). Accordingly, Sri Lanka Accounting Standards are based on the *IFRS* formulated by the IASB (Institute of Chartered Accountants of Sri Lanka, 2014b). Entities having public accountability are required to comply with Sri Lanka Accounting Standards (SLFRSs), an equivalent of the *IFRS*. All Specified Business Enterprises are required to use full SLFRSs even if their securities do not trade in a public market.

Further, the CASL has introduced the Sri Lanka Accounting Standards for Small and Medium-Sized Entities (*SLFRS for SMEs*), an equivalent of the *IFRS for SMEs* effective from 1 January 2012 (Institute of Chartered Accountants of Sri Lanka, 2012). Before adoption of the *IFRS* in 2012, accounting standards issued for Specified Business Enterprises by the CASL were known as Sri Lanka Accounting Standards (SLAS), and the accounting standards issued for small and medium sized enterprises were called the Sri Lanka Accounting Standards for Smaller Enterprises (SLASSE).[11]

Sri Lanka made no modifications to the *IFRS for SMEs* and adopted the SME definition given by the IASB. The president of the CASL believes that adopting the *IFRS for SMEs* would allow banks and other financial institutions to better access a company's performance and risk, as well as improve confidence in company records and reduce barriers to accessing finance (Institute of Chartered Accountants of Sri Lanka, 2014b). Further, the president of the CASL stated that local SMEs would be able to establish a comparable set of financial statements with SMEs globally. In 2012, the World Bank extended a grant of US$500,000 to the CASL. One of the aims of this grant was to strengthen the financial reporting of SMEs by improving the awareness and skills in *IFRS for SMEs* among SME accountants (Sunday Observer, 2012).

The CASL introduced *SLFRS for Smaller Entities* in 2015. This accounting standard became operative for financial statements covering periods beginning on or after 1 January 2016. It could be applied by an entity that is not any of the following: (a) an entity that had revenue in excess of Rs100 million (approximately US $671,140) in the reporting period; (b) an entity that had equity in excess of Rs50 million (approximately US$335,570) at the end of the previous reporting period; (c) a company that is required to prepare group financial statements by the law relating to companies; or (d) an entity that holds assets in a fiduciary capacity as one of its primary businesses (Institute of Chartered Accountants of Sri Lanka, 2015). The

[11] Smaller Enterprises (SE) are companies, not listed in a stock exchange licensed under the Securities and Exchange Commission Act No. 36 of 1987 which fall below all the upper thresholds and stand above any one of the lower thresholds described as follows. Upper Thresholds: (1) Which have an annual turnover below Rs750 million; (2) At the end of the previous financial year, had shareholders' equity below Rs150 million; (3) At the end of the previous financial year, had gross assets below Rs450 million; (4) At the end of the previous financial year, had liabilities to Banks and other financial institutions below Rs150 million and (5) Have a staff below 1000 persons. Lower Thresholds: (1) Which have an annual turnover in excess of Rs50 million or (2) At the end of the previous financial year, had shareholders' equity in excess of Rs10 million or (3) At the end of the previous financial year, had gross assets in excess of Rs30 million or (4) At the end of the previous financial year, had liabilities to Banks and other financial institutions in excess of Rs10 million or (5) Have a staff in excess of 100 persons.

content of the accounting standard *SLFRS for Smaller Entities* and a comparison of this accounting standard with *SLFRS* and *SLFRS for SMES* are presented in appendix A.

2.8 Summary

This chapter discussed the uniqueness of Sri Lanka in terms of its historical, cultural and religious values, as well as the legal and political environment, the economic and social environment, and the financial reporting environment. Sri Lanka has a rich historical and cultural heritage covering more than 2,500 years. Buddhism evolved as an integral part of the Sri Lankan culture under royal patronage. Sri Lanka was under colonial rule for more than four centuries. Sri Lanka's culture, commercial practices, legal systems, and education were largely influenced by the British who created the crown colony. Sri Lanka has become a multi-cultural, multi-religious, and multi-lingual country.

Evidence of financial reporting practices in ancient Sri Lanka can be found in Buddhist monasteries, which were required to keep accounting records. Subsequently, financial reporting practices were largely influenced by the British. More recently, the financial reporting practices were directly subject to international influences such as those of the World Bank. Following the World Bank's recommendations, Sri Lanka adopted into their financial reporting system the *IFRS* issued by the IASB. Since the IASB uses English as the language for publishing their materials, the diversity in cultures and languages may cause problems of inconsistent interpretation and application of *IFRS for SMEs* within the country (Poudel et al., 2014).

The adoption of *IFRS for SMEs* is not likely to result in increasing transparency and accountability due to the underdeveloped legal and institutional framework in Sri Lanka. The broad aim of comparable financial statements may be undermined if weak enforcement and corruption leads to different compliance levels across companies (Poudel et al., 2014). Recruitment of skilled personnel could also be problematic and very expensive for Sri Lankan SMEs as there is a shortage of qualified accountants. Lack of widespread technical expertise in Sri Lanka may have implications on the effective implementation of international accounting standards. This raises questions about whether accounting standards developed with significant influence from advanced industrialised countries, are suitable for developing countries if they are not modified to reflect local conditions (Poudel et al., 2014).

The next chapter which discusses the literature on SME financial reporting may provide some indications and understandings on how Sri Lanka could develop their accounting practices.

CHAPTER THREE

FINANCIAL REPORTING BY SMALL AND MEDIUM ENTITIES

3.1 Introduction

Financial reporting by SMEs has attracted enormous attention, particularly after the issue of the International Financial Reporting Standard for Small and Medium-sized Entities (*IFRS for SMEs*) (see: Aboagye-Otchere & Agbeibor, 2012; Albu, 2013; Albu et al., 2010; Albu et al., 2013; Chand et al., 2015; Devi & Samujh, 2014, 2015; Eierle & Haller, 2009; Kaya & Koch, 2015; Litjens, Bissessur, Langendijk, & Vergoossen, 2012; Ram & Newberry, 2013). The International Accounting Standards Board (IASB) was not the first to develop a differential financial reporting framework [12] for Small and Medium Entities (SMEs). Differential reporting for SMEs has been articulated and practised for number of years in some developed countries such as United Kingdom (1997), and New Zealand (1994) as well as some developing countries such as Sri Lanka (2003), and South Africa (2000) (Confederation of Asian and Pacific Accountants, 2003). The justification for differential financial reporting rests mainly on two foundations: differences between users and their information needs; and the cost-benefit of SME financial reporting (Eierle, 2005).

Sri Lanka's adoption of *IFRS for SMEs* supersedes the Sri Lankan Accounting Standards for Smaller Enterprises (SLASSE) issued in 2003. Even though, the *IFRS for SMEs* is simpler than the full *IFRS* it is still based on a framework which focuses strongly on outside equity investors as the main users of financial information (Devi & Samujh, 2014; Di Pietra et al., 2008; Evans et al., 2005). The basic objective of financial reporting taken from that framework does not seem to be appropriate for

[12] Differential reporting is built on "the notion that some entities should be allowed to depart from some particular requirements of accounting standards or the entire accounting standards in preparing their financial statements"(Confederation of Asian and Pacific Accountants, 2003, p. 7).

SMEs since most of them are managed by their owners and there is little need for stewardship reporting between the management and the owners (Carsberg et al., 1985). Thus, a critical question that arises is whether the primary users of SME financial information are same as the users of large entities. As the basis of any financial reporting framework is information needs of users, the users and their uses of SME financial information needs to be explored. A review of previous studies regarding users and uses of SME financial statements assists to identify gaps in the literature and provides rationale for the research questions. This chapter therefore reviews and analyses the literature on SME financial reporting, which has focused on two main issues: users and uses of SME financial information and the current financial reporting frameworks in various jurisdictions.

Section 3.2 begins with a discussion on SME definitions and provides the SME definition adopted for the study. This is followed by a discussion on the objectives of financial reporting in section 3.3 and the conceptual framework for financial reporting issued by the International Accounting Standards Board (IASB). Sections 3.4 and 3.5 review studies regarding users and uses of SME financial statements. Section 3.6 examines current financial reporting frameworks in various jurisdictions including Sri Lanka. Finally, section 3.7 concludes the chapter.

3.2 Defining Small and Medium Enterprises (SMEs)

There is no standard definition for SMEs. Diversity and richness of the characteristics of SMEs, political strategies and economic conditions are factors which hinder the existence of a common and generally accepted definition of SMEs (Organisation for Economic Co-operation and Development, 2005). SMEs are defined in a variety of ways by various countries using a number of parameters. Quantitative criteria are often used in defining SMEs as they allow a clear delimitation between small and medium entities (Buculescu, 2013). The most commonly used quantitative criteria are: number of persons employed; total assets value; and annual turnover.

The European Commission uses criteria based on turnover, total assets, and employee numbers to define SMEs. As shown in Table 4, the European Commission (2003) defines small enterprises as those that employ less than 50 employees and annual turnover or annual balance sheet total[13] does not exceed 10 million Euros (US$10.7 million approximately). Medium-sized enterprises are defined as enterprises which employ less than 250 employees with an annual turnover of less than or equal to 50 million Euros (US$85 million approximately) and an annual balance sheet total of less than or equal to 43 million Euros (US$73.1 million approximately). Although the employee number threshold is compulsory, it is not mandatory to meet both turnover and balance sheet thresholds concurrently (European Commission, 2003).

There is no common definition for SMEs among South Asian countries. For example, Bangladesh defines SMEs based on the value of fixed assets (excluding land and building) and/or the number of employees (Asian Development Bank, 2014). Manufacturing firms with fixed assets of Tk5 million - Tk100 million (US$63,036 - US$1,260,716 approximately) and 25-99 employees, and service and trade firms with fixed assets of Tk5 million - Tk10 million (US$63,036 - US$126,072 approximately) and 10-25 employees, are considered small. Manufacturing firms with fixed assets of Tk100 million - Tk300 million (US$1,260,716 - US$3,782,148 approximately) and 100-250 employees, and service and trade firms with fixed assets of Tk10 million - Tk150 million (US$126,072 - US$1,891,074 approximately) and 26-100 employees are considered medium-sized.

In Sri Lanka, there is no universal definition for SMEs. Various government agencies and other organisations use different criteria to identify SMEs on the basis of their assistance programmes. Table 4 provides the definitions of SMEs given by various organisations in Sri Lanka. For the data collection purpose of this thesis, SMEs will be defined as firms with 5-99 employees. This determination is consistent with the definition given by the World Bank’s enterprise survey for Sri Lanka (World Bank, 2016). This definition was selected because it helps to differentiate small businesses from larger businesses, and it allows for easy

[13]The annual balance sheet total refers to the value of a company’s main assets.

gathering of accurate, relevant and useful data from the Department of Census and Statistics of Sri Lanka. This thesis selects SMEs from a database maintained by the Department of Census and Statistics of Sri Lanka, which categorises entities on the criterion of number of employees.

The Association of Southeast Asian Nations (ASEAN) countries adopt different definitions for SMEs based on their own parameters (see Table 4 for Southeast Asian country-specific SME definitions). For example, Malaysia defines SMEs by reference to the number of employees and annual turnover, while the Philippines uses number of employees and total assets value. However, the IASB's SME definition in the *IFRS for SMEs* is based on qualitative characteristics. The IASB's definition is not based on size-threshold and consequently is therefore, different to that used by most countries. However, authorities at the individual jurisdiction level are permitted to decide what constitutes an eligible entity to which the *IFRS for SMEs* can be applied (International Accounting Standards Board, 2009b).

Table 4 : SME definition around the world

Region	Country	Small enterprises			Medium enterprises		
		No. of employees	**Total assets**	**Total annual turnover**	**No. of employees**	**Total assets**	**Total annual turnover**
European Union		<50	≤ €10 million	≤ €10 million	<250	≤ €43 million	≤ €50 million
South Asia	Bangladesh	25-99	Tk5 – 100 million	-	100-250	Tk101 -300 million	-
		10-25	Tk5-10 million	-	26-100	Tk11-150 million	-
	India	-	> Rs2.5 - < 50 million investment in plant and machinery	-	-	≥ Rs50 - < 100 million investment in plant and machinery	-
		-	> Rs1 - < 20 million investment in equipment	-	-	≥ Rs20 - < 50 million investment in equipment	-
	Sri Lanka	SMEs are defined as enterprises with a capital investment of less than Rs.5 million which employ fewer than 50 employees (As defined by Department of Small Industries)					
		-	<Rs20 Million Assets value excluding land and buildings value	-	-	<Rs.50 Million Assets value excluding land and buildings value	-
		<49	-	-	50 - 99	-	-
ASEAN	Philippines	10-99	P3,000,001-15,000,000	-	100-199	P15,000,001-P100,000,000	-
	Singapore	Annual sales turnover of not more than S$100 million or employment size of not more than 200 employees					

While Sri Lanka and Bangladesh adopted the IASB's SME definition, some countries have added size tests or other restrictions. For example, Singapore added size criteria based on turnover, assets, or employee number (International Financial Reporting Standards Foundation, 2016) to define an entity as small. The Philippines added criteria based on total assets and total liabilities (International Financial Reporting Standards Foundation, 2016).

3.3 Objectives of financial reporting

Reporting the stewardship of management and providing decision useful information are the two main objectives of financial reporting as established in the conceptual frameworks of the IASB (International Accounting Standards Board, 2009b).This section discusses these two financial reporting objectives.

3.3.1 Stewardship

There is no commonly accepted definition of stewardship in the literature. The concept is subject to a variety of alternative interpretations (O'Connell, 2007). Birnberg (1980) suggests the notion of stewardship accounting evolved from the traditional custodial role contained in information that facilitates what might broadly be termed 'accountability reporting'. In this sense the notion of stewardship discussed by Birnberg (1980), may be viewed as virtually synonymous with the concept of accountability (O'Connell, 2007).

In the IASB's accounting standard *IFRS for SMEs*, the stewardship role of financial statements is designed to show the results of the stewardship of management for the entrusted resources (International Accounting Standards Board, 2009b). It is claimed that stewardship plays an important role in information dissemination where the owners are not the managers of the entity (Mala & Chand, 2015). One of the key features of large companies is the separation of ownership and control, with those who invest in the business entrusting responsibility for managing the business to the directors (Collis, 2003). Unlike large companies, the separation of ownership and control is not common in the majority of SMEs (Carsberg et al., 1985). As a consequence, the stewardship role of financial reporting may be "redundant" (Jarvis

& Collis, 2003a). An owner can observe the behaviour of an employed manager on a daily basis (McMahon & Stanger, 1995).

3.3.2 Decision usefulness

The decision usefulness objective of financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity (International Accounting Standards Board, 2010, p. 9). The rationale for the identification of users and uses of financial information is therefore, based on decision usefulness objective (Son, Marriott, & Marriott, 2006). The objective designates accounting as a process of providing the relevant information to the relevant decision makers (Gray, Owen, & Adams, 1996). Accordingly, useful information should be included in financial statements while subjective information is discouraged unless it provides users with crucial information (Ijiri, 1975).

The decision usefulness objective was first promoted by the Trueblood Report in the USA (Son et al., 2006). The American Institute of Certified Public Accountants (AICPA) asserts that the objective of financial statements is to provide information useful to investors and creditors for making economic decisions (American Institute of Certified Public Accountants, 1973). Although primary attention was devoted to investors and creditors, the AICPA explicitly acknowledged the existence of a variety of users, including employees, by declaring that "while users differ, economic decisions are similar" (American Institute of Certified Public Accountants, 1973, p. 18). The Trueblood Report states that the societal goals of an enterprise are as equally important as the economic goals (American Institute of Certified Public Accountants, 1973, p. 54). Therefore, enterprises should provide decision useful information to all the stakeholders, and not just the investors or creditors (American Institute of Certified Public Accountants, 1973, p. 54).

In the United Kingdom, the Corporate Report (Institute of Chartered Accountants in England and Wales, 1975) was an early attempt to discuss the decision usefulness perspective of financial statements (Dang-Duc et al., 2006). The Institute of Chartered Accountants in England and Wales (1975, p. 28) states the basic objective of corporate reports is to provide information useful to "those having reasonable rights to such information". However, this statement is very much a matter of opinion as it was not tested empirically (Collis, 2003). The Corporate Report explicitly identifies the following as the users of accounting reports: equity investors, loan creditors, analysts-advisors, business contacts, employees, government and the general public (tax payers, ratepayers, consumers, political parties, and consumers and environmental protection societies) (Institute of Chartered Accountants in England and Wales, 1975, p. 17). Jarvis (1996) argues that users and their needs for financial information in this report were limited to public listed companies rather than smaller companies. Since the accounting standard *IFRS for SMEs* is based on the IASB's 1989 conceptual framework (International Accounting Standards Board, 2009a), the following section discusses objectives of financial reporting with reference to the IASB's 1989 conceptual framework.

IASB's 1989 conceptual framework for the Preparation and Presentation of Financial Statements

The IASB's 1989 framework stated the first objective of financial statements is to:

> … provide information about the financial position, performance and cash flows of the entity that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs (International Accounting Standards Board, 2009b, p. 12).

The second objective is to report the results of the stewardship of management or the accountability of management for the resources entrusted to it (International Accounting Standards Board, 1989). Financial statement users identified in the IASB's 1989 *Framework for the Preparation and Presentation of Financial Statements* include: investors; employees; lenders; suppliers and other trade creditors; customers; government and their agencies; and the public (International Accounting Standards Board, 2009b). Internal users such as managers are excluded as they have access to inside information (International Accounting Standards Board, 2009b). In this respect, Schiebel (2008, p. 4) contends that the financial statements prepared under the IASB framework are "designed to reduce information asymmetries between the insiders of a reporting entity and the various outsiders making economic decisions involving that entity".

The IASB's aim in introducing new financial reporting standards for SMEs holds the concept of 'user oriented financial information' (International Accounting Standards Board, 2009b). The IASB points out that the differences between full *IFRS* and *IFRS for SMEs* should be established based on the accounting information needs of the users and cost-benefit considerations (International Accounting Standards Board, 2009a). Conversely, the IASB believes that a different framework for SMEs is not needed, since by fulfilling the needs of investors and creditors it also satisfies other categories of users (International Accounting Standards Board, 2009a, p. 33). The IASB argues that the information needs of users of SME financial statements were similar in most ways to those of users of publicly accountable entities' financial statements (International Accounting Standards Board, 2004). Financial statement users identified by the IASB in the *IFRS for SMEs* include: banks; vendors; credit rating agencies; customers; and shareholders that are not also managers of SMEs (International Accounting Standards Board, 2009b). Even though, the IASB's 1989 framework included government agencies as users of financial information, the accounting standard *IFRS for SMEs* did not consider them as users of SME financial information. Users such as owner-managers, and tax authorities are excluded from its scope as they have access to inside information (International Accounting Standards Board, 2009b). However, research identifies owner/directors and taxation authorities as the main users of the financial information of SMEs (see for example Di Pietra et al., 2008, Evans et al., 2005, and Sian and Roberts, 2006). Consequently, financial statements for SMEs frequently take their reference point from the national taxation authorities (Briciu, Groza, & Gânfalean, 2009; Devi & Samujh, 2014).

According to the decision usefulness objective, financial reporting framework needs to be derived through the financial information needs of the users at large. Jonas and Young (1998) and Young (2006) argues that a user perspective was emphasised frequently in financial accounting standards but in absence of empirical knowledge about information needs and users of financial statements. The decision-usefulness approach created by the standard setters has been documented but is not based on scientific research. Rather, it has emerged through a consultative process over time (Coetsee, 2010; McCartney, 2004). Therefore, determining the main users of SME financial information is necessary to assess the IASB's view regarding the need for general purpose financial statements for SMEs. The following section discusses previous studies on users and uses of SME financial information.

3.4 Previous research on users of SME financial reporting

Early research carried out with auditors (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Page, 1984) and directors (see for example: Carsberg et al., 1985; Page, 1984) of SMEs in Ireland and the United Kingdom shows that the most important users of SME statutory financial statements were entity directors, followed by tax authorities and banks or lenders. Trade creditors and customers were perceived to be less important. A summary of previous studies on users of SME financial reporting is presented in Table 5. Table 5 shows most of research in United Kingdom was conducted more than a decade ago. In the work of Collis and Jarvis (2000), the questionnaire responses of 385 independent, active small companies filing full audited accounts revealed that small company statutory financial statements were provided mainly to banks and other finance providers (69.1%), tax authorities (45.2%), and company directors who are not shareholders (19%). Sian and Roberts (2009) undertook a similar survey but used a wider group with both incorporated and unincorporated small businesses. The analysis of responses from 299 small business owners and 398 accountants showed owners, tax authorities, and banks were the main users of financial statements, while only a few small business owners (3.8%) reported providing their financial statements to customers and suppliers.

Table 5 : Previous studies on main users of SME financial reporting

Author	Country	Main users of SME financial reporting				
		Directors [14] / owners	**Banks**	**Tax authority**	**Creditors**	**Others**
Developed countries						
Page (1984)	United Kingdom	Yes	Yes	Yes	No	No
Carsberg et al. (1985)	United Kingdom	Yes	Yes	Yes	No	No
Collis and Jarvis (2000)	United Kingdom	Yes	Yes	Yes	No	No
Sian and Roberts (2009)	United Kingdom	Yes	Yes	Yes	No	No
Barker and Noonan (1996)	Ireland	Yes	Yes	Yes	No	No
Maingot and Zeghal (2006)	Canada	Yes	Yes	Yes	No	No
Rennie and Senkow (2009)	Canada	Yes	Yes	No	No	No
Haller and Eierle (2007)	Germany	Yes	Yes	No	No	No
Developing countries						
Dang-Duc et al. (2006)	Vietnam	No	No	Yes	No	No

Source: Author

The findings from non-UK based studies of financial reporting by SMEs such as that conducted by Maingot and Zeghal (2006) do not differ significantly from those of UK-based research in terms of the array of user groups. Based on the responses to the questionnaire survey of 162 stakeholders of Canadian SMEs, including owners, managers, and accountants, Maingot and Zeghal (2006) find the three most important users of small entity financial statements were tax authorities, banks, and managers. Another study from Canada by Rennie and Senkow (2009) find lenders and owners were the most important users of financial statements. Similarly, the survey of German SMEs discovers only banks and owners were SME financial statement users (Haller & Eierle, 2007). Vendors and other stakeholders, such as employees, customers and potential investors are not regarded as important users of the financial statements of SMEs.

[14]This includes both directors and managers of SMEs and owners and shareholders of SMEs.

A limited range of users was identified in Vietnam, a developing country, by Dang-Duc et al. (2006). The 19 qualitative interviews undertaken in their study of owners of small companies, accountants, loan officers, and government agencies, reveal that the main users of small companies' financial statements were perceived to be tax authorities and government agencies. By contrast, the studies conducted in the developed countries did not identify government institutions as a main user of SME financial information. Only a minority of the companies interviewed identified banks as an important user of SME financial information in Vietnam (Dang-Duc et al., 2006).

Reviews of the literature on users of SME financial statements and their information needs were carried out by Di Pietra et al. (2008), Evans et al. (2005), and Sian and Roberts (2006). These studies affirm that many SMEs produce financial statements primarily for tax authorities, owner-managers and banks. Although most of the researchers identify owner/directors and taxation authorities as the main users of the financial statements of SMEs, accounting standard setting bodies such as the IASB focus on the general purpose of financial statements and exclude the specific needs of these two users (Son et al., 2006).

3.5 Research literature on financial information needs of SME users

The identification of the needs of users of SME financial information is important, especially when developing or modifying financial reporting requirements for SMEs. This section, considers how different classes of user groups (management, owner/shareholders, banks, tax authorities, trade creditors and customers) use financial information of SMEs based on empirical findings.

Management

Carsberg et al. (1985) find that small company directors used financial statements to make decisions about dividends and directors' pay. Collis and Jarvis (2000) further find that small company financial statements were perceived to be most useful for deciding director's pay and bonuses, and also comparing performance across prior periods. A subsequent study by Sian and Roberts (2009) with a sample of owner-managed small businesses, provided similar results, except the financial statements were not viewed as useful information sources for deciding directors' remuneration. All of these researchers observe that financial statements are perceived to be less useful for management purposes when compared to management information such as management accounts, bank statements, and budgets.

United Kingdom based studies discovered computerised accounting systems, including accounting software packages, were widely used among SMEs (Collis & Jarvis, 2002; McMahon, 1999; Sian & Roberts, 2009). This implies that not only financial statements but also more frequent and detailed management reports can easily be generated from computerised systems. Several studies show that many SMEs use a computerised accounting system to keep records and to produce management information (see, for example, Marriott & Marriott, 2000; Sian & Roberts, 2009). Given the ease with which management information can be produced, it is likely that the usefulness of financial statements for management purposes will decrease. Owner-managers believe the complicated accounting rules and unfamiliar accounting concepts used to prepare financial statements were also reasons for the limited usefulness of financial statements for their decision making (Argilés & Slof, 2003; Bunea, Sacarin, & Mihaela, 2012; Halabi, Barrett, & Dyt, 2010; Sian & Roberts, 2009).

Owners/Shareholders

Studies suggest that management and ownership in small businesses is rarely separate. Page (1984) found the vast majority of directors of 413 UK small companies owned 50 per cent or more of the issued share capital. More recent studies conducted with UK by Collis (2008) and Collis and Jarvis (2000), show similar results. Most small companies are owner-managed and have between one to four shareholders. This structure allows the owners or shareholders to observe the behaviour of an employed manager on a daily basis (McMahon & Stanger, 1995). The Canadian Accounting Standards Board (2007) reveals that many minority shareholders of private firms, especially SMEs, seem to have family or employee relationships which gives them access to internal financial information. Collis and Jarvis (2000) also assert that the majority of owners or shareholders have access to financial information for controlling and monitoring purposes, a situation which made the stewardship role of financial reporting to owners or shareholders redundant. Greenhalgh (2000), Marriott and Marriott (2000) and Nandan (2010) highlight the importance of management accounting information for the owner-managers of small and medium enterprises (SMEs). Nandan (2010) argues that like large firms, SMEs' require adequate and sophisticated management accounting techniques and systems to better manage scarce resources and enhance customer and owner-manager values.

Banks

Research studies submit that financial statements play an important role in bank lending decisions (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Maingot & Zeghal, 2006; Page, 1984). Earlier, Stanga and Tiller (1983) analyse the informational needs of 230 bank loan officers in the United States who make lending decisions to small private companies. The statement of changes in financial position, revenue associated with each major industry segment, operating income or loss of each major industry segment were rated by the respondents as being very important in the decisions to lend SMEs.

Berry, Faulkner, Hughes, and Jarvis (1993) establish that accounting information is important, in the United Kingdom, for lending decisions to small businesses, but that it is used in different ways and given different weightings depending on various other internal and external factors. The major sources of financial information used in lending decisions to small business relates to profitability, gearing and security whilst liquidity apparently plays a smaller role (Berry et al., 1993). Further, from their own analysis and an analysis of the literature, Berry et al., (1993) suggest that four factors i.e. the person, the quality of information, the type of proposition and the banking environment were likely to influence the lending decisions. Another research study conducted in United Kingdom by Deakins and Hussain (1994), applies an innovative research methodology. The authors presented business plans of new entrepreneurs seeking funding decisions. They were interviewed by 30 bank managers to discover that decision making is not consistent across bank officers. Their findings suggest that bank officers in United Kingdom placed most importance on gearing, financial asset information of the entrepreneurs, and explanations about income generation (Deakins & Hussain, 1994). However, bank officers treat management and cost accounting information, managerial qualities and skills of entrepreneur as unimportant for assessing risks (Deakins & Hussain, 1994). More recently, Berry, Grant, and Jarvis (2004) conduct semi-structured interviews with 10 European bankers. The majority of the bankers look at profitability and future cash flows when making lending decisions to SMEs in the United Kingdom.

A postal survey of Australian small businesses seeking debt or equity finance demonstrate that annual and periodic financial statements, future-oriented financial statements and business plans are provided to finance providers (McMahon, 1999). By contrast, Dang-Duc, Marriott, and Marriott (2008) examine the use of SME financial statements by bank lending officers in Vietnam. These lending officers convert financial statement information into a standardised form - they consider the 'unconverted' financial statements are less useful in loan decision making (Dang-Duc et al., 2008). Further, such as site visits and direct communication with clients were used as alternative sources of information (Dang-Duc et al., 2008). Financial statements are key sources for making lending decisions of German banks; the most important factors are the cash flow and tax balance sheet (Zuelch & Burghardt, 2010). When SMEs do not provide cash flow statements, analysts estimate the cash flow on the basis of the data gathered from the statements on financial positions and comprehensive incomes (Zuelch & Burghardt, 2010).

Several studies investigate the usefulness of audited financial statements and accounting standards for bank lending decisions. Baker and Cunningham (1993) notice loan officers have more confidence in the audited financial statements if they have been prepared using GAAP, and they have more confidence in income tax basis statements if they have been reviewed by a certified public accountant. Similarly, Abu-Nassar and Rutherford (1996) observe user groups in less developed countries such as Jordan placed greater importance on the information contained in the auditor's report. Additionally, Duréndez Gómez-Guillamón (2003) investigate the opinion of bank officers about the usefulness of audited reports for making financing decisions. He argues that bank officers ensure the accuracy of financial information by requiring their clients to provide audited reports. Similarly, Berry and Robertson (2006) find audited financial statements are an important source of information for the lending decision (Berry & Robertson, 2006). Although studies on the use of SME financial statements by banks show that they play an important role in lending decisions, there is no evidence on their role as means of monitoring borrowing.

Tax authorities

From the regulators' standpoint, financial reporting and taxation have different objectives. Financial reporting provides information for users while tax reporting serves as a basis for determining taxable income (Eberhartinger, 1999). However, many small entity owners perceive financial reporting as a legal obligation for filing tax returns (Walton, Haller, & Raffournier, 2003). Studies in developed countries and emerging economies showed that tax authorities are one of the principal users of SME financial statements. According to the International Federation of Accountants (2006) the major uses of SME financial statements by the tax authorities include: determining gross profit; assessing directors' fees; ensuring that expenses are reasonable; and checking for a clean audit report. Barker and Noonan (1996) demonstrate that tax authorities use financial statements to assess gross profit; examine directors' fees and expenses; and to see whether a company's financial statements are accompanied by a qualified auditor report. For the IASB, tax reporting does not fall within the scope of general purpose financial statements as each jurisdiction has its own taxation rules (International Accounting Standards Board, 2009a).

Trade creditors and customers

John and Healeas (2000) and Sian and Roberts (2009) point out that trade creditors do not depend on financial statements for their credit decisions, but they tend to use independent sources before extending credit. Studies reveal that only a small number of SMEs provide their financial statements to creditors, customers/suppliers. For example, of the 385 UK small companies investigated in Collis and Jarvis (2000), around 33 per cent report reading the published financial statements of their major customers, and about 24 per cent indicate reading the published financial statements of major suppliers or creditors (Collis & Jarvis, 2000).

The report of the Professional Oversight Board for Accountancy (2006) asserts that many SMEs used other companies' financial statements to assess the creditworthiness of prospective customers before granting trade credit. Kitching, Kasperova, Blackburn, and Collis (2011) explore the views of preparers and users of SME abbreviated financial statements in the United Kingdom.[15] Of the 149 small companies who responded to their questionnaire survey, about 24 per cent indicated that they use abbreviated financial statements of potential customers. However, abbreviated financial statements are of limited value because they lack detail and offer limited financial transparency (Kitching et al., 2011).

There are number of important limitations in the literature on SME users and their financial information needs. Only a few studies examine the users and uses of SME financial information. Notably, research on SME financial reporting in the context of developing countries is rare. Further, much of the data used in the literature is now dated and even the more recent literature analyses data collected prior to 2010. Since 2009, SME financial reporting frameworks have undergone substantial reform. For example, the IASB introduced the *IFRS for SMEs* in 2009 and many countries including Sri Lanka subsequently adopted that standard. Therefore, up-to-date empirical data obtained on users and their financial information from this research is useful in evaluating accounting standards for SMEs.

Additionally, many researchers (see for example: Barker & Noonan, 1996; Collis & Jarvis, 2000; Haller & Eierle, 2007; Maingot & Zeghal, 2006; Page, 1984; Rennie & Senkow, 2009; Sian & Roberts, 2009) survey the views of a single user group, whilst ignoring other users of SME financial information such as lenders, tax authorities, regulators and other government institutions. Thus, including other

[15] Small companies filing abbreviated financial statements must register an abbreviated balance sheet and related notes, but not a profit and loss account or other financial statements required of large companies.

users is vital when examining the perceptions of users and uses of SME financial information. In this thesis, the perceptions of owner-managers and accountants of SMEs as well as other users' points of view is investigated.

Postal questionnaire surveys with directors/owners of SMEs and auditors of SME financial statements dominates the literature (see for example: Barker & Noonan, 1996; Collis & Jarvis, 2000; Haller & Eierle, 2007; Maingot & Zeghal, 2006; Page, 1984; Rennie & Senkow, 2009; Sian & Roberts, 2009). Only 19 interviews were conducted in a qualitative study in Vietnam (Dang-Duc et al., 2006). Using a single method for collecting data may be inadequate to address the complexity of social science based research questions (Creswell, 2014). This thesis therefore, uses both questionnaires and semi-structured interviews to investigate SME users and their financial information needs.

The IASB adopted a decision-usefulness objective when formulating accounting standards for SMEs. It is timely and important to evaluate the decision-usefulness of SME financial information objective in the developing country setting. With the exception of one research study (see Dang-Duc et al., 2006), research has not evaluated the decision-usefulness of SME financial information. Additionally, much of the extant literature focuses on SMEs in general and does not distinguish between large SMEs, that may have external shareholders, and the small, and medium-sized SMEs. Evans et al. (2005) assert that differences in users and their needs exist within SMEs, especially between the very small entities and the large SMEs. How the information of financial statements is used by different user groups and how SME users and their financial information needs differ according to the size of SME are important issues to be understood. More importantly, this understanding is needed for developing a relevant financial reporting framework for SMEs.

3.6 Financial reporting frameworks in various jurisdictions

This section provides an overall understanding of the current financial reporting frameworks for SMEs employed by a selection of jurisdictions, viz., United Kingdom, New Zealand, Australia, South Africa, three ASEAN countries, and five

South Asian Countries. Table 6 summarises the current financial reporting frameworks of the various jurisdictions.

United Kingdom (UK)

With effect from 1 January 2016, the financial reporting structure in the UK follows an *IFRS* based approach with three tiers: EU-adopted *IFRS* for group listed companies, an adaptation of *IFRS for SMEs* for non-publicly accountable entities, and a simplified version for micro-entities incorporating the requirements of the EU Accounting Directive (Collis, Jarvis, & Skerratt, 2017). The *IFRS* as adopted by the EU is required for the consolidated financial statements of all European companies whose debt and equity securities trade in a regulated market in the United Kingdom. The principal securities exchange in the United Kingdom (London Stock Exchange Main market) is a regulated market to which the EU IFRS regulation applies (Financial Reporting Council, 2015b). Publicly listed group entities have been required to use the EU-adopted *IFRS* since 2005, but may choose between *IFRS* and *FRS 102* for preparing their individual parent accounts (Collis et al., 2017). *FRS 101 (Reduced Disclosure Framework)* allows subsidiaries in a listed group to apply the same accounting as in the group accounts, but with reduced disclosure (Collis et al., 2017).

The requirements in the *FRS 102* applicable in the United Kingdom and Republic of Ireland are based on the *IFRS for SMEs* issued in 2009. However, the Financial Reporting Council of United Kingdom modified the IASB developed *IFRS for SMEs* substantially, both in terms of the range of entities eligible to apply it and in terms of accounting treatments provided (Financial Reporting Council, 2015a). To reflect this wider scope the name of the standard was revised to *FRS 102 Financial Reporting Standard applicable in the UK and Republic of Ireland* (Financial Reporting Council, 2015a). *FRS 102* can be used by any non-publicly accountable entity.

FRS 102 was revised in 2015, and a new Section 1A was introduced for entities classified as small. Section 1A set out the presentation and disclosure requirements for small entities.[16] Subsequently, *FRS 105* was introduced and is applicable to the Micro entities.[17] The recognition and measurement requirements of *FRS 105* are based on *FRS 102* with a number of simplifications. Micro-entities need only provide the minimum disclosures required by law (Collis et al., 2017).

New Zealand

The financial reporting framework of New Zealand has been developed using a ‘user- needs’ approach (External Reporting Board, 2012). The External Reporting Board (XRB) in New Zealand concludes that user-needs cannot be adequately addressed by a single set of accounting standards, and that a multi-standards approach that also uses tiers to match costs and benefits should be adopted (External Reporting Board, 2012, p. 6). Under *the Financial Reporting Act 2013*, entities moved to the *NZ IFRS Reduced Disclosure Regime* (*NZ IFRS RDR* for periods beginning on or after 1 April 2015 (External Reporting Board, 2012). Consequently, the only accounting standard issued by the XRB was *NZ IFRS* or *NZ IFRS RDR* (Simkins, 2012).

The entities that are not large[18] do not have to prepare general purpose financial statements that comply with New Zealand GAAP. Accordingly, most SMEs in New Zealand do not have to follow accounting standards issued by the XRB, but continue to prepare financial statements in accordance with the minimum financial reporting requirements to meet the information needs of the Inland Revenue and other stakeholders. The Inland Revenue sets its minimum financial reporting requirements as historical cost, double-entry, and accrual based special purpose

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[16] A company qualifies if it does not exceed two or more of the following criteria: turnover £10.2m; Balance Sheet total £5.1m; number of employees 50.
[17] A company qualifies if it does not exceed two or more of the following criteria: turnover £632,000; Balance Sheet total £312,000; number of employees 10.

[18] An entity is large if it has total expenses > NZ$30 million.

financial statements (Inland Revenue Department, 2013; PricewaterhouseCoopers New Zealand, 2013).

Australia

In Australia, the *IFRS* are incorporated into Tier 1, with additional paragraphs on the applicability of each standard in the Australian environment (International Financial Reporting Standards Foundation, 2016). *IFRS* are required for all entities that meet the definition of a reporting entity [19] under Australian accounting standards (International Financial Reporting Standards Foundation, 2016). The concept of the reporting entity is "not dependent on the sector (public or private) within which the entity operates, the purpose (business or non-business/profit or not-for-profit) for which the entity was created, or the manner in which the entity is constituted (legal or other)" (Australian Accounting Research Foundation, 2001, p. 7). The concept of a reporting entity is linked to the information needs of users of general purpose financial statements in making and evaluating resource allocation decisions (Australian Accounting Research Foundation, 2001). Entities that are not reporting entities are not obliged to prepare general purpose financial statements.[20] Instead they prepare special purpose financial statements (Deloitte, 2014). The following entities apply Tier 1 requirements in preparing general purpose financial statements: for-profit entities in the private sector that have public accountability (including pension funds); and the Australian Government and State, Territory and Local Governments. The following entities may apply either Tier 2 or Tier 1 requirements in preparing general purpose financial statements: for-profit private sector entities that do not have public accountability; all not-for-profit

[19] A reporting entity is "an entity in respect of which it is reasonable to expect the existence of users who rely on the entity's general purpose financial statement for information that will be useful to them for making and evaluating decisions about the allocation of resources. A reporting entity can be a single entity or a group comprising a parent and all of its subsidiaries" (Deloitte, 2014, p. 1).

[20] In Australia, following three surrogates indicate circumstances where dependent users exist for general purpose financial statements: 1.Separation of management from economic interest; 2. Economic or political importance/influence; and 3. Financial characteristics (Australian Accounting Research Foundation, 2001, p. 9).

private sector entities; and public sector entities other than the Australian Government and State, Territory and Local Governments.

Non-reporting entities can use the *IFRS for SMEs*. Australia's Tier 2 reporting requirements are referred to as Reduced Disclosure Requirements (*RDR*), which are available for general purpose financial reporting by non-publicly accountable entities. All SMEs that are 'reporting entities' are permitted to use *IFRS*, i.e. the Tier 1 Australian Accounting Standards Board (AASB) reporting requirements or the Tier 2 AASB reporting requirements (International Financial Reporting Standards Foundation, 2016). Non-reporting entities, however, have the option to prepare special purpose financial statements to meet the special purpose needs of the users. In June 2010, the AASB decided to introduce the Reduced Disclosure Requirements (*RDR*) instead of adopting the *IFRS for SMEs* (Australian Accounting Standards Board, 2012).

South Africa

The financial reporting structure in South Africa follows a three-tiered system of financial reporting. Accounting standards in Tier 1 and 2 are fully aligned with the *IFRS* issued by the IASB. The adoption of either *IFRS* or *IFRS for SMEs* by companies is dependent, on each company's public interest score[21] (International Financial Reporting Standards Foundation, 2016). Further simplification (Tier 3) is provided for SMEs that have a public interest score under 100 points and whose financial statements are internally compiled. SMEs in Tier 3 can use their own accounting policies if they are not required to comply with any other financial reporting standards (International Financial Reporting Standards Foundation, 2016).

[21]public interest score for each financial year, calculated as the sum of the following: (a) a number of points equal to the average of employees of the company during the financial year ("employee", has the meaning set out in the *Labour Relations Act, 1995*); (b) one point for every R1 million (or portion thereof) in third party liability of the company, at the financial year end; (c) one point for every R1 million (or portion thereof) in turnover during the financial year; and (d) one point for every individual who, at the end of the financial year, is known by the company- (i) in the case of a profit company, to directly or indirectly have a beneficial interest in any of the company's issued securities; or (ii) in the case of a non-profit company, to be a member of the company, or a member of an association that is a member of the company.

ASEAN countries

In Malaysia, entities other than private entities[22] are subject to the Malaysian Financial Reporting Standards, while for private entities, there is an option to apply the Malaysian Private Entities Reporting Standards, which is largely based on the *IFRS for SMEs*. Malaysia replaced the term 'small and medium sized entities' with 'private entities'. In Singapore, Tier 1 and Tier 2 reporting standards are based on *IFRS* (known as Singapore Financial Reporting Standards) and *IFRS for SMEs* (known as the SFRS for Small Entities) respectively. SFRS for Small Entities are designed for non-public accountable entities meeting certain size criteria.[23] Unlike Malaysia and Singapore, Thailand has not yet adopted either *IFRS* or *IFRS for SMEs*. Entities whose equity or debt instruments are traded in a public market, entities whose operation is mainly holding assets in a fiduciary capacity, and public companies under the *Public Company Act*, are required to report under Thai Financial Reporting Standards (Tier 1). Simplified accounting standards known as the Thai Accounting Standard for non-publicly accountable entities (Tier 2) are developed locally and applicable to all sizes of non-publicly accountable entities. However, Thailand is in the process of adopting the *IFRS for SMEs* standard, to be known as the *Thai Financial Reporting Standard for SMEs (TFRS for SMEs*). A study is currently in progress as to which type of entity will be required to adopt the *TFRS for SMEs*.

[22] A private entity is a private company as defined in section 2 of the Companies Act 2016 that is not itself required to prepare or lodge any financial statements under any law administered by the Securities Commission or Bank Negara Malaysia; and is not a subsidiary or associate of, or jointly controlled by, an entity which is required to prepare or lodge any financial statements under any law administered by the Securities Commission or Bank Negara Malaysia.

[23] An entity is eligible to use the Singapore Financial Reporting Standards for Small Entities if it is not publicly accountable, publishes general purpose financial statements for external users, and meets the definition of a 'small entity' for each of the previous two consecutive financial reporting periods, with amended application to newly incorporated entities. An entity qualifies as a small entity if it meets at least two of the three following criteria: (1) total annual revenue of not more than Singapore Dollar (SGD) 10 million (approximately US$7.5 million). (2) total gross assets of not more than SGD10 million (approximately US$7.5 million). (3) total number of employees of not more than 50.

Table 6 : Financial reporting frameworks in various jurisdictions, as of June 2016

Jurisdiction	**Accounting Standards**		
	Tier 1	**Tier 2**	**Tier 3/Tier 4/Tier 5**
United Kingdom	***EU adopted IFRS*** Public listed companies	***FRS 102, The Financial Reporting Standard*** *Applicable in the UK and Republic of Ireland*	***FRS 105 The Financial Reporting Standards applicable to the Micro-entities regime***
New Zealand	***New Zealand equivalents to International Financial Reporting Standards (NZ-IFRS)*** Entities that have public accountability or is a large for-profit public sector entity with total expenses > NZ$30million	***New Zealand equivalents to International Financial Reporting Standards Reduced Disclosure Regime (NZ-IFRS-RDR)*** Entities that do not have public accountability and for-profit public sector entities that are not large has total expenses < NZ$30million but > NZ$2million	**Special purpose financial reporting for prescribed SMEs**
Australia	***Australian Accounting Standards*** For-profit entities in the private sector that have public accountability and the Australian Government and State, Territory and Local Governments	***Australian Accounting Standards – reduced disclosure requirements*** For-profit private sector entities that do not have public accountability; all not-for-profit private sector entities; and public sector entities other than the Australian Government and State, Territory and Local Governments	**Special purpose financial reporting for non-reporting entities**
South Africa	***IFRS*** All companies with securities traded in public, companies which are not within the scope of the *IFRS for SMEs*	***IFRS for SMEs*** Entities without public accountability and that are required to or choose to prepare general purpose financial statements	***Own accounting policies*** SMEs that have a public interest score under 100 points and whose financial statements are internally compiled can use their own accounting policies

Table 6: Continues

Jurisdiction	Accounting Standards		
	Tier 1	**Tier 2**	**Tier 3/Tier 4/Tier 5**
Malaysia	***IFRS adopted as Malaysian Financial Reporting Standards*** Public entities	***Malaysian Private Entities Reporting Standard*** Private companies incorporated under the Companies Act 1965	-
Singapore	***IFRS adopted as Singapore Financial Reporting Standards*** Companies incorporated under the Singapore Companies Act	***IFRS for SMEs adopted as Singapore Financial Reporting Standards for Small Entities*** Small entities that, if not publicly accountable, publish general purpose financial statements for external users, and meet the definition of a 'small entity'	-
Thailand	***Thai Financial Reporting Standards*** Entities whose equity or debt instruments are traded in a public market, Entities whose operation is mainly holding assets in a fiduciary capacity, and Public companies under Public Company Act	***Thai Accounting Standard for Non-Publicly Accountable Entities***	-
Bangladesh	***IFRS adopted as Bangladesh Financial Reporting Standards*** All companies whose securities are traded in public	***IFRS for SMEs adopted as Bangladesh Financial Reporting Standard for SMEs*** Small and medium sized enterprises	-

Table 6: Continues

Jurisdiction	Accounting Standards		
	Tier 1	**Tier 2**	**Tier 3/Tier 4/Tier 5**
India	***Indian Accounting Standards*** All companies whose securities are traded in public	-	-
Nepal	***IFRS adopted as Nepal Financial Reporting Standards*** All listed companies and government owned business entities	***Nepal Accounting Standards with exemptions and simplifications for SMEs*** Small and medium sized enterprises	-
Pakistan	***IFRS*** Listed, public interest, and large-sized non- listed companies	***IFRS for SMEs*** Medium-sized entities	***Accounting and Financial Reporting Standards for Small Sized Entities*** Small sized entities
Sri Lanka	***IFRS adopted as Sri Lanka Accounting Standards (SLFRS)*** All companies whose securities are traded in public and specified business enterprises as defined by the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995	***IFRS for SMEs adopted as Sri Lanka Accounting Standards for SMEs*** SMEs that do not have public accountability	***Sri Lanka Accounting Standard for Smaller Entities (SLFRS for Smaller Entities)*** Smaller entities

Source: Author

South Asian countries

In both Sri Lanka and Bangladesh, accounting standards in Tier 1 and Tier 2 are fully aligned with *IFRS* and *IFRS for SMEs* respectively. Bangladesh made a minor modification to the accounting standard *IFRS for SMEs* while Sri Lanka accepted the standard without modification (International Financial Reporting Standards Foundation, 2016). Both countries used the public/non-public distinction for categorising companies in Tier 1 and Tier 2. Sri Lanka has introduced another Tier of accounting standard known as Sri Lanka Accounting Standards for Smaller Entities[24] with effect from 1 January 2016.

In India, all domestic companies whose securities trade in a public market other than the SME Exchange are required to use Indian Accounting Standards. SMEs can apply these accounting standards with some exemptions. (Institute of Chartered Accountants of India, 2016). India has not yet adopted either the *IFRS* or *IFRS for SMEs* (International Financial Reporting Standards Foundation, 2016). Nepal has adopted full *IFRS* in the form of the Nepal Financial Reporting Standards for all listed companies and government owned business entities. SMEs may apply existing Nepal Accounting Standards with certain exemptions and simplifications for SMEs (International Financial Reporting Standards Foundation, 2016). Nepal has not yet adopted the accounting standard *IFRS for SMEs*.

The current financial reporting framework in Pakistan consists of a three-tiered system. Pakistan has adopted Tier 2 and Tier 3 accounting and financial reporting standards for medium sized entities and small-sized entities respectively. Tier 2 accounting standards are based on the *IFRS for SMEs* (International Financial Reporting Standards Foundation, 2016). A small-sized entity is one which has paid up capital not exceeding Rs.25 million; and an annual turnover not exceeding Rs.100 million (Institute of Chartered Accountants of Pakistan, 2016). These small-

[24] An entity that is NOT any of the following is a smaller entity: an entity that had revenue in excess of Rs.100 million in the reporting period; an entity that had equity in excess of Rs.50 million at the end of the previous reporting period; a company that is required to prepare group financial statements by the law relating to companies; or an entity that holds assets in a fiduciary capacity as one of its primary business.

sized entities are required to apply Tier 3 accounting standards (International Financial Reporting Standards Foundation, 2016).

The review of financial reporting frameworks of various selected countries reveals that with the exemption of Australia, India, New Zealand and Thailand, other countries have already adopted the *IFRS for SMEs* as the tier 2 reporting standard in their financial reporting framework. Both Australia and New Zealand identified the Reduced Disclosure Requirements option as a better alternative to the *IFRS for SMEs* (Australian Accounting Standards Board, 2012) and decided against adoption of *IFRS for SMEs*. Many SMEs in New Zealand do not need to prepare general purpose financial statements. Rather, they prepare special purpose financial statements in compliance with taxation regulations. Similarly, SMEs in Australia have the option to prepare special purpose financial statements to meet the special purpose needs of the users.

In many countries, a third tier of reporting standards is provided for use by SMEs. However, the criteria used for classification of entities into tiers varies by countries. The United Kingdom has further simplified financial reporting requirements for micro-entities. South African SMEs have given an option to use their own accounting policies based on their public interest score. Sri Lankan SMEs can use Tier 3 reporting standards according to their size category.

3.7 Summary

This chapter examined the objectives and conceptual framework for financial reporting with the focus on users and uses of SME financial information. The definition of what constitutes an SME is complex. Country-specific definitions for SMEs are often based on size-thresholds such as number of employees, annual turnover, and total asset values. The IASB's SME definition in the *IFRS for SMEs* outlines that the standard is for entities that do not have public accountability and produce general purpose financial statements. According to this definition, SMEs can vary from those of very small entities to those of large unlisted companies. This broad SME definition appears to be geared towards the larger end of the SME spectrum. Researchers employ a range of different criteria to define SMEs, which makes comparison between studies problematic. The general purpose financial reporting model used in the *IFRS* and adopted for financial reporting by SMEs, emphasises decision-usefulness and stewardship as objectives of financial reporting for external users. However, the general purpose model may not be appropriate for SME financial reporting.

The literature on users and uses of SME financial statements is informed by a small number of studies. Notably, research on SME financial reporting in developing countries is limited. Most studies were undertaken more than ten years ago, so their findings were dated. Much of the extant literature focusses on SMEs in general and does not analyse results by the size of the entity.

Di Pietra et al. (2008), Evans et al. (2005), and Sian and Roberts (2009) identify significant gaps in the research literature on SMEs, they conclude that there is a lack of clarity about the users and their uses of SME financial statements. The results from the empirical studies on SME financial statement users shows a narrow range of user groups. Most studies elicit the views of a single user group and ignored other users of SME financial information. There are disagreements as to what extent SME financial information is used by different users for their decision making. Consequently, the fundamental question about who are the users and what are their uses of SME financial information, still remains unanswered. These deficiencies in the literature provide a rationale for this thesis.

An analysis of financial reporting frameworks in various countries reveals that most countries have adopted/adapted *IFRS* into Tier 1 reporting standards with the exceptions of India and Thailand. For most countries, Tier 2 reporting standards are also based on *IFRS for SMEs*. Whilst countries have adopted the *IFRS for SMEs*, with or without modifications, both developed economies (such as New Zealand and Australia) and developing economies (such as Thailand, India and Nepal) have not adopted *IFRS for SMEs*.

This chapter has explored the literature on SME financial reporting giving special emphasis on users and their financial information needs, as well as the financial reporting frameworks used by various jurisdictions around the world. The next chapter discusses the development of the accounting standard *IFRS for SMEs* and reviews studies on *IFRS for SMEs*.

CHAPTER FOUR

THE INTERNATIONAL FINANCIAL REPORTING STANDARD FOR SMES (*IFRS FOR SMES*)

4.1 Introduction

This chapter analyses the IASB's development of the *IFRS for SMEs* based on the comment letters received for both the Discussion Paper and the Exposure Draft (ED) of the standard. The chapter also examines studies on *IFRS for SMEs* focusing principally on the research questions for this thesis.

The *IFRS for SMEs* was an outcome of a five year development process pioneered by the IASB (International Accounting Standards Board, 2009a). This accounting standard was adopted in Sri Lanka for Sri Lankan SMEs as the *Sri Lanka Accounting Standards for SMEs* (*SLFRS for SMEs*) effective from 1 January 2012 (Institute of Chartered Accountants of Sri Lanka, 2012). The *IFRS for SMEs* follows a "one-size-fits-all" principle and it is for those companies that do not have public accountability,[25] regardless of size. However, the IASB's arguments about the need for the *IFRS for SMEs*, and the standard itself have been the subject of debate (see, for example, Aboagye-Otchere & Agbeibor, 2012; Chand et al., 2015; Devi & Samujh, 2015; Di Pietra et al., 2008; Eierle & Haller, 2009; Evans et al., 2005; Kiliç et al., 2016; Singh & Newberry, 2009). Opponents argue that the IASB used a very broad definition for SMEs making it difficult to design a single standard useful for a heterogeneous group of entities (see for example: Di Pietra et al., 2008; Evans et al., 2005; Holgate, 2007). Chand et al. (2015, p. 143) claim "this definition excludes consideration of the position of SMEs in most developing economies". It is also contented that the IASB did not give enough attention to the position of SMEs in most developing countries (Bohušová & Blašková, 2012; Chand &

[25] According to the IASB, an entity has public accountability if its debt or equity is traded or in the process of becoming traded in a public market or it holds assets in a fiduciary capacity for a broad group of outsiders as one part of its primary business. This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks.

Cummings, 2008; Chand et al., 2015; Devi & Samujh, 2014, 2015; Ram & Newberry, 2013; Singh & Newberry, 2009).

Section 4.2 provides a discussion focusing on the comment letters received by the IASB on the Discussion Paper and the ED of the accounting standard *IFRS for SMEs*. Section 4.3 reviews studies on the international financial reporting standards relating to the research questions of this thesis. Section 4.4 concludes the chapter.

4.2 Analysis of comment letters to Discussion paper and Exposure Draft of the accounting standard *IFRS for SMEs*

Shortly after its inception in 2001, the IASB began a project to develop accounting standards suitable for SMEs (Singh & Newberry, 2009). The IASB's objectives for developing *IFRS for SMEs* was to address the need for international comparability in the financial reporting of SMEs and to ease the financial reporting burden on SMEs (International Accounting Standards Board, 2009a). The IASB's decision to develop a separate set of standards for SMEs was driven by international bodies such as the World Bank and the European Commission (Singh & Newberry, 2009).

The IASB rejected a 'fresh start' approach because they believed it could have resulted in: different objectives of financial reports; different qualitative characteristics of financial information; different definitions of the elements of financial statements; and different concepts of recognition and measurement (International Accounting Standards Board, 2009a, p. 33). The IASB concluded that a 'fresh start' approach would be costly, time-consuming and pointless (International Accounting Standards Board, 2009a, p. 33).

In June 2004, IASB published a Discussion Paper titled *Preliminary Views on Accounting Standards for Small and Medium sized Entities* (International Accounting Standards Board, 2004). The Discussion Paper sought comments on the IASB's proposed approach to developing the SME standard. It set out nine issues, which were used to develop nine questions in the Discussion Paper (Ram, 2012). The IASB received 120 responses to the Discussion Paper (Singh & Newberry, 2009). Of these, 21 submissions came from 15 developing countries, and 77 submissions from 24 developed countries (Ram & Newberry, 2013). The largest number of submissions coming from the UK and European bodies (Ram & Newberry, 2013). The number and distribution of responses for each of the IASB's project document are summarised in Table 7 and Table 8.

Table 7: Comment letters from developing countries to IASB's project documents

Country	**Number of submissions**		
	Discussion paper	**Staff Questionnaire**	**Exposure Draft**
Argentina	2	1	1
Brazil	1	1	1
Cameroon	-	1	1
China	-	1	1
Bulgaria	1	-	-
Colombia	2	-	2
Costa Rica	1	-	2
Ecuador	-	-	1
El Salvador	-	-	1
Fiji	-	-	1
India	1	2	2
Indonesia	-	-	1
Iran	-	-	1
Jamaica	-	-	1
Kenya	-	1	2
Korea	1	1	3
Kyrgyz republic	-	1	-
Malawi	1	-	1
Malaysia	2	3	1
Mexico	1	1	1
Mozambique	2	-	-
Pakistan	1	1	2
Philippine	-	-	1
Poland	-	-	1
Russia	1	1	2
South Africa	3	4	5
Tanzania	-	-	1
Thailand	-	-	1
Tunisia	-	-	1
Uruguay	-	1	1
Venezuela	-	-	1
Zambia	1	-	1
Total	21	20	41

Source: Ram (2012)

Table 8: Comment letters from developed countries and other organisations to IASB's project documents

Country	Number of submissions		
	Discussion paper	**Staff Questionnaire**	**Exposure Draft**
Australia	8	3	7
Austria	1	2	4
Barbados	-	-	1
Belgium	4	2	1
Brussels	-	1	-
Canada	2	1	5
Czech Republic	-	1	-
Denmark	1	3	2
Finland	1	1	2
France	2	4	9
Germany	12	8	17
Greece	1	-	-
Hong Kong	1	1	2
Ireland	-	1	3
Israel	1	1	1
Italy	4	3	8
Japan	3	3	1
Malta	1	-	-
Netherlands	2	2	3
New Zealand	4	4	1
Norway	1	1	2
Portugal	1	1	-
Singapore	1	1	-
Spain	1	2	3
Sweden	3	2	1
Switzerland	2	1	-
UK	19	6	21
United Arab Emirates	-	-	1
US	1	5	6
Total Submissions from developed countries	77	60	101
Total Submissions from developing countries (from Table 7)	21	20	41
Submissions from global/international organisations	7	9	13
Submissions from European bodies	13	11	5
Submissions from unknown location	2	1	1
Total submissions received	**120**	**101**	**161**

Source: Ram (2012)

In April, 2005, a Staff Questionnaire on Recognition and Measurement Simplification was issued for public comment. The IASB received 101 submissions from 40 countries in response to the staff questionnaire (Ram, 2012). Of these, 20 submissions came from 14 developing countries, and 60 submissions from 25 developed countries, with the largest number of submissions coming from the European professional organisations and the global and international organisations (Ram, 2012).

In 2007, the Exposure Draft (ED) of the *International Financial Reporting Standard for Small and Medium Enterprises* was issued for public comment (International Accounting Standards Board, 2007). It was based upon the same theoretical concepts as the full *IFRS*. The IASB believes that the information needs of external users of SME financial statements are similar in most ways to those of publicly accountable entities' financial statements (International Accounting Standards Board, 2004). Therefore, the content of the accounting standards for SMEs was extracted from the full *IFRS* in a so-called 'top-down approach (Baskerville & Cordery, 2006; Devi & Samujh, 2015; Fearnley & Hines, 2007; Quagli & Paoloni, 2012; Santucci, 2010).

The ED of *IFRs for SMEs* attracted 161 submissions from 51 countries. 41 submissions came from 29 developing countries, and 101 submissions from 22 developed countries, with the largest number of submissions coming from the UK and Germany (Ram, 2012). However, as can be seen from the Table 7, no submissions were received from Sri Lanka on the IASB's project of *IFRS for SMEs*. Overall, there was few responses from developing countries.

4.2.1 Developing countries and their needs

The IASB said it was developing the SME standard for both SMEs in developed and developing economies, but the Discussion Paper asked no questions specific to developing countries. Further, the staff summary prepared by the IASB based on responses to the Discussion Paper did not report any comments about developing countries (Ram, 2012). However, comments on the Discussion Paper highlighted issues of accessibility, comprehensibility, language barriers and the applicability of international accounting standards to developing countries. There was also a call to involve developing country professional bodies in the project (Singh & Newberry, 2009). Respondents to the Staff Questionnaire argued that the recognition and measurement requirements arising from fair value accounting were complex and burdensome because developing countries lacked active markets, expertise, and resources. Although the ED did not seek responses on developing country issues, 19 submissions mentioned these concerns. Five of these submissions were from developing countries, 10 from developed countries, three from international organisations, and one from an international accounting firm. Table 10 provides a summary of responses to ED of the accounting standard *IFRS for SMEs* commenting on developing countries.

Eight respondents to the ED commented that developing countries lacked active markets to allow fair value determinations of most of their assets. For example, the International Network of Accountants and Auditors (2007, p. 10) highlighted that "many SMEs, particularly in emerging economies, do not have access to working markets from where they could obtain information regarding the fair value of their assets". Others argued that some developing countries do not have the support of specialists needed to assist in fair value determination, thus potentially undermining the credibility and reliability of information through lack of precision and excessive subjectivity (International Federation of Accountants, 2007; Singh & Newberry, 2009; South African Institute of Chartered Accountants, 2007).

Table 9 : Summary of responses to Exposure Draft IFRS for SMEs commenting on developing countries

Organisation	Country	Affiliation	Developing countries' needs	Small entities	Lack of market	Lack of expertise/ resources	Language barrier	Access to IFRS
Responses from developing countries								
University of Cape Town	South Africa	Academic				X		
Fiji Institute of Accountants	Fiji	Professional Body				X		
South African Institute of Chartered Accountants	South Africa	Professional Body				X		
Malaysian Accounting Standards Board	Malaysia	Standard Setter			X			
Federation Argentina de Consejos Profesionales de Ciencias Economicas	Argentina	Professional Body	X		X			
Responses from developed countries, international organisations and accounting firms								
Inter-American Accounting Association	Canada/US	Professional Body			X			
Institute of Chartered Accountants of Scotland	UK	Professional Body	X					
New York Society of CPA's	US	Professional Body			X			
Certified General Accountants Association of Canada	Canada	Professional Body						X
Ernst & Young	Global	Accounting Firm	X					

Table 9: continues

Organisation	Country	Affiliation	Developing countries' needs	Small entities	Lack of market	Lack of expertise/ resources	Language barrier	Access to IFRS
Consiglio Nazionale dei Dottori Commercialisti and the Consiglio Nazionale dei Ragionieri	Italy	Professional Body			X			
Association of Chartered Certified Accountants (UK)	UK	Professional Body		X				X
International Network of Accountants and Auditors	UK	Professional Body			X	X		
European Accounting Association	EU	Regional Body	X	X				
The Confederation of Asian and Pacific Accountants		Regional Body		X		X	X	
Hong Kong Institute of Certified Public Accountants	Hong Kong	Professional Body		X				
International Federation of Accountants		International Body		X	X			
Institute of Chartered Accountants of Barbados	Barbados	Professional Body	X		X	X		
London Society of Chartered Accountants	UK	Professional Body		X				

Source: Adapted from Singh and Newberry (2009, pp. 505-506)

Six respondents commented on the applicability of *IFRS for SMEs* to small entities in developing countries (Singh & Newberry, 2009). The Hong Kong Institute of Certified Public Accountants (2007) and Association of Chartered Certified Accountants (2007) argued that the proposed *IFRS* was not for small entities at all, but rather was directed at medium-sized non-publicly accountable entities. As a consequence, the International Federation of Accountants (2007, p. 4) state that "it may prove ill-suited on cost-benefit grounds for application by the great majority of small entities that produce general purpose financial statements for external users, especially those operating in developing nations".

Six respondents suggested developing countries may lack the resources, expertise, and access to information necessary to prepare financial statements in accordance with the *IFRS* (International Network of Accountants and Auditors, 2007). The ED's cross-references to the *IFRS* would, therefore, increase the burden on those in developing countries because they would need to know the *IFRS* to apply the SME requirements (Confederation of Asian and Pacific Accountants, 2007).

Several submissions highlighted specific consideration of developing countries' needs. The ED omitted simplifications of several matters including hyperinflation and agriculture because these were deemed not relevant for SMEs. The IASB proposed cross-reference to the *IFRS*, if SMEs should encounter such issues. Ernst & Young (2007) argues that those matters are relevant in developing countries, and therefore that simplified accounting guidance on accounting in hyperinflationary economies and on agriculture is necessary. In this context, Institute of Chartered Accountants of Barbados (2007, p. 1) notes:

> The burden of complying with full IFRS is clearly greater for SMEs in developing markets operating in emerging economies. The SME standards as drafted do very little to reduce this burden. The Board's concern in the SME accounting project should be to develop standards for those jurisdictions where the need is greatest and not for jurisdictions which already have their own standards and standard-setting bodies.

4.2.2 IASB's Framework, SME users and their information needs

Association of Finnish Accounting Firms (2007) commented to the IASB that the ED on *IFRS for SMEs* had a very strong focus on the needs of capital markets and investors. The IASB's 1989 conceptual framework was biased towards large publicly accountable entities, and thus was not suitable for SMEs (Evans et al., 2005). Because the ED was merely a scaled-down version of *IFRS* for listed companies, its requirements would be burdensome for SMEs (Lungu, Caraiani, & Dascalu, 2007). Di Pietra et al. (2008) state that the principles of the framework need to be tailored to better meet the characteristics of SMEs. SME users' needs are less complicated than those of large firm information users (Lungu et al., 2007). Several problems might appear during the application of the "top-down approach", even though simplifications had been made (Lungu et al., 2007). SMEs are different from large and listed entities in their reporting objectives, accountability relationships, and strategies. For example, many SMEs have little or no separation between ownership and control, and they often focus more on survival than profit maximisation or growth (Evans et al., 2005).

The responses to the Discussion Paper and ED came predominantly from the accounting profession, and regulators, rather than users and preparers of SME financial statements (Di Pietra et al., 2008). Schiebel (2008) argues the IASB had relied on the responses of accounting regulators, the profession, and academics, when the IASB should have focused on the users and preparers of SMEs' financial statements. The director of the *IFRS for SME* project did however, establish an informal user panel to obtain comments from the users' perspectives (Ram & Newberry, 2013). Some board members of IASB criticised the panel membership because it consisted of investment and security analysts who dealt mostly with large entities and so were deemed to be inappropriate individuals to comment on SMEs (Ram & Newberry, 2013). What this means is that inadequate user involvement in the accounting standard setting process could impair the decision usefulness of accounting information for users (Durocher, Fortin, & Côté, 2007; Harding & McKinnon, 1997). This raises an important question relating to the due process followed in the IASB's *IFRS for SMEs*. The due process in accounting standards setting is for the standard setter to keep its constituencies informed of matters under consideration and to provide them with adequate opportunities to present their views (Bradbury & van Zijl, 2006; Ram & Newberry, 2013; Suchman, 1995; Tandy & Wilburn, 1992).

4.2.3 Appropriateness of SME definition given by the IASB

The IASB used a very broad definition for SMEs making it difficult to design a single standard useful for a heterogeneous group of entities (Di Pietra et al., 2008). The IASB decided to define SMEs as entities without public accountability and no size criteria was provided. Holgate (2007) indicates that the IASB definition of an SME as an entity without public accountability would include private equity companies and other large, privately-held companies. The size of these large, privately-held companies might be equal to companies listed in capital markets and have economic significance in terms of "an employer, supplier, or taxpayer, or other stakeholder" (Holgate, 2007, p. 82). Holgate questions whether this form of entity should be allowed to apply the *IFRS for SMEs*. The IASB definition also implies that the standards would have a large audience with differing information needs, especially between the smallest and largest SMEs (Evans et al., 2005). As a result, the standards might not be able to meet the needs of the different financial statement user groups (Evans et al., 2005). Furthermore, the term 'SME' is confusing as it suggests a size, not a reference to non-public accountable entities (Evans et al., 2005).

In order to determine the content of the accounting standards, the IASB used an SME with 50 employees as a model (International Accounting Standards Board, 2007). When presented with the assertion that it was unrealistic to design a single standard that would be applicable to any sized private entity, the IASB (2009) argued that the *IFRS for SMEs* was an appropriate standard for any entity which was required, or elected to, publish general purpose financial statements, regardless of the entity's size. Although the IASB claimed that the standard was applicable to any sized entities, some of its measurement principles are considered to be too burdensome for micro-entities or even for SMEs with up to 50 employees, and thus it was not suitable for smaller SMEs (International Federation of Accountants, 2007; United Nations Conference on Trade and Development, 2007).

Neag, Masca, and Pascan (2009) disagree with the IASB's argument that the *IFRS for SMEs* are appropriate to micro entities. They contend that *IFRS for SMEs* is more appropriate for larger unlisted entities. Therefore, there should be recognition of micro-entities as a distinct category that has different financial informational needs. Neag et al. (2009) argue in favour of a separate, less complex standard for micro entities and agrees with Evans et al. (2005) who recommend that the IASB develop a three-tier accounting standard system. The United Nations (2010) also challenges the suitability of the *IFRS for SMEs* for smaller enterprises. It also recommends the development of a third-tier or level of financial standards for micro-entities that would use a simplified accruals-based accounting, closely linked to cash transactions (United Nations, 2010).

After considering comments received at two stages of the standard development process (Discussion Paper and ED of *IFRS for SMEs*), the IASB issued the final version of the International Financial Reporting Standards for Small and Medium-sized Entities in July 2009 (International Accounting Standards Board, 2009b). Before being finalised, the standard was tentatively renamed 'IFRS for Private Entities' and then 'IFRS for Non-Public Accountable Entities' (Devi & Samujh, 2015; Ram & Newberry, 2013). However, it was issued as *IFRS for SMEs*.

The content of the *IFRS for SMEs* is based on the full *IFRS*, with simplifications for both disclosure requirements and measurement and recognition methods, for example,

- topics less relevant to SMEs are excluded, such as earning per share, segment information and interim reporting (International Accounting Standards Board, 2009a, p. 32)
- disclosure requirements are reduced, from around 3,000 items in the full IFRS to approximately 300 items in the *IFRS for SMEs* (Pacter, 2011)
- some options in relation to fair value accounting are not available e.g. revaluation of property, plant and equipment and intangible assets
- some measurement and recognition methods are simplified in certain areas, e.g.
    - basic financial instruments e.g. cash and trade accounts receivable and payable are measured at amortised cost

- borrowing costs and research and development costs must be recognised as expenses (International Accounting Standards Board, 2009a, p. 39:40)

4.3 Research on *IFRS for SMEs*

Since the publication of *IFRS for SMEs* here has not been a large number of articles produced on its development, application or implementation. What literature exists, consists of empirical and theoretical studies carried out in different locations. Table 10 presents the published research on *IFRS for SMEs* relevant to the scope of this thesis, and the research questions of this thesis.

Table 10 : Prior research on *IFRS for SMEs* (after issuance of the accounting standard *IFRS for SMEs*)

Region	**Author/s and the year of publication**	**Location**	**Methodology/Sample**	**Main findings**
EU	Eierle and Haller (2009)	Germany	Questionnaire survey of 410 SMEs	SMEs do not consider their international suppliers and customers as major users of their financial statements and see little or no need to provide internationally comparable financial statements. Size effects are revealed with regard to the structure of entities, their international exposure and the relevance of particular accounting issues.
	Paseková, Müllerová, Strouhal, and Čiževská (2010)	Czech Republic and Ukraine	Questionnaire survey of 115 SMEs in the Czech Republic and 50 SMEs in Ukraine	SMEs in both countries are only weakly interested in reporting under IFRS. The majority of companies use accounting only to provide data which are necessary for calculation of the tax base.
	Neag (2010)	Romania	Questionnaire survey of SMEs	*IFRS for SMEs* should not be compulsory for all entities as many of the requirements are not applicable for entities with a simple business model.
	Albu et al. (2010)	Romania	Literature review and 7 interviews with auditors, preparers, professional bodies	Application of IFRS for SMEs would affect the accounting profession and education.
	Bunea et al. (2012)	Romania	Questionnaire survey of accounting professionals	Professional accountants agree with SMEs financial reporting in accordance with European directives
	Lapteş and Popa (2012)	Romania	Questionnaire survey of 38 professional accountants	Professional accountants do not consider *IFRS for SMEs* as an alternative for improving the SMEs accounting system in Romania.

Table 10: continues

Region	Author/s and the year of publication	Location	Methodology/Sample	Main findings
EU	Quagli and Paoloni (2012)	European countries[26]	Questionnaire survey of responses from 81 preparers and 14 users[27]	Preparers manifest stronger opposition to the *IFRS for SMEs*, while users are more favourable.
	Albu et al. (2013)	Czech Republic, Hungary, Romania, and Turkey	Five interviews with preparers, six with auditors, four with users, and eight interviews with professional and regulatory bodies	Preparers, professional bodies and regulators show support for convergence. In contrast, users and auditors favoured adoption of *IFRS for SMEs*
	Uyar and Güngörmüş (2013)	Turkey	Questionnaire survey of 128 accounting professionals	Inadequacy of accounting personnel's training and lack of training programmes are obstacles to implementation of *IFRS for SMEs*.
	Turegun and Kaya (2014)	Turkey	Questionnaire survey of 217 accounting professionals	Turkish SMEs are not ready for implementing *IFRS for SMEs* due to application and implementation issues of the standard.
	Kiliç et al. (2016)	Turkey	Questionnaire survey of 198 SMEs	Preparedness of the SMEs for *IFRS for SMEs* is low in Turkey.

[26] European countries include Germany, Austria, Spain, the UK, Belgium, Italy, Luxembourg, France, Greece, Denmark, The Netherlands, Finland, Portugal, Sweden and Poland.

[27] Preparers and users were selected from responses to the questionnaire on the public consultation of the *IFRS for SMEs* promoted by the European Commission.

Table 10: continues

Region	Author/s and the year of publication	Location	Methodology/Sample	Main findings
Africa	Van Wyk and Rossouw (2009)	South Africa	Questionnaire survey of 242 preparers of SMEs financial statements	IFRS for SMEs is not deemed to be relevant to smaller and micro-entities in South Africa.
	Aboagye-Otchere and Agbeibor (2012)	Ghana	Questionnaire survey of 149 small businesses	SMEs in Ghana have limited international structure and activities. Therefore, no need for internationally comparable financial reporting information. In total, 19 of the 27 issues addressed by the Standard and assessed in the study were found to be irrelevant to SMEs in Ghana.
Oceania	Laing (2012)	Australia	Three case studies of family owned SMEs	The cost of meeting the financial reporting requirements is a burden for SMEs.
	Chand et al. (2015)	Fiji	Questionnaire survey of 155 professional accountants	*IFRS for SMEs* may not be appropriate to all SMEs as they found it costly to comply with *IFRS for SMEs*
Asia	Devi and Samujh (2014)	ASEAN countries	Critical analysis of literature	The *IFRS for SMEs* is not appropriate for ASEAN countries

Source: Author

4.3.1 Need for international accounting standards for SMEs

In its basis for conclusions on the *IFRS for SMEs*, the IASB argues that the need for global SME financial reporting standards arises out of the international structures and activities of SMEs and their financial statement users (International Accounting Standards Board, 2009a, p. 16). The IASB asserts that SMEs deal with financial institutions, suppliers, customers, credit rating agencies, venture capital firms and investors outside their home countries (International Accounting Standards Board, 2009a, p. 16). Therefore, entities that undertake international activities may find the compliance with internationally accepted standards advantageous in making their financial statements more reliable internationally (Guerreiro, Rodrigues, & Craig, 2008; Murphy, 1999).

According to Hodgdon, Tondkar, Adhikari, and Harless (2009), entities with international operations face different and challenging financial reporting regulations of the countries in which they operate, so those entities may have a greater incentive to adopt international financial reporting standards. Furthermore, entities that try to obtain financing from international banks and other international financial institutions find it beneficial to comply with international reporting standards (Dumontier & Raffournier, 1998). Similarly, entities which have foreign partners or export activities are more likely to apply a new financial reporting standard set (Atik, 2010).

However, it is claimed that SMEs do not engage in international activities to the extent envisaged by the IASB (Aboagye-Otchere & Agbeibor, 2012; Eierle & Haller, 2009; Lungu et al., 2007). Eierle and Haller (2009) analyse the international orientation of German SMEs. The responses to the questionnaire reveal that German SMEs have considerable cross-border activities, especially relating to exports and imports, other international activities are for most entities of minor importance. Comparatively, large SMEs conduct more cross-border activities than small SMEs.

Burpitt and Rondinelli (2000) claim that the decision to export is a difficult one for most small businesses as they often lack the resources needed to engage in exporting. Barriers to internationalisation as perceived by SMEs include: limited financial resources; high costs of selling abroad; limited access to capital; limited knowledge of overseas market opportunities; and the lack of government assistance to export (see, Burpitt & Rondinelli, 2000; Coviello & McAuley, 1999; Shaw & Darroch, 2004; Ward, 1993).

Despite the importance of exports and imports reported by about half of the responding German SMEs do not see any need to provide internationally comparable financial accounting data. (Eierle & Haller, 2009). Therefore, Eierle and Haller (2009) suggest that German SMEs do not consider foreign suppliers and customers as major users of their financial statements. Similarly, Kiliç et al. (2016) find large SMEs in Turkey have more foreign activities than small SMEs. Hence, the *IFRS for SMEs* seems to be more advantageous for and applicable to large SMEs. Lungu et al. (2007) claim that international accounting standards may not be needed for small SMEs, or those that are not interested in growing or taking part in international activities of any sort.

The Conseil National de la Comptabilité (2008) surveyed French companies to find that the international activities of French businesses are concerned primarily with imports and exports. These international activities however, do not necessarily result in a need for international SME accounting standards as customers and vendors are not primary users of SME financial statements. Aboagye-Otchere and Agbeibor (2012) assess the suitability of the accounting standard *IFRS for SMEs* in Ghana. They conclude that SMEs in Ghana have limited international structures and activities and so do not need internationally comparable financial reporting information.

Contrary to Eierle and Haller (2009) and the Conseil National de la Comptabilité (2008), a survey of SMEs in six EU countries: France; Germany; Italy; the Netherlands; Spain; and the UK, establishes that most entities (more than 80 percent in each country and irrespective of size) are in support of internationally comparable accounting rules (Mazars, 2008).[28] While a consensus exists, regarding a need for

[28] Mazars is a group of accountants located in Thailand who provides a range of services to their clients including accounting, taxation, audit, and business advisory services (Mazars, 2017).

international accounting standards, the reasons vary from one country to another. More than 60 per cent of French SMEs identify the necessity of breaking the link between tax rules and accounting and the possibility of being able to provide all external parties with a single set of financial statements as key advantages they would expect to derive from international accounting standards (Mazars, 2008). Two-thirds of German SMEs consider that international accounting standards would primarily improve management and internal communications within their group (European Union) (Mazars, 2008).

Although there exists some literature on the need of the international financial reporting standards for SMEs (Aboagye-Otchere & Agbeibor, 2012; Conseil National de la Comptabilité, 2008; Eierle & Haller, 2009; Kiliç et al., 2016; Mazars, 2008), they are few, context specific, use varying SME definitions and provide mixed evidence. Some studies (Conseil National de la Comptabilité, 2008; Mazars, 2008) are based on the Exposure Draft; not the final version of *IFRS for SMEs* issued as a standard. There is a lack of literature on the subject in developing and Asian countries context.

4.3.2 Relevance of the content of the *IFRS for SMEs*

In developing the *IFRS for SMEs*, the IASB started from full *IFRS* and omitted issues that were deemed to be irrelevant to SMEs (International Accounting Standards Board, 2009a). However, the IASB's efforts in this direction have been criticised. For example, Van Wyk and Rossouw (2009) consider that some of the topics were only "partially applicable" to SMEs and SMEs were not necessarily involved in the industries to which these topics referred. Furthermore, their findings reveal that certain aspects of impairment of assets, related party disclosure, intangible assets, government grants, non-current assets held for sale and discontinued operations, foreign exchange rates, and employee benefits were not really applicable to SMEs (Van Wyk & Rossouw, 2009).

Similarly, Aboagye-Otchere and Agbeibor (2012) find more than two-thirds of the accounting issues addressed in the *IFRS for SMEs* are of little or no relevance to SMEs in Ghana. Eierle and Haller (2009) ascertain that three-quarters of German SMEs seldom, if ever, encounter the following accounting issues: the sale of business/discontinued operations, leases in which the company acts as lessor, share-based payments, transactions to hedge price or exchange risks (except foreign exchange risk in a foreign currency position), investment in listed associates and listed subsidiaries. (Eierle & Haller, 2009) A clear size effect was found in most of the issues. Overall, the level of relevance or frequency is generally lower for small SMEs than for large SMEs (Eierle & Haller, 2009).

Other research based on the *IFRS for SMEs* does not specifically investigate the relevance of the content of *IFRS for SMEs*. Paseková et al. (2010) declare only a small percentage of SMEs in the Czech Republic and Ukraine are really interested in providing a "true and-fair view". The majority of companies use accounting just to provide data which are necessary for calculating tax liability. SMEs in both countries are only weakly interested in reporting under *IFRS for SMEs* (Paseková et al., 2010).

Neag (2010) conducts research in Romania to garner the opinions of the preparers of financial statements regarding *IFRS for SMEs*. The preparers believe that the *IFRS for SMEs* should not be compulsory for all entities, as many of the requirements are not applicable for entities with a simple business model. Another study, using textual analysis of Romanian accounting regulation and *IFRS for SMEs* together with interviews, concludes that there are many inconsistencies in Romanian legislation when compared to *IFRS for SMEs* and that the application of *IFRS for SMEs* would have implications on the accounting profession and education (Albu et al., 2010). A majority of the professional accountants in Romania do not consider *IFRS for SMEs* as an alternative for improving financial reporting by SMEs (Lapteş & Popa, 2012). Similarly, professional accountants in Romania reveal that a more simplified financial reporting system is needed for SMEs and they preferred SME financial reporting in accordance with European directives (Bunea et al., 2012).

Quagli and Paoloni (2012) selected users and preparers from those who had responded to a public consultation questionnaire promoted by the European Commission on the *IFRS for SMEs*. They ascertain preparers manifest stronger opposition to the *IFRS for SMEs*, than users, who are more favourably disposed towards it. Further, they claim German-speaking countries and Latin countries show much less appreciation for the standard than did Anglo−Nordic countries. According to them:

> The reasons are that both bring accounting and political diversity in the three contexts: the Latin and German Countries are more oriented toward an active role of EU and the maintenance of a "legal" value of financial statements while the Anglo–Nordic are more diffident toward EU and traditionally oriented to a strong informative role of financial statements (Quagli & Paoloni, 2012, p. 151).

4.3.3 Cost and benefit of international financial reporting standards for SMEs

The costs and benefits of financial reporting can be associated with preparers of financial statements, users of financial statements, auditors, and standard setters (Litjens et al., 2012). The costs-benefit balance of financial reporting are met when the benefits derived from information exceed the costs borne or imposed upon the enterprise in the preparation of financial statements (International Accounting Standards Board, 2009b, p. 14). It is therefore clear that the financial reporting requirements should only be imposed if the benefits exceed the costs. Cost-benefit considerations are included in the IASB's framework as part of the standard-setter's responsibilities (Schipper, 2010). Therefore, the standard setter is supposed to consider whether the benefits arising from a given standard justify the costs associated with that standard (Schipper, 2010).

4.3.3.1 Benefits of international financial reporting standards

The benefits are associated with what the enterprises and users of financial statements gain from the use of the financial statements in monitoring and making decisions. The IASB believes that the adoption of *IFRS for SMEs* will enhance SMEs' access to international finance through preparing internationally comparable financial information (International Accounting Standards Board, 2009b). However, Sy and Tinker (2013) argue that improvement in global comparability may benefit multinational corporations, and their Big Four accounting firms, but companies with primarily domestic operations will not receive the same benefit. The Confederation of Asian and Pacific Accountants (2003) argues that generally the benefits will increase with the number and diversity of users, the satisfaction of their information needs, and the existence of qualitative characteristics of the information, such as reliability, relevance, and timeliness.

Furthermore, benefits associated with accounting standards include the credibility of financial reporting, the functioning of capital markets, access to and cost of capital, and management decision making (International Accounting Standards Board, 2009b; Litjens et al., 2012; Schipper, 2010). However, findings from 60 firms drawn from among Australia's top 200 corporations, Jones and Higgins (2006) report the majority of respondents do not feel their companies would realise these benefits from them adopting the *IFRS*.

4.3.3.2 Costs of international financial reporting standards

Costs associated with financial reporting are the costs of developing and implementing financial reporting requirements such as accounting standards, maintaining compliances, and analysing information (Litjens et al., 2012). Costs may also include adverse effects on an enterprise or its stockholders through disclosing information, and the collective time needed to understand and use the information (Schipper, 2010). Evidence suggests that the size of the enterprise has an impact on the cost of producing financial statements (Jarvis & Collis, 2003b). As SMEs are unable to spread the costs across large scale of operations, they are typically subject to proportionately higher costs than larger firms (Kitching, 2006; Stainbank & Tafuh, 2011). Keasey and Short (1990) investigated the accounting burden in a sample of 100 small firms in the UK and claim that the size of the company was a significant factor in the cost-benefit balance.

The adoption of *IFRS* is therefore, likely to have a large impact on firm's financial reporting costs (George, Ferguson, & Spear, 2013; Hail, Leuz, & Wysocki, 2010; Jermakowicz & Gornik-Tomaszewski, 2006). Following the mandatory adoption of *IFRS* within the EU per-firm estimates of transition costs in order of 0.31 per cent of total sales for smaller firms, and up to 0.05 per cent for larger firms were calculated (Institute of Chartered Accountants in England and Wales, 2007). A survey of professional auditors at a Big Four accounting firm shows that auditors believe that certain aspects of the *IFRS* reporting requirements require greater auditor effort and expertise to ensure adequate compliance (George et al., 2013). As a result, auditors charge higher fees to compensate for their additional efforts (Charles, Glover, & Sharp, 2010; George et al., 2013; Ghosh & Pawlewicz, 2009). Similarly, Cameran and Perotti (2014) investigate how the introduction of the international financial reporting standards affects auditors' fee determination in the banking industry in Italy. Their results indicate that higher fees are paid after the adoption of *IFRS*.

Compliance with accounting standards, such as the *IFRS for SMEs is* also perceived to be costly to SMEs. SMEs usually do not have in-house qualified accountants and thus depend on their external professional accountants to prepare financial statements (Carsberg et al., 1985; Kitching et al., 2011; Marriott & Marriott, 2000; Professional Oversight Board for Accountancy, 2006). SMEs may lack accounting skills and infrastructure to implement accounting regulations and standards (Dang-Duc, 2011). As a result, SMEs incur higher accountancy fees (Eierle & Haller, 2009; Stainbank & Tafuh, 2011). Accountants' limited knowledge of *IFRS* is one of the main problems faced by developing countries when adopting *IFRS* (Halbouni, 2005). In Turkey, Uyar and Güngörmüş (2013) used a questionnaire survey to investigate basic knowledge and perceptions of professional accountants regarding the accounting standard *IFRS for SMEs*. Their findings suggest that the majority of the participants are not aware of the key differences between the *IFRS* and the *IFRS for SMEs*, and the simplifications made in the *IFRS for SMEs*. Further, the inadequacy of accounting personnel's training and a lack of training programmes arranged by professional bodies are serious obstacles in implementing the standard. Another study with professional accountants in Turkey finds that SMEs are not ready to apply and implement the *IFRs for SMEs* (Turegun & Kaya, 2014).

SMEs have difficulties in obtaining competent persons because of their inability to offer competitive salaries and benefits (Jennings & Beaver, 1997). Compliance with accounting standards is likely to place cost burdens on the SMEs and they are not compensated adequately by the benefits that owner-managers or external users may gain from the provision of such information (Dang-Duc, 2011). Maingot and Zeghal (2006) argue that the main disadvantage of financial reporting among SMEs in Canada was the cost in monetary terms as well as in terms of time and inconvenience. However, they do not explicitly discuss the relationship between the costs and the benefits of financial reporting in their study.

In response to the *ED: IFRS for SMEs,* Di Pietra et al. (2008) note that costs are perceived to exceed benefits, and therefore, large SMEs are more favourably disposed towards the standard than the small SMEs (Di Pietra et al., 2008). They recommend modifying the disclosure, recognition or measurement principles in the standard. Further, Di Pietra et al. (2008) comment that the standard for SMEs should not be based on the concepts and principles in the IASB framework or other existing standards. Field testing with 15 German SMEs, resulted in negative views as most participating SMEs consider the proposed standards too costly to apply (Accounting Standards Committee of Germany, 2008). Also in Germany, Eierle and Haller (2009) find that higher costs were incurred by fair value accounting for plant, property and equipment. Firms may need to increase their use of outside technical advice in areas of uncertainty, such as using independent valuers of the fair value of assets (Taylor, 2009).

Chand et al. (2015) gather opinions from professional accountants in Fiji on the costs of compliance with *IFRS for SMEs*. Their results show 66.9 per cent of respondents strongly agree with the statement that the costs of complying with *IFRS for SMEs* are far greater than the corresponding benefits. Further, 69.3 per cent of respondents recognise that the information required to apply *IFRS for SMEs* is not available, or is available only with undue cost or effort (Chand et al., 2015). Additionally, 74.5 per cent of respondents indicate that the use of fair value accounting in *IFRS for SMEs* imposes significant additional costs on preparers and is not justified on cost/benefit grounds. To make implementation more cost effective for SMEs in Fiji, 66.7 per cent of the respondents hold the view that additional exemptions need to be granted in *IFRS for SMEs* (Chand et al., 2015).

Pacter (2007, pp. 360-362) outlines some salient concerns associated with the application of fair value accounting in developing countries, which includes: inactive market in developing countries; cost of applying recognition and measurement principles; shortage of skilled valuers; government controlled markets; weak regulatory environment; and lack of valuation standards and guidance. Based on a survey of 156 practising auditors in Sri Lanka, Kumarasiri and Fisher (2011) examine the issues and challenges of fair value information. Specific challenges of concern to Sri Lankan auditors include: lack of auditor knowledge, the prevalence of inactive markets, difficulties associated with the variation in techniques used to ascertain fair values across different industries, general complexities in ascertaining fair values, and the incorporation of future events and conditions into valuations (Kumarasiri & Fisher, 2011).

Albu et al. (2013) investigate the perceptions of stakeholders involved in financial reporting in four emerging economies (the Czech Republic, Hungary, Romania, and Turkey) about costs, benefits, and strategy of implementing the *IFRS for SMEs*. Albu et al. (2013) find the main costs of the application of *IFRS for SMEs* are related to training accountants and the possible emergence of separate reporting systems for financial accounting and taxation. Other perceived costs relate to upgrading information technology systems and paying external experts and auditors.

A study conducted by Devi and Samujh (2014) on the suitability of *IFRS for SMEs* to the ASEAN countries ascertain several countries are not ready to adopt or implement the *IFRS for SMEs*. ASEAN countries do not have the necessary resources or infrastructure to support implementation. Further, the *IFRS for SMEs* does not reflect the culture of accounting and business practices existing in those countries and capital markets assumption does not sit well with the SMEs (Devi & Samujh, 2014, p. 3). On these grounds Devi and Samujh (2014) argue that the *IFRS for SMEs* would be more of a burden than a benefit to ASEAN members.

Using a multiple case study approach, Laing (2012) assesses the relevance of *IFRS for SMEs* in Australia. The key finding is that SME's are strongly influenced by the prevailing taxation regulations rather than by any form of accounting standard requirements. The cost of meeting the financial reporting requirements is a burden SME's are ill prepared to bear and such costs are not justified by any claim of being useful to the owners or other possible stakeholders.

The extant literature on *IFRS for SMEs* is sparse and mostly conducted through questionnaire surveys. Comprehensive evidence is missing regarding the accounting topics that are relevant to SMEs and there is a lack of empirical evidence on the costs and benefits of the *IFRS for SMEs*. This thesis fills this gap by adopting both quantitative and qualitative methods to examine the need of internationally comparable financial information for SMEs in Sri Lanka, focusing specific costs and benefits and the relevance of the content of *IFRS for SMEs*.

4.4 Summary

It was evident from the analysis of the IASB project that developing countries were not sufficiently involved in developing the accounting standard *IFRS for SMEs*. The IASB's consultative documents (Discussion Paper; staff questionnaire on recognition and measurement; and drafted), did not contain any questions about developing countries. Furthermore, in analysing the responses to these documents, the perspectives of developing countries were not considered by the IASB (Singh & Newberry, 2009). Di Pietra et al. (2008, p. 43) ask "if the *IFRS for SMEs* is of greatest relevance to developing economies, are these economies' needs and circumstances considered"? Therefore, it is unlikely that the concerns of SMEs in developing countries are adequately addressed. Further, it is claimed the IASB gave less consideration to users' participation in the consultation process during the development of the standard because the major commentators were represented by auditors, accountants and standard setters (Schiebel, 2008). If the *IFRS for SMEs* does not reflect the information needs of SME users, the perceived benefits of financial information for SME users become uncertain.

Additionally, other aspects of the *IFRS for SMEs* are also criticised. For example, the IASB's framework for developing the *IFRS for SMEs*; the need for an international accounting standard for SMEs; the applicability to micro entities; and the cost-benefit considerations, and implementation issues. Analysis of the literature after the issuance of the accounting standard *IFRS for SMEs*, shows that though *IFRS for SMEs* is a simplified version of the full IFRS, the application of the standard seems to be burdensome for SMEs in many jurisdictions. Further, adopting the *IFRS for SMEs* is challenging, with several practical difficulties in implementation. As a result, it can be argued that the *IFRS for SMEs* is not suitable for all entities in the SME spectrum, and the necessity of enforced international reporting standards for smaller entities is debatable. Owing to the lack of empirical research and grounded studies on the *IFRS for SMEs* in developing and Asian countries, further research is needed to examine the effect of its adoption in these countries. The decision by Sri Lanka to adopt the *IFRS for SMEs* without any modification, cannot be said to decide the issue of whether the standard is appropriate to Sri Lankan SMEs. The answer to this question will depend on empirical research, such as this thesis, to contribute to understanding and knowledge within the context of Sri Lanka.

The following chapter outlines the theoretical perspective used to analyse the findings.

CHAPTER FIVE

THEORETICAL FRAMEWORK

5.1 Introduction

This chapter presents the theoretical framework used to guide this thesis and to analyse the findings. A theoretical framework can be defined as a set of interrelated constructs, concepts, definitions, or propositions that present a systematic view of phenomena which could be used to guide a particular research project (Collis & Hussey, 2009; Creswell, 2003; Gaffikin, 2008). In order to generate findings that are of interest to the wider accounting research community, the researcher must be able to make linkages between theory and findings from the field. Prior theories have the potential to provide deeper insights into accounting practices being investigated as well as legitimising the research findings. Llewelyn (2003) claims theorisation is the "value-added" of qualitative academic research and it offers a greater understanding of the empirical issues under discussion. This thesis adopts institutional theory, particularly New Institutional Sociology (NIS), as its theoretical lens.

This chapter is structured as follows: Sections 5.2 outlines and discusses the institutional theory framework and the sub-theories that are used in accounting. Section 5.3 outlines the NIS perspective, examines types of institutional isomorphism. Section 5.4 presents the theoretical framework used in this thesis to examine the adoption of *IFRS for SMEs* in Sri Lanka. Finally, section 5.5 summarises applications of NIS to accounting research. Section 5.6 concludes the chapter.

5.2 Institutional theory

Institutional theory drawn from the social science literature defines institutions as a "way of thought or action of some prevalence and permanence, which is embedded in the habits of a group or the customs of a people" (Hamilton, 1932 p.84, cited in, Burns & Scapens, 2000). Barley and Tolbert (1997, p. 96) adds to the earlier definition by describing institutions as "the shared taken for granted assumptions which identify categories of human actors and their appropriate activities and relationships".

Institutional theory is built in the belief institutional environments are socially constructed (Carruthers, 1995; DiMaggio & Powell, 1983; Meyer & Rowan, 1977). Scott (2001) explains organisations cannot be understood by insulating them from their surrounding social and cultural context. Institutional theory has largely been used to examine the interdependencies between accounting and its social environment (Scapens, 1994; Scapens & Roberts, 1993; Scott, 1995).

This thesis examines the need for internationally comparable accounting information for Sri Lankan SMEs. While developed countries such as Australia and New Zealand have not adopted the *IFRS for SMEs* (Chand et al., 2015), many developing countries such as Sri Lanka have embraced this accounting standard (Bohušová & Blašková, 2012; Quagli & Paoloni, 2012). It was argued that developing countries had to proceed with *IFRS* upon pressures from external forces (Al-Omari, 2010; Irvine, 2008; Mir & Rahaman, 2005). Similarly, Chua and Taylor (2008, p. 463) argue that "diffusion of IFRS is more about political and social dimensions of globalisation than it is about the alleged economic benefits of convergence in international accounting standards". Players in world capital markets such as the World Bank represent a major global institutional force pushing countries to adopt *IFRS* or develop national standards based on *IFRS*, and even in some cases making the adoption of *IFRS* a requirement of their loans (Irvine, 2008; Mir & Rahaman, 2005). It could therefore, be argued that the need for international accounting standards cannot be explored appropriately without an understanding of the institutional forces that provide the context for such a decision.

An institutional approach is valuable in understanding the processes and consequences of change in specific settings, particularly where accounting regulations are developed and applied for the first time (Potter, 2005). As Suddaby, Cooper, and Greenwood (2007) contend, institutional theory offers a valuable theoretical framework for understanding the dynamics of globalization and the process by which dominant templates are adapted to local contexts and diffused globally. An examination of the process of adopting *IFRS for SMEs* through an institutional lens provides an opportunity to enhance the understanding of the role of key institutions such as the World Bank, the IASB and the professional accounting associations in shaping the processes by which accounting changes occur. The literature has identified three branches of institutional theory: Old Institutional Economics; New Institutional Economics; and New Institutional Sociology (NIS) that are particularly relevant to the study of accounting (Burns & Scapens, 2000; Hussain & Hoque, 2002).

Old Institutional Economics is concerned with the institutions that shape the actions and thoughts of individual human agents (Scapens, 2006). It examines why and how particular rules, norms, behaviour or systems exist, change or stabilise over time. It focuses on the role of rules, routines, habits and taken-for-granted ways to explain how things become reutilised and ultimately taken for granted in organisations over time. Furthermore, it emphasises the role of a variety of influences such as power, politics, values and cognition for how systems and organisational practices evolve and are shaped over time (Burns & Scapens, 2000; Scapens, 2006).

By contrast, going beyond an individual perspective, New Institutional Economics uses economic reasoning to explain the diversity in forms of institutional arrangements. However, economic factors are only one part of several interrelated influences (Scapens, 2006). Therefore, this thesis adopts NIS which is a broader multi-dimensional approach for focussing on issues of external and internal organisational contexts (Greenwood & Hinings, 1996). NIS facilitates the understanding of the relationship between organisational structures and the wider social environment in which organisations are situated (Hussain & Hoque, 2002).

NIS theory provides a valuable theoretical framework because of its focus on the social environment as an essential constituent in establishing the social structures of an institution (Heidhues & Patel, 2012). The use of NIS to guide accounting research is well established (Burns & Scapens, 2000; Burns & Vaivio, 2001; Carpenter & Feroz, 2001; De Villiers & Alexander, 2014; De Villiers, Low, & Samkin, 2014; Fogarty & Rogers, 2005; Lawrence, Sharma, & Nandan, 2009; Modell, 2009b; Scapens, 2006; Sharma, Lawrence, & Lowe, 2014). NIS has been used in the accounting literature to identify and explain the sources of isomorphic pressures on the adoption of accounting systems such as *IFRS* (see for example, Al-Omari, 2010; Albu, Albu, Bunea, Calu, & Girbina, 2011; Hassan, Rankin, & Lu, 2014; Hassan, 2008; Heidhues & Patel, 2012; Irvine, 2008; Judge, Li, & Pinsker, 2010; Kholeif, 2010; Mir & Rahaman, 2005; Tan, Chatterjee, Wise, & Hossain, 2016).

5.3 New institutional sociology

Meyer and Rowan (1977) and DiMaggio and Powell (1983) utilise NIS to explain the adoption of new structures and practices by "institutionalised" organisations. By focusing on the environment of the organisations in terms of the influences of external factors on their structures and practices, NIS offers a framework for understanding the socio-economic, political and legal influences on both countries and firms and their strategic responses to those influences (DiMaggio & Powell, 1983; DiMaggio & Powell, 1991; Hussain & Hoque, 2002; Meyer & Rowan, 1977). NIS seeks to explain the similarity among organisations which operate in similar environment, societal sectors or organisational fields (Scapens, 2006). DiMaggio and Powell (1983) point out that institutional pressures could occur from three sources of isomorphism, viz., coercive, mimetic, and normative.

5.3.1 Coercive isomorphism

Coercive isomorphism results from formal and informal pressures exerted on organisations by other organisations they depend on and by cultural expectations in the society within which organisations function (Carruthers, 1995; DiMaggio & Powell, 1983). These pressures are exerted through the need for resources, regulations, executive regulations and laws (Modell, 2009b; Scapens, 2006). Such pressures may be exerted in a diversity of ways through force, persuasion, or invitation to join in collusion. Organisations within any country are influenced by rules and regulations institutionalised and legitimised by the state (Meyer & Rowan, 1977). The state establishes regulations (e.g. Companies Act) and enforces regulations which act as coercive mechanisms (Scott, 2008; Touron, 2005). Chua and Taylor (2008) argue that government or regulators actions have encouraged widespread diffusion of *IFRS* regardless of economic rationale. Further, Brown and

Tarca (2005) acknowledge that the successful adoption of the *IFRS* is less likely to be achieved without regulatory oversight that promotes rigorous and consistent use of *IFRS* – some coercion is needed. Similarly, Jermakowicz and Gornik-Tomaszewski (2006) show the majority of EU-listed companies would not adopt *IFRS* unless they were required to do so by EU regulations. Organisations can be required to commit to different levels of harmonisation due to rules and regulations set up by the stock market regulators, and other regulatory agencies, such as accounting and audit standard-setting institutions (Boolaky & Soobaroyen, 2017).

Institutions such as the World Bank and the IMF can pressure a country or an organisation to conform to international standards (Boolaky & Soobaroyen, 2017). The rationale underlying this institutional coercion is primarily financial dependence of the influenced organisation (Lawrence et al., 2009; Mir & Rahaman, 2005; Sharma, Lawrence, & Lowe, 2010; Sharma et al., 2014; Tsamenyi, Cullen, & González, 2006). DiMaggio and Powell (1983) note that in cases where alternative suppliers are either not readily available or require effort to locate, the stronger party to the transaction can coerce the weaker party to adopt its practices in order to accommodate the stronger party's needs. In other words, resource providing or controlling organisations are able to influence by coercion resource-dependent organisations (Oliver, 1991).

5.3.2 Mimetic isomorphism

DiMaggio and Powell (1983) argue that organisations tend to model themselves on industry leaders that they perceive to be most successful. In this respect, large multinational companies benchmark against their peers and smaller companies benchmark against industry leaders (De Villiers & Alexander, 2014). A country's commitment to adopt certain practices could also be influenced by the presence of foreign commercial partners (Boolaky & Soobaroyen, 2017). In explicating mimetic institutional isomorphism, DiMaggio and Powell (1983, p. 155) propose that organisations that are struggling to establish clear and well-defined technologies will most likely import institutionalised rules, processes and practices. Mimetic isomorphism may take place: when organisational technologies are poorly understood; when goals are ambiguous; or when the environment generates symbolic uncertainty (DiMaggio & Powell, 1983). If an organisation or country does not have standards to follow they are likely to mimic standards (e.g. the *IFRS*) that are seen to be legitimatised or accepted by 'leaders" such as the IASB.

5.3.3 Normative isomorphism

Normative isomorphism arises from group norms to adopt particular institutional practices (DiMaggio & Powell, 1983). These often form part of an educational or professional training process and are taught and reinforced by universities and professional associations (Abernethy & Chua, 1996; DiMaggio & Powell, 1983). Members of professional bodies are motivated to fulfil their obligation in order to maintain their professional status conferred through professional membership (Barbu & Baker, 2010; Carpenter & Feroz, 2001; Mezias & Scarselletta, 1994; Touron, 2005). For example, Sharma et al. (2014) find the introduction of accounting routines, language and practices in a privatised public sector organisation were driven by the efforts of accountants, who were recruited specifically to champion these new institutional norms. The degree of professionalisation in accounting practices is also influenced by audit firms. Jones and Higgins (2006) indicate that the external auditor is the most dominant party involved in the *IFRS* implementation process in Australia, either as independent consultants assisting in the *IFRS* adoption process or as the organisation's auditor required to provide audit opinion on the financial statements. Professional accountants and auditors possess the power to influence and shape the institutional environment within organisations (Chua & Taylor, 2008).

NIS theory places emphasis on the organisational field to the exclusion of other dimensions (Scott, 1991; Scott & Meyer, 1991). DiMaggio and Powell (1983, p. 148) define the organisational field as "those organisations which, in the aggregate, constitute a recognized area of institutional life: key suppliers, resources and product consumers, regulatory agencies, and other organisations that produce similar services or products". Thus, NIS theory neglects institutional dynamics across different levels of analysis over time (Dillard, Rigsby, & Goodman, 2004; Greenwood & Suddaby, 2006; Hopper & Major, 2007; Modell, 2009b). To date, research has restricted the application of NIS largely to factors at the organisational field level (Ezzamel, Robson, Stapleton, & McLean, 2007; Greenwood, Hinings, & Suddaby, 2002; Greenwood & Suddaby, 2006; Suddaby et al., 2007). Using a hierarchy of institutional influences, Scott (2001) distinguishes three levels of institutional pressures. He argues that higher level institutions (e.g. societal and global) formally propose models and standards which form and restrain actions at lower levels. At the second level there are the organisational governance structures which comprise the organisational field and at the third level organisations themselves. The highest level institutions affect the lower level institutions (Boolaky & Soobaroyen, 2017; Scott, 2001).

Dillard et al. (2004) suggest individual organisations and organisational fields exist in an economic and political context, and that this context provides the foundation for institutional practice (Dillard et al., 2004). According to this view, actors in the institutionalisation process exercise influence at different levels, with "governmental officials, regulators and legislators" as the "primary agents at the economic and political level", industry leaders, unions and consultants exercising influence at the organisational field level, and workers and managers exercising influence at the organisational level (Dillard et al., 2004, p. 513). The result is "continual dynamic change" through multiple levels, from political and economic settings, through organisational fields to individual organisations (Dillard et al., 2004, p. 512). In the same vein, Irvine (2008) suggests that in an increasingly globalised world, powerful institutional forces operate at an international level on individual national states, which then become a field for the transmission and adoption of acceptable institutional practices.

NIS theory has been criticised because it appears to ignore human agents and their interests (DiMaggio & Powell, 1983; DiMaggio & Powell, 1991; Tolbert & Zucker, 1983). As Dillard et al. (2004), Dambrin, Lambert, and Sponem (2007), and Lounsbury (2008) submit, a major criticism of NIS is its inattention to the role of proactive actors in constructing institutions. However, recent institutional studies have begun to consider aspects of institutional change by highlighting the role that individuals play in change processes (Burns & Scapens, 2000; Dillard et al., 2004; Sharma & Lawrence, 2008; Sharma et al., 2010, 2014).

In this context, the Institutional entrepreneur has been a major step by introducing individuals as agents into institutional theory (Dorado, 2005; Lounsbury, 2008; Scapens, 2006; Sharma et al., 2010). Institutional entrepreneurs have been defined as organised actors who have interests in particular institutional arrangements and who leverage resources to create new institutions or transform existing ones (DiMaggio, 1988; Maguire, Hardy, & Lawrence, 2004). This concept assumes that individuals act in self-interest to transform their institutional environment by aligning it with their particular goals. It introduces the concept of the institutional entrepreneur as an agent who commands and mobilizes resources to alter or create institutional structures (DiMaggio, 1988).

Battilana, Leca, and Boxenbaum (2009) specify two conditions that actors must fulfil to be regarded as institutional entrepreneurs: first, they must initiate changes that break with institutionalised templates and institutional logics within a given context, and second, they must mobilise resources to implement these changes, thereby contributing to the institutionalisation of alternative practices. According to Battilana et al. (2009), social position can enable institutional entrepreneurs to mobilise allies to support the implementation of divergent changes. When institutional entrepreneurs' social positions do not enable them to mobilise others easily, they might try to convince actors who occupy higher status social positions to endorse their projects (Battilana et al., 2009). This thesis uses the framework provided by NIS, and in particular, institutional isomorphism in examining the adoption of the *IFRS for SMEs* in Sri Lanka.

5.4 Theoretical framework for adoption of *IFRS for SMEs* in Sri Lanka

Consistent with Dillard et al. (2004) and Irvine (2008), this thesis explores institutional pressures on the decision to adopt *IFRS for SMEs* both at country (Sri Lanka) and firm (SMEs) levels. Sri Lanka is a developing country and its national institutional orientation is different from those of developed countries where international financial reporting standards originated. Sri Lanka was a British colony and the prevailing legal and accounting systems were largely influenced by the British systems (De Zoysa & Rudkin, 2010). Sri Lanka became a free market economy in 1977 and became attractive to both Western donors and large multinational companies. The civil war that plunged the country into twenty five years of violence and destructive conflict had also impacted on political, social and economic environment in Sri Lanka (Athukorala & Jayasuriya, 2013). As a result, post-war Sri Lanka depended largely on foreign aid to rebuild its economy. Sri Lanka, in per capita terms, became the world's leading aid recipient (Arunatilake, Jayasuriya, & Kelegama, 2001). For these reasons, donor institutions such as the World Bank and the IMF are able to influence the Sri Lankan financial accounting and reporting systems. The Sri Lankan setting therefore provides an interesting and novel context to study the institutionalisation of *IFRS for SMEs*. Figure 1 depicts the theoretical model adapted for the thesis to explore the decision to adopt the *IFRS for SMEs* in Sri Lanka.

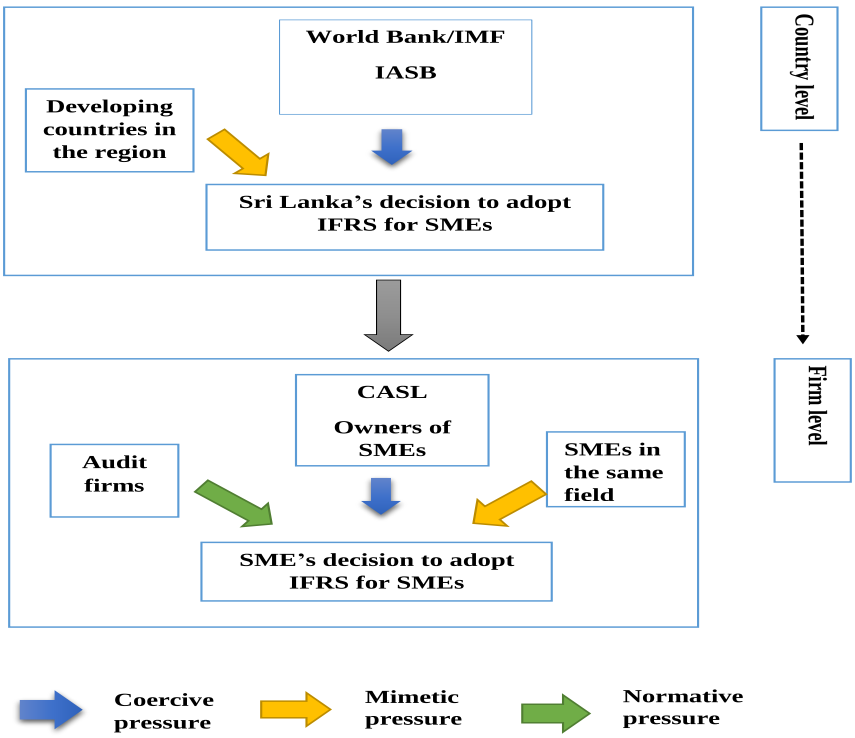

Figure 1: Theoretical framework for adoption of the accounting standard *IFRS* for SMEs in Sri Lanka

Source: Author

Coercive pressures comprise of formal and informal pressures from other organisations upon which an organisation is dependent and the expectations of the society in which the organisation operates (DiMaggio & Powell, 1983). Resource dominant actors such as the World Bank, the Asian Development Bank and the IMF coerce recipients of their finance to adopt the *IFRS*. DiMaggio and Powell (1991) note that in cases where alternative sources are either not readily available or require effort to locate, the stronger party to the transaction can coerce the weaker party to adopt its practices in order to accommodate the stronger party's needs. In other words, resource providing or controlling organisations are able to influence resource-dependent organisations. In developing countries, the two primary organisations that use coercive institutional forces are the World Bank and the IMF.

Sri Lanka is a large recipient of foreign aid from the World Bank and the IMF. Consequently, these international organisations exert pressures on Sri Lanka to adopt certain practices. For example, as part of its recommendations for improving accounting and auditing frameworks in Sri Lanka, the World Bank recommended that CASL adopt *IFRS* as promulgated by the IASB without modification (World Bank, 2004). The IASB also exerts coercive pressures by encouraging countries around the world to adopt the *IFRS* (Barbu & Baker, 2010; Irvine, 2008).

Institutional pressures determined at the country level were transmitted to the organisational level when the CASL achieved its *IFRS* convergence target on 1 January 2012. Since CASL formulates all the accounting regulations and also controls the accounting profession in Sri Lanka, CASL is able to exert coercive pressure on Sri Lankan SMEs to adopt the *IFRS for SMEs*. Coercive isomorphism also arises when organisations change their institutional practices in response to pressure from stakeholders upon whom the organisation is dependent (Deegan & Samkin, 2013).

Developing countries are more likely to mimic their trade partners or countries within their geographical region that are *IFRS* adopters (Al-Omari, 2010; Irvine, 2008). Therefore, it could be argued that Sri Lanka's decision to adopt *IFRS for SMEs* is influenced by *IFRS* adoption decisions of other developing countries in the

Asian region. Further, it is reasonable to believe that SMEs tend to copy, or mimic, the accounting practices of other successful organisations in the same industry.

Normative isomorphism is the process by which organisations adopt the structures and procedures advanced by particular dominant professions, professional bodies and/or consultants (DiMaggio & Powell, 1983). The degree of professionalisation in the accounting practices is influenced by the audit firms. The Big Four accounting firms play an important role in the globalization of accounting and represent the normative pressure that affect the decision to implement *IFRS* (Albu et al., 2011). Audit firms that provide accounting and auditing services exert normative pressures on their SME clients to adopt *IFRS for SMEs* through opinions or suggestions on financial reporting practices. The CASL, also actively promotes the adoption of the *IFRS for SMEs* in Sri Lanka. They conduct training courses and seminars to professional members including small and mid-tier audit firms in Sri Lanka. In addition, the CASL educates its members by providing interpretations and guidance on the standards issued by the IASB. These propositions will be examined in the perceptions provided by the survey respondents of this thesis. NIS theory, therefore provides a strong framework by which to examine and to explain the *IFRS* adoption process in Sri Lanka.

5.5 Prior research on NIS theory for adoption of *IFRS*

The NIS theory has been used in prior research to understand how a specific accounting system is introduced, adopted, and used in an organisational setting. For instance, Hussain and Hoque (2002) use NIS theory to report the performance measurement practices of four Japanese banks. Their results indicate that several institutional forces influenced the banks to implement a particular measurement system. Of these, economic constraints appear to be the most forceful factor, followed by the central bank’s regulatory control, accounting standards/financial legislation, management’s strategic focus, bank size, competition, and an organisational tendency to copy best practices from others (Hussain & Hoque, 2002). Scholars have supported the use of NIS theory in particular institutional isomorphism, in explaining the *IFRS* adoption. Table 11 illustrates studies that use

NIS theory to explain *IFRS* adoption. These studies give an indication of sources of isomorphism for adoption of *IFRS*.

Table 11: Prior research on IFRS using NIS theory

Author	**Country**	**Level of analysis**	**Method**
Mir and Rahaman (2005)	Bangladesh	Country	Archival data and 27 interviews
Irvine (2008)	United Arab Emirates	Country	Publicly available data about UAE
Hassan (2008)	Egypt	Country	12 interviews and document analysis
Kholeif (2010)	Egypt	Company	Case study of a state-owned Egyptian company
Al-Omari (2010)	Jordan	Country	Conceptual paper
Judge et al. (2010)	132 countries	Cross-countries	Archival data-developing and developed countries
Lasmin (2011)	161 countries	Cross-countries	Archival data
Albu et al. (2011)	Romania	Country	Both primary (11 semi-structured interviews) and secondary data
Heidhues and Patel (2012)	Germany	Country	Review of history
Hassan et al. (2014)	Iraq	Country	Review history
Alver, Alver, and Talpas (2014)	Estonia	Country	Literature review and document analysis
Tan et al. (2016)	USA	Country	Conceptual paper
Al-Htaybat (2017)	Jordan	Country	11 interviews
Mantzari, Sigalas, and Hines (2017)	Greece	Non-listed companies	Survey with 80 non-listed companies and 9 semi-structured interviews

Source: Author

In investigating the *IFRS* adoption in Bangladesh using institutional isomorphism as a theoretical lens, Mir and Rahaman (2005) find that the institutional actors involved in the adoption of the *IFRS* in Bangladesh are the Government of Bangladesh, the World Bank, Asian Development Bank and the Institute of Chartered Accountants of Bangladesh. The IAS adoption process was initiated following a World Bank grant to the Bangladeshi Government for the development of Accounting and Auditing Standards in Bangladesh. The Government delegated the process to the Securities and Exchange Commission of Bangladesh as the main institution responsible for overseeing the process. The Securities and Exchange Commission of Bangladesh then empowered the Institute of Chartered Accountants of Bangladesh, which is recognised as the sole authority in Bangladesh for adoption of *IFRS* and International Standards on Auditing (Mir & Rahaman, 2005).

Irvine (2008) focuses on institutional pressures of the global and societal context to analyse the option taken by the United Arab Emirates (UAE) to adopt *IFRS*. The study reveals this was a response to coercive, normative, and mimetic forces emanating from regulatory regimes of the World Bank, relationships with multinational corporations, the Big Four accounting firms and the UAE's trading partners. Foreign aid was used by international donor agencies as a mechanism to coerce developing countries to adopt the *IFRS* (Irvine, 2008). Within the UAE, all the Big Four accounting firms have a presence and require clients to present their financial statements under *IFRS* (Irvine, 2008). Thus the Big Four accounting firms have driven the adoption of *IFRS*, and benefited financially from the adoption (Irvine, 2008).

Hassan (2008) shows that external coercive pressures from foreign aid provided by the IMF are influential in Egypt's moving towards the adoption of the *IFRS*. In another study conducted in an Egyptian state-owned enterprise, Kholeif (2010) reveals the company faced conflicting institutional demands from outside to adopt *IFRS*. The Central Agency for Accountability required the company to use the Uniform Accounting System (as a state-owned enterprise) and the Egyptian Capital Market Authority required the partially private sector company registered in the stock exchange to use the *IFRS*.

Al-Omari (2010) identifies the World Bank and the capital markets exerting coercive pressures, the Big Four accounting firms supplying normative pressures, and trade partners and multinational corporations exerting mimetic pressures that led to the *IFRS* adoption in Jordan. Similarly, Al-Htaybat (2017) identifies coercive pressures as the main reason for *IFRS* adoption in Jordan. Foreign governments, the capital market, foreign investors and aid agencies are the most prominent external coercive pressures demanding Jordan to adhere to the *IFRS*.

Judge et al. (2010) sought to understand why some economies have quickly embraced the *IFRS* while others partially adopt *IFRS* and still others continue to resist. They find all three forms of isomorphic pressures (i.e., coercive, mimetic, and normative) are predictive of *IFRS* adoption. Consequently, institutional theory with its emphasis on legitimacy-seeking by social actors is supported by their data. This suggests that the *IFRS* adoption process and decision are driven more by institutional pressures, than by economic logic (Judge et al., 2010, p. 161). Similarly, Lasmin (2011) after examining the decision of countries to adopt or not to adopt the *IFRS*, identifies social pressures of isomorphic change are better predictive factors than economic pressures. He claims that countries decide to adopt the *IFRS* because they are forced by international organisations to comply with the *IFRS*; they mimic other organisations and countries that are perceived as more successful and legitimate.

Albu et al. (2011) use NIS theory to discuss two stages of *IFRS* implementation in Romania. The first step was a result of coercive external forces, that is, the influence of the World Bank. Given the lack of other factors to favour the change process, it is argued that the actual implementation of *IFRS* in that period was very limited. The second step of *IFRS* implementation concerned only listed and financial institutions. They posit that this reduction in scope was accompanied by a change process more significant than in the previous period. Findings show the two stages of *IFRS* implementation had different outcomes, with a more profound and qualitative impact of the second phase. They argue that effective *IFRS* implementation happens when users begin to demand better accounting information, auditors require higher reporting standards, and preparers become better qualified.

Heidhues and Patel (2012) examine the development of German accounting and the adoption of *IFRS* using NIS theory. Based on a historical examination of accounting development in Germany, they conclude *IFRS* adoption is largely the result of economic and political power and pressures in the international economy rather than normative alignment with German traditional values and expectations. The move in favour of *IFRS* in Germany was largely influenced by the coercive authority of the United States, which is regarded as a dominating power in the global financial market. Additionally, they identify mimetic pressures that contribute to *IFRS* adoption in Germany. Specifically, uncertainty with regard to appropriate standards for capital markets, increasing industry pressure, and the acceptance of statements prepared in accordance with *IFRS* fostered the adoption of *IFRS* in Germany.

Hassan et al. (2014) find that all three forms of institutional isomorphism explain the initial decision to adopt *IFRS* in Iraq. The most significant force in the decision to adopt *IFRS* was coercive pressures from the international institutions, such as the World Bank and the IMF, from which the government has obtained funds and advice to assist in economic development. The accounting system in Iraq is likely to be advanced due to mimetic and normative pressures from Iraq's trade partners, multinational corporations, and the accounting profession (Hassan et al. (2014).

Alver et al. (2014) investigate how globalisation and the *IFRS* have affected the development of financial accounting and reporting in Estonia. The EU has provided coercive institutional pressure for the development of accounting legislation in Estonia to support adoption of the *IFRS*. They find the IASB exerting mimetic, and the Big Four exerting normative institutional pressures on the decision to adopt *IFRS*. In Estonia, the impact of Big Four audit firms on financial statements presentation is seen to be significant, as they audit the most of Estonian public interest entities and therefore, directly influence the preparation and presentation of the financial statements (Alver et al., 2014).

Tan et al. (2016) utilise institutional isomorphism to study the potential adoption of *IFRS* in the United States, at the country level. They believe that such change would be influenced by isomorphic pressures. The coercive pressures include adoption by other major economies externally, the accounting profession, and large firms internally (Tan et al., 2016). Normative isomorphism is reflected in the recommendations of the accounting professional bodies, large accounting firms, and the experience of other adopters. Mimetic isomorphism takes place as a result of United States accounting failures. Thus legitimacy is achieved through copying another established system (Tan et al., 2016).

A recent study conducted in Greece by Mantzari et al. (2017) indicates that the motivations to adopt the *IFRS* by Greek non-listed companies are not primarily related to the technical competence of the standards. The adoption of *IFRS* is driven predominantly by the pressures exerted by parent companies on their subsidiaries, by the legal requirements of the state and through borrowing and debt-contracting requirements enforced by financial institutions (Mantzari et al., 2017).

While prior studies have discussed *IFRS* adoption using institutional theory at country and firm level; no study uses both country and firm level data. The adoption decision taken at the country level does not necessarily transmit to the firm level (Aboagye-Otchere & Agbeibor, 2012). The adoption and implementation of international accounting standards such as the *IFRS for SMEs* depends to some extent on individual firms and their institutional environment (Aboagye-Otchere & Agbeibor, 2012). Samaha and Khlif (2016) identify a gap in empirical research regarding *IFRS* adoption decision making at both country and firm level in developing countries. Therefore, in order to acquire a holistic understanding of the *IFRS* adoption, both country and firm level decision making should be analysed. This thesis, based in Sri Lanka, analyses the adoption of the *IFRS for SMEs* at both country and firm level.

All research using NIS theory (as shown in Table 11) is focused on the full *IFRS* adoption by large and/or listed companies. SMEs' decision to adopt the accounting standard *IFRS for SMEs* has not been explored using NIS theory. Unlike large/listed companies, the SME cluster is a broad category including companies of different sizes. The major source of funds for SMEs is usually debt capital provided by banks, which have access to organisational information and require more information than the public stakeholders (Mantzari et al., 2017). Another key difference between listed companies and SMEs is that the primary users of SME financial information are the owner-managers, tax authorities, and banks (Collis & Jarvis, 2000). Consequently, the type of the accounting standards used to prepare financial statements may be of less importance to SMEs that often use private communication routes to respond to the information needs of key users, such as banks (Chen, Hope, Li, & Wang, 2011). The institutional environment within which SME financial reporting operates could be different from large/listed companies. Therefore, the findings from research using large companies may not be applicable to SMEs.

Further, there are few studies based in developing countries, particularly from South Asian. Most of the research is conceptual and only five empirical studies are available. This thesis therefore, extends the existing knowledge and contributes to the international accounting literature by focusing upon how institutional pressures drive the decision to adopt *IFRS for SMEs* in Sri Lanka both at country and SME firm level.

5.6 Summary

This chapter provided an overview of institutional theory and its sub-theories. The NIS framework of institutional theory, including institutional pressures was presented. Institutional theory is concerned with generally accepted social norms and /or institutional practices which are imposed on the organisations. In addition, the chapter has also examined research that utilises NIS as the theoretical lens to study *IFRS* adoption. Organisations correspond to institutionalised structural forms and/or practice through the processes of isomorphism.

There are three forms of institutional isomorphism in which change can occur. External institutional pressures include coercive, normative, and mimetic pressures can shape structures and practices of organisations. Since accounting information must be viewed as legitimate to be trusted by its stakeholders, institutional theory is a useful theoretical lens for investigating the adoption of new accounting standards by SMEs. The extent to which NIS explains adoption of the *IFRS for SMEs* both at country (Sri Lanka) and firm level (SMEs) will be examined with the empirical evidences.

CHAPTER SIX

RESEARCH METHODOLOGY

6.1 Introduction

This chapter describes and justifies the methodology adopted to answer the research questions:

- How do Sri Lankan users and their financial information needs differ with regard to size of SMEs? and
- Do Sri Lankan SMEs need internationally comparable financial information?

A research methodology is an important and essential element of the research process, as it describes the core assumptions regarding the nature of knowledge and the methods through which that knowledge can be obtained, as well as about the nature of the phenomenon to be investigated (Llewellyn, 1993; Morgan & Smircich, 1980). Research in accounting is greatly influenced by the theoretical perspectives advanced by social science (Humphrey & Scapens, 1996; Laughlin, 1995). The social science literature provides a variety of philosophical lenses for studying accounting phenomenon ranging from an objectified view of accounting to a view where accounting is seen to be socially constructed (Baxter & Chua, 2003; Broadbent & Laughlin, 1997; Chua, 1986a; Hines, 1989; Morgan & Willmott, 1993).

Once researchers decide their position on how to seek knowledge and explain the existence of some form of truth and reality, they are in a better position to explore the possible techniques of data collection (Chua, 1986b; Llewellyn, 1993; Tomkins & Groves, 1983). Chua (1986a, p. 604) states "methodological assumptions indicate the research methods deemed appropriate for the gathering of research data". Llewellyn (1993, p. 232) suggests that the "methodology adopted will shape the research process and the research findings to a far greater extent than will the research method". Therefore, once a methodology is decided upon, the researchers can then proceed to identify methods by which data will be collected.

Section 6.2 provides a general explanation of methodology, followed by an analysis of the positivist, the interpretative and the pragmatic approaches in accounting research. In section 6.3, a discussion of the mixed methods approach is provided. Section 6.4 explains the mixed methods research design adopted for this thesis. Section 6.5 concludes the chapter.

6.2 Towards a choice of methodological perspective

According to Llewellyn (1993, p. 232) in the social sciences, "methodology reflects the ontological and epistemological assumptions of the researcher (particularly those concerning the relationship between the subject and the object)". An appropriate research methodology cannot be selected without concern for the philosophical assumptions (ontological and epistemological) about the world. These paradigms or worldviews determine the conduct and outcomes of research. Ontology concerns the nature of reality (Hopper & Powell, 1985). Ontological assumptions form two extreme parts of a continuum:

> … on one extreme the social world and its structures can be regarded as having an empirical, concrete existence external to and independent of and prior to the cognition of any individual, on the other extreme reality is depicted as existing only as a product of individual consciousness-the external world consists simply of concepts and labels created by people to help them understand reality and negotiate a shared conception of its nature with other (Hopper & Powell, 1985, p. 431).

Accounting researchers may adopt a view that reality exists independent of the researcher and is something "out there" (Chua, 1986b, p. 606) which can be discovered. This view of reality encourages the researcher to undertake research where the phenomenon under study 'comes into being' by using scientific methods (Chua, 1986b; Willmott, 1983). These methods include, hypothesis testing using a structured set of predetermined variables, and experiments in a controlled environment where the researcher is a passive participant and follows a predetermined structured set of rules (Hopper & Powell, 1985; Willmott, 1983). According to Willmott (1983), an objective view of reality can be used in accounting research only if the variables of a phenomenon being studied are stable. Adopting the view that reality is socially constructed implies that reality is multifaceted because it is shaped by both human and non-human interactions (Hines, 1989). This view of reality encourages the researcher to seek to capture and reflect on the distinctive form and process of the research setting (Willmott, 1983). According to Chua (1986a, p. 615), "social reality is emergent, subjectively created, and objectified through human interaction. All actions have meaning and intention that are retrospectively endowed and that are grounded in social and historical practices".

Epistemological considerations address the question of how we know a phenomenon and how we verify what we know as truth, also known as 'theory of knowledge' (Carter & Little, 2007). According to Chua (1986a, p. 604), "epistemological assumptions decide what is to count as acceptable truth by specifying the criteria and the process of assessing truth claims". The epistemological belief of a researcher will be contingent upon the researcher's ontological beliefs (Chua, 1986a). If the researcher views reality as an object, then the researcher will use scientific methods to prove or falsify the phenomenon under study. Alternatively, if the researcher views reality as a social construct then the researcher will engage in using subjective and interpretative methods to investigate the phenomenon under study.

Various classifications of methodological orientation exist in the accounting, sociology, and organisation studies literature (see Burrell & Morgan, 1979; Chua, 1986a; Hopper & Powell, 1985; Morgan & Smircich, 1980). However, the classificatory scheme which provides a starting point for the discussion in this section is Burrell and Morgan (1979) framework.[29] The Burrell and Morgan framework provides a two-by two matrix based on two bipolar continuums (Laughlin, 1995). The first continuum dichotomises between "objectivist" and "subjectivist" as alternative approaches to understanding empirical research while the second provides assumptions with respect to the nature of society (i.e. 'sociology of regulation' versus 'sociology of radical change') (Burrell & Morgan,

[29] Most of the other classificatory schemes are either critiques or expansions of Burrell and Morgan's work.

1979). Combining these dichotomies with assumptions about ontology, epistemology, human nature, and methodology, Burrell and Morgan (1979) distinguish between four paradigms namely; functionalism, interpretivism, radical structuralism, and radical humanism as illustrated in Figure 2.

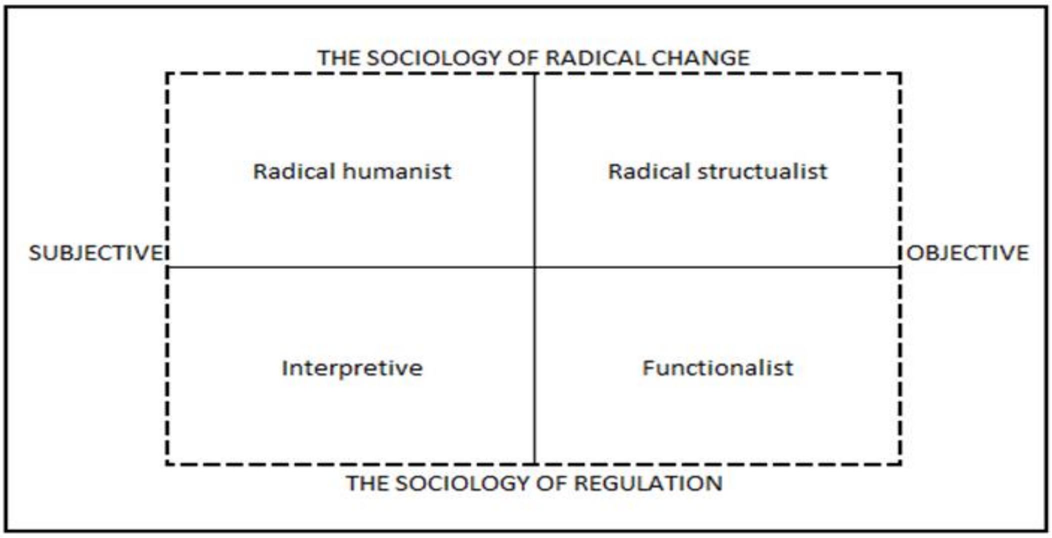

Figure 2: Burrell and Morgan's four paradigms for the analysis of social theory

Source: Burrell and Morgan (1979), p. 22

According to Burrell and Morgan (1979, p. 25) the functionalist paradigm "represents a perspective which is firmly rooted in the sociology of regulation and approaches its subject matter from an objectivist point of view". Burrell and Morgan (1979) argue that, by contrast, the interpretive paradigm is:

> … informed by a concern to understand the world as it is, to understand the fundamental nature of the social world at the level of subjective experience; it seeks explanation within the realm of individual consciousness and subjectivity, within the frame of reference of the participant as opposed to the observer of action.

Burrell and Morgan (1979) contend the researcher who adopts either a functionalist or interpretive agrees with the principle of regulation and stability. However, those in interpretive paradigm adopt the subjectivist approach, which employs nomialistic ontology, an anti-positive epistemology, and an ideographic methodology. Those who adopt the functionalist paradigm take an objective approach to reality and utilise a realistic ontology, a positive epistemology, and a nomothetic methodology (Burrell & Morgan, 1979).

In contrast to the sociology of regulations, the sociology of radical change includes the radical humanist and radical structuralist paradigms. These seek to understand social structures in a holistic way by adopting a Marxist ideology which assumes that society's members have different interests' and wealth (Burrell & Morgan, 1979). The radical humanist paradigm observes society through a subjective lens and seeks to change social structures by eliminating constraints on human potential (Burrell & Morgan, 1979). It views the world as it is rather than how it might be. Researchers who employ the radical humanist paradigm aim to understand the relationship between individual consciousness and the external world. As with the interpretive paradigm, it adopts a nomialistic, anti-positivist, and ideographic point of view (Burrell & Morgan, 1979). The radical structuralist paradigm views the social world from an objective stand point and concentrates on changing its structure. As with the functionalist paradigm, it focuses on the real, positivist, and nomothetic methodology (Burrell & Morgan, 1979). From the Burrell and Morgan (1979) paradigmatic model, two paradigms have emerged which have been generally used to classify all social enquiries (Guba & Lincoln, 1998). These are the functionalism (also known as positivism/quantitative paradigm) and interpretivism (also known as qualitative paradigm).

6.2.1 Positivism

Accounting research based within the functionalist paradigm is labelled as positivist (Chua, 1986a). Positivists are of the view that social phenomena can be measured, and thus they can be interpreted using quantitative methods of analysis (Bryman, 2012; Saunders, Lewis, & Thornhill, 2007). Walliman (2005) indicates that positivism generates knowledge that is based on scientific logic and mathematical proof. Accounting research has been, and continues to be, dominated by positivism (Bisman, 2010; Fraser, 2014). Positivist research literature presupposes that the scientific approach is appropriate to the discovery, explanation and prediction of accounting phenomena (Bisman, 2010). The positivist accounting research is perceived as providing a worldview, which claims the existence of a world with an objective reality, a determinable nature that is knowable and exists independent of human beings (Chua, 1986a). The positivist accounting research views accounting as an object and distinct from the contextual environment in which accounting is practised. It expects the research design to be structured in such a way that the impact of all extraneous factors that might bias and thus invalidate the results are minimised (Willmott, 1983).

Accounting researchers using the positivist approach have been criticised for isolating the practice of accounting from its contextual environment (Baxter & Chua, 2003; Hines, 1989; Hopper & Powell, 1985; Humphrey & Scapens, 1996). The common argument is that accounting as a practice does not exist independently of the accounting practitioner, the purpose of the practice and the users of the accounting information. Critics of the positivist approach hold the view that knowledge constructed using the assumptions of this approach does not provide a 'holistic' meaning of the accounting phenomenon studied. This is because the effects of the interactions amongst the accounting practitioners, the users of accounting information and the environment on the accounting phenomenon studied do not form a part of the research process and their influences are not considered in the construction of knowledge (Baker & Bettner, 1997; Hopper & Powell, 1985). Hopper and Powell (1985, p. 450) advocate that accounting should no longer be studied in a mode which is divorced from its social context and which ignores the influence of "wider social and political collectives".

Baker and Bettner (1997, p. 293) claim that "the type of research prevalent in the mainstream accounting journals, which is characterised by a positivist methodological perspective and an emphasis on quantitative methods, is incapable of addressing accounting's complex social ramifications". They explain that while quantitative methods enable researchers to detect variations between the elements under investigation, it does not allow for an analysis of why such differences and gaps emerge (Baker & Bettner, 1997).

6.2.2 Interpretivism

The interpretive, radical humanist, and radical structuralist paradigms are alternatives to positivist accounting research (Chua, 1986a). The shift from positivist to subjective thinking in accounting research (Laughlin, 1995), including from quantitative to qualitative research (Parker, 2012), became apparent in 1970s. Humphrey and Scapens (1996) claim that the interpretive methodology allows the researcher to study accounting within its social context and incorporate the wider social and political influences in explaining the construction of knowledge. The aim of interpretive research is to capture the lived experience of actors being studied (Chua, 1986a, 1988; Parker, 2008). Further, Chua (1986a, p. 603) states:

> All human knowledge is a social artifact - it is a product of the constituting labour of people as they seek to produce and reproduce their existence and welfare (quoted from Habermas, 1978). Knowledge is produced by people and is about people and their social and physical environment. Accounting is no different.

Baxter and Chua (2003, p. 98) expand: “accounting is a discipline of the social and it seemed important to us to understand it in the context of a broader set of disclosures from the social science”. According to Hopper and Powell (1985, p. 431), “the external social world consists simply of concepts and labels created by the people to help them understand reality and negotiate a shared conception of its nature with others”. While positivists focus on measuring social phenomena, interpetivism advocates exploring the complexity of social phenomena to develop an understanding (Bryman, 2012). Creswell and Clark (2011) point out that the interpretivism paradigm tends to explore, explain and develop an understanding in order to clarify or illustrate the meaning of terms.

Burrell and Morgan (1979) explain that each of the four paradigms can be seen as separate and mutually exclusive. They contend that a social science researcher has to adopt only one of these paradigms when conducting their work. However, this contention has been criticised by a number of authors (for example: Chua, 1986a; Clair, 1999; Deetz, 1996). The researcher can even be in the middle and hence adopt a perspective which spans two paradigms (Chua, 1986a). Indeed, Chua (1986a) criticised Burrell and Morgan’s framework for ignoring the possibility that individuals are influenced by their social environment. Lukka (2010, p. 112) tends to support these criticisms, for “while accounting can by no means be labelled as a single-paradigm discipline, either in principle or in practice, it is strongly dominated by one paradigm”.

Some scholars argue that lack of alignment across paradigms in relation to ontological and epistemological assumptions is a philosophical barrier to mix positivism and interpretivism research (Hoque, Covaleski, & Gooneratne, 2013; Modell, 2009a; Smith, 1983; Smith & Heshusius, 1986). This incompatibility has created the so called ‘paradigm wars’ or ‘paradigm debate‘ in which proponents of the positivistic paradigm reject the interpretivist paradigm, and vice versa (Migiro & Magangi, 2011). While advocates of positivism and advocates of interpretivism have been engaged in this paradigm war, there is a growing number of researchers who are questioning the value of strict adherence to a purist view of either paradigm (Johnson & Onwuegbuzie, 2004; Kakkuri-Knuuttila, Lukka, & Kuorikoski, 2008). Their main contention is that the overemphasis on the epistemological origins of a particular approach may hamper communication between researchers working in different approaches (Kakkuri-Knuuttila et al., 2008) and could undermine ability of researchers to choose and implement the most appropriate research design for answering the research questions raised (Ritchie & Lewis, 2003). Some scholars say this paradigm debate hinders the opportunity to converge the two paradigms (Bryman, 2012; Migiro & Magangi, 2011). The pragmatic worldview has emerged as a convincing response to these kinds of arguments, that enable investigators the opportunity to “put together insights and procedures from both approaches to produce a superior product” (Johnson & Onwuegbuzie, 2004, p. 17).

6.2.3 The pragmatic worldview

The pragmatist point of view rejects the forced choice between positivism and interpretivism with regard to methods, logic and epistemology (Tashakkori & Teddlie, 1998). Pragmatists maintain that scientific inquiry is not formalistic and the researcher may be both objective and subjective in epistemological orientation over the course of studying a research question (Tashakkori & Teddlie, 1998). Pragmatic researchers place at the heart of their endeavours their research questions (Johnson & Onwuegbuzie, 2004), rather than pre-occupied with ontological and epistemological debates about truth and reality (Cherryholmes, 1992). Tashakkori and Teddlie (2003, p. 713) define methodological pragmatism as:

> … a deconstructive paradigm that debunks concepts such as “truth” and “reality” and focuses instead on “what works” as the truth regarding the research questions under investigation. Pragmatism rejects the either/or choices associated with the

> paradigm wars, advocates for the use of mixed methods in research, and acknowledges that the values of the researcher play a large role in interpretation of results.

Morgan (2007) advocates the “pragmatic approach” as a new guiding paradigm in social science research, as a basis for supporting work that combined qualitative and quantitative methods. Table 12 summarises the framework proposed by Morgan (2007) where he contrasts qualitative and quantitative research approaches in the social sciences with the pragmatic approach.

Table 12 : Alternative to the key issues in Social Science Research Methodology

	Qualitative approach	Quantitative approach	Pragmatic approach
Connection of theory and data	Induction	Deduction	Abduction
Relationship to research process	Subjectivity	Objectivity	Inter-subjectivity
Inference from data	Context	Generality	Transferability

Source: Morgan (2007, p. 71)

Rather than favouring deduction or induction, pragmatism espouses abduction (Nelson & Evans, 2014). The pragmatic approach uses abductive reasoning which moves back and forth between induction and deduction by firstly converting observations into theories and then assessing those theories through action (Morgan, 2007). Morgan (2007) contends that one of the most common uses of this type of reasoning is to further a process of inquiry that evaluates the results of prior inductions through their ability to predict the workability of future lines of behavior. He reasons that the inductive results from a qualitative approach could serve as inputs to the deductive goals of a quantitative approach, and vice versa. The advantage of such an approach is that it combines loyalty to the existing theory with loyalty to the new data, instead of taking sides (Sinkovics & Alfoldi, 2012).

Pragmatism emphasizes inter-subjectivity, rather than favouring objectivity or subjectivity (Nelson & Evans, 2014). In explaining inter-subjectivity, Morgan (2007, p. 72) argues the usual forced dichotomy between subjective and objective is an equally forced artificial summary of the relationship between researchers and the research process, and that any practicing researchers have to work back and forth between various frames of reference. Morgan (2007, p. 72) thus claims that with a pragmatic approach there is no problem in asserting both that “there is a single ‘real world’ and that all individuals have their own unique interpretations of that world”. Transferability proposes that findings need not to be so unique that they have no implications beyond the research context or so generalised that they would apply across the board in any setting (Dures, Rumsey, Morris, & Gleeson, 2010; Morgan, 2007).

Morgan (2007) advocates transferability as arising from a solidly pragmatic focus on what people could do with the knowledge they produce and how much existing knowledge might be usable in a new set of circumstances. Morgan (2007) concludes his arguments for a pragmatic approach by indicating that the great strength of this approach to social science research methodology was due to its emphasis on the connection between epistemological concerns about the nature of the knowledge that are produced and technical concerns about the methods that are used to generate knowledge.

Creswell (2014, p. 11) claims that pragmatism provides a basis for the following knowledge states:

1. Pragmatism is not committed to any one system of philosophy and reality. This applies to mixed methods research in that inquirers draw liberally from both quantitative and qualitative assumptions when they engage in their research.
2. Individual researchers have a freedom of choice. In this way, researchers are free to choose the methods, techniques, and procedures of research that best meet their needs and purposes.
3. Pragmatists do not see the world as an absolute unity. In a similar way, mixed methods researchers look to many approaches for collecting and analysis data rather than subscribing to only one way (e.g., quantitative or qualitative).
4. Truth is what works at the time. It is not based in a duality between reality independent of the mind or within the mind. Thus, in mixed methods research, investigators use both quantitative and qualitative data because they work to provide the best understanding of a research problem.
5. The pragmatist researchers look to the *what* and *how* to research based on the intended consequences- where they want to go with it. Mixed methods researchers need to establish a purpose for their “mixing,” a rationale for the reasons why quantitative and qualitative data need to be mixed in the first place.

6. Pragmatists agree that research always occurs in social, historical, political, and other contexts. In this way, mixed methods studies may include a postmodern turn, a theoretical lens that is reflective of social justice and political aims.
7. Pragmatists have believed in an external world independent of the mind as well as that lodged in the mind. But they believe that we need to stop asking questions about reality and the laws of nature (Cherryholmes, 1992).

Pragmatism was suggested as the philosophical assumption by many social scientists (see for example: Johnson & Onwuegbuzie, 2004; Morgan, 2007; Onweugbuzie, 2002; Tashakkori & Teddlie, 1998) for mixing quantitative and qualitative approaches. Consequently, pragmatism is associated with mixed methods research (Feilzer, 2010). It enables researchers to combine elements of qualitative and quantitative research approaches (Creswell, 2014). Mixed methods research designs have been growing in popularity in the accounting literature (Birchall, Murphy, & Milne, 2016; Brown & Brignall, 2007; Kakkuri-Knuuttila et al., 2008; Martinov-Bennie & Mladenovic, 2015; Modell, 2005, 2010; Vaivio & Sirén, 2010).

6.3 Mixed methods approach

The mixed methods research approach by definition is:

> …the type of research in which a researcher or team of researchers combines elements of qualitative and quantitative research approaches (e.g., use of qualitative and quantitative viewpoints, data collection, analysis, inference techniques) for the broad purposes of breadth and depth of understanding and corroboration (Johnson, Onwuegbuzie, & Turner, 2007, p. 123).

This research methodology is argued to be intellectual and practical, as it is likely to have the advantage of overcoming the weaknesses inherent in single methods (Johnson & Onwuegbuzie, 2004), and to provide the most informative, complete, balanced, and useful research results (Johnson et al., 2007). The mixed methods research approach evolved from triangulation (Tashakkori & Teddlie, 2003). Triangulation has been defined as the "combination of methodologies in the study of the same phenomenon" (Denzin, 1970, p. 297). The researchers have used various terms to describe mixed methods research approach. For example, it is termed as 'multi-strategy research' in Bryman (2001), 'multimethod research' in

Brewer and Hunter (2006), and 'multiple methods' in Robson (2002). According to Creswell (2003, p. 18), the mixed methods approach employs "strategies of inquiry that involve collecting data either simultaneously or sequentially to best understand research problems". It involves gathering numerical and text data with a research database containing both quantitative and qualitative information (Creswell, 2003).

In the last two decades, mixed-methods research has been applied widely in many fields of social science, such as sociology, education, evaluation, and health science (Creswell, 2009; Molina-Azorín, 2011). In the fields of management and accounting research where positivism has long dominated, mixed methods research has started to attract increasing attention (Cassell, Buehring, Symon, Johnson, & Bishop, 2006; Grafton, Lillis, & Mahama, 2011; Modell, 2005, 2009a, 2010). The mixed method approach permits a more thorough and comprehensive investigation of the subject than would the use of one method alone. The mixed method approach also helps to achieve cross validation of data and so avoids information bias which can stem from the use of a single method of gathering data (Hussey & Hussey, 1997; Silverman, 2013). The combination of the quantitative and qualitative approaches permits the shortcomings of each to be overcome (Creswell & Clark, 2011; Johnson & Onwuegbuzie, 2004).

A purely quantitative study might not be suitable for exploring SME financial reporting in Sri Lanka. The holistic meaning of SME financial reporting should be obtained by way of qualitative approach considering the effects of the interactions amongst the accounting practitioners, regulators, users of accounting information and the environment on the financial reporting phenomenon. This form of inquiry enables a researcher to construct knowledge of the phenomenon being studied by interpreting the meaning of human action within its social setting (Chua, 1986a) and helping develop a deep understanding of the empirical results.

The pragmatic philosophical perspective is therefore, deemed appropriate for the adoption of mixed methods research in the present thesis. As explained in Chapter 1 and Chapter 2 of this thesis, financial reporting in developing countries, and in particular in Sri Lankan SMEs, is a field in which the underlying concepts have not been adequately addressed in the extant literature. A mixed method approach allows a rich and comprehensive description about SME financial reporting in Sri Lanka to be obtained.

6.4 Mixed methods research design for this thesis

The importance of mixed methods design was fundamental in designing the framework for this thesis. There has been a great deal of attention paid to the classification of mixed methods design since the end of the 1980s (Creswell & Clark, 2007). A recent classification of Creswell and Clark (2011) point out that there are four main mixed methods designs: 1) convergent parallel design; 2) explanatory sequential design; 3) exploratory sequential design; and 4) embedded design. However, although different features have been emphasized and different names have been given, there are more similarities than differences among these classifications (Creswell & Clark, 2011).

There are four key principles for designing mixed methods research: 1) the level of interaction between the quantitative and qualitative methods; 2) the relative priority or weight given to the quantitative and qualitative methods; 3) the timing of the quantitative and qualitative data collection and analysis; and 4) the stage or stages in the research process at which the quantitative and qualitative phases are connected and the results are integrated (Creswell & Clark, 2011; Ivankova, Creswell, & Stick, 2006; Morgan, 1998). Three types of decisions are to be addressed in light of these principles, namely the interaction decision, the timing decision, and the weighting and mixing decision.

Interaction decision

The level of interaction between the quantitative and qualitative method is an important principle. There are two levels of interaction: 1) the independent level; and 2) the interactive level (Creswell & Clark, 2011). This thesis adopts the independent level of interaction, where the quantitative and qualitative methods are implemented so that they are independent from the other. The researcher only mixes the two methods when drawing conclusions during the overall interpretation at the end of the study.

Timing decision

Timing (also named as "implementation" or "sequence") refers to the temporal relationship of the quantitative and qualitative data collection and analysis (Creswell & Clark, 2011; Greene, Caracelli, & Graham, 1989; Morgan, 1998). Timing relates to the decision on whether the quantitative and qualitative studies are in a sequence (one following another), or concurrently (Ivankova et al., 2006). Concurrent timing occurs when the quantitative and qualitative data are collected and analysed at the same time. On the other hand, in the sequential study, quantitative and qualitative data are collected and analysed over the period of time in two distinct phases. It means that the researchers use one type of data before using the other data type (Creswell & Clark, 2011; Ivankova et al., 2006).

For this thesis, concurrent timing was adopted due to both theoretical and practical considerations. Both numerical and narrative data were used to provide a broad and complementary explanations of the SME financial reporting in Sri Lanka. For the purpose of validation, the data were triangulated by comparing and contrasting quantitative statistical results with qualitative findings. It is suggested that the concurrent design is more appropriate for a mixed methods study in which the purpose is to take advantage of data triangulation (Creswell & Clark, 2011; Ivankova et al., 2006). Since the research field is Sri Lanka, both types of data had to be collected in one visit to the field within a limited time frame. If the quantitative and qualitative phases are conducted sequentially, the two phases of data collection could not be completed within the time frame. Concurrent design was therefore, adopted for this thesis.

Weighting decision and mixing decision

In concurrent designs, there is a weighting option. The research may give equal weight to both the quantitative and qualitative methods or may weight them unequally (Creswell & Clark, 2011). This thesis gives equal weight to both quantitative and qualitative methods as both approaches were used to address the research questions of the thesis.

Researchers need to decide how to mix quantitative and qualitative data within their research (Creswell & Clark, 2011). According to Creswell and Clark (2011, p. 66), "mixing occurs at four possible points during the research process: interpretation, data analysis, data collection, and design". This thesis mixed quantitative and qualitative findings when the results were interpreted. Mixing during interpretation occurs when the quantitative and qualitative findings are mixed during the final step of the research process after the researcher has collected and analysed separately both sets of data (Creswell & Clark, 2011). In this thesis, the data collection and analysis of the quantitative and qualitative thesis are reported separately, and then integrated to answer the research questions.

Findings from the quantitative and qualitative thesis are compared and connected when the results are discussed. While the triangulation approach adopted was useful to capture a holistic understanding of a social phenomena, it also created challenges in analysing and making sense of empirical evidence collected from various sources and in different ways (Hoque & Hopper, 1997). To overcome this problem, results obtained from the quantitative data were matched with various themes/concepts identified in the interview data analysis (Sharma et al., 2010; Tsamenyi et al., 2006) at the interpretation stage. Figure 3 illustrates the concurrent mixed methods design for this thesis.

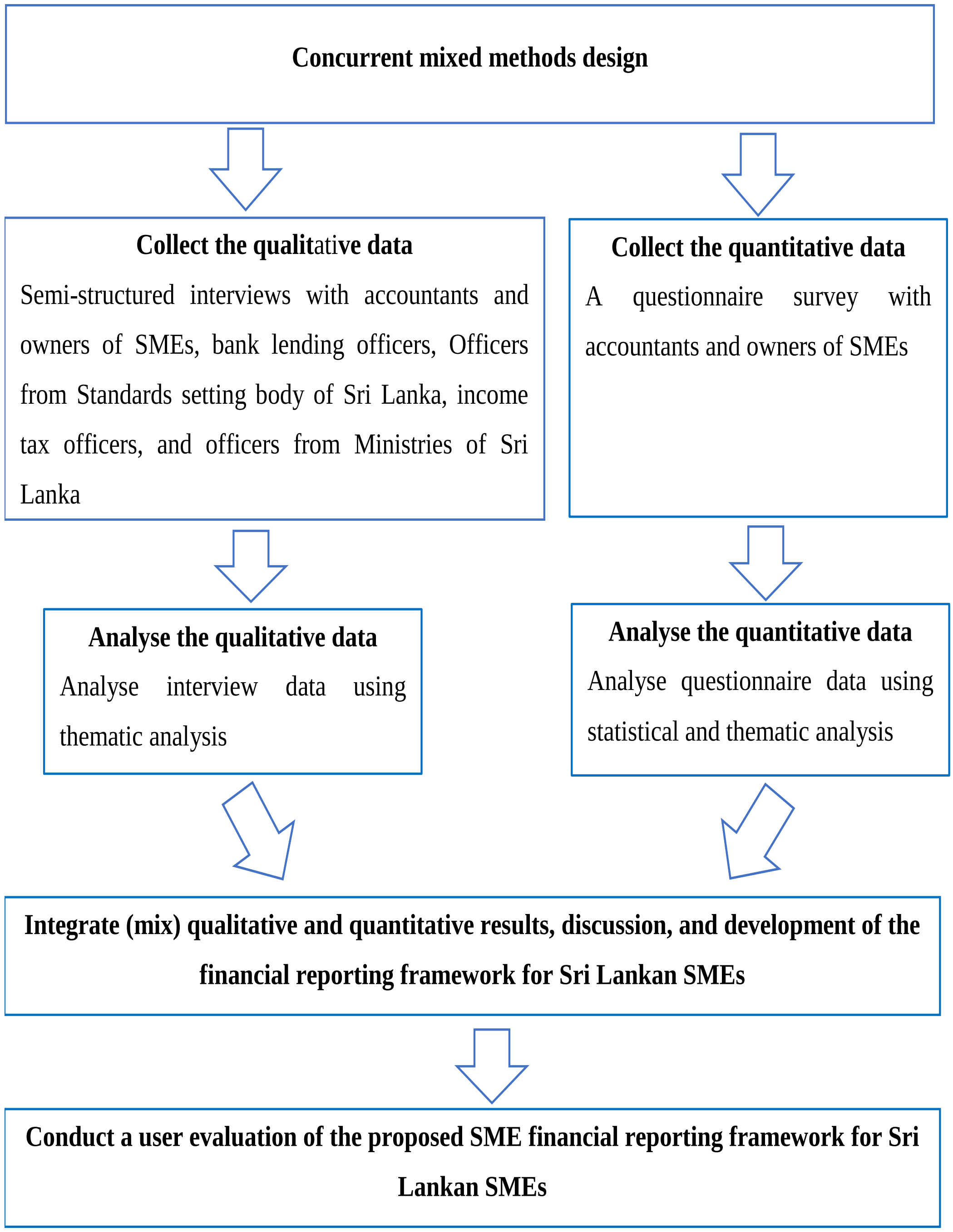

Figure 3 : Concurrent mixed methods design for this thesis

Source: Author

The qualitative data collection involved semi structured interviews with a sample consisting of accountants and owners of SMEs, bank loan officers, tax officers, officers from standards setting body of Sri Lanka, and officers from Ministries of Sri Lanka. The quantitative data collection was by questionnaire survey of accountants and owners of SMEs. SME accountants refer to those who are working for SMEs in the position of accountants or preparing SME financial information. Thematic analysis was used to analyse the qualitative data, while statistical analysis was applied to the quantitative data acquired from the questionnaire survey. Both quantitative and qualitative data collection were undertaken concurrently. Following the integration of the results obtained from the qualitative and quantitative data analysis, a financial reporting framework for Sri Lankan SMEs was developed. As the final stage of the research a user evaluation of the proposed framework was conducted to test the appropriateness of the framework to users of SME financial information. For this purpose, only a limited number of users of SME financial information, were selected and interviewed.

6.5 Summary

This chapter described the research methodology adopted for this thesis. The underlying philosophical assumptions were addressed at the beginning of the chapter. A discussion of the positivism and interpretivism paradigms were provided as an aid for understanding the approach to the research. The pragmatic philosophical perspective is adopted and its tenets are clarified. This pragmatist point of view is illustrated as rejecting the forced choice between positivism and interpretivism with regard to methods, logic and epistemology (Tashakkori & Teddlie, 1998)**.** Pragmatic researchers place at the heart of their endeavours the research questions (Johnson & Onwuegbuzie, 2004), rather than being pre-occupied with ontological and epistemological debates about truth and reality (Cherryholmes, 1992).

Accordingly, the research thesis adopted the mixed methods methodological approach to obtain answers for the research questions. Mixed methods research approach has been widely used in social science, and researchers in the fields of management, and accounting. The mixed methods approach, provides researchers with a more thorough and comprehensive investigation of the phenomena than would the use of one method alone. As a result, by mixing quantitative and qualitative methods it is possible to take advantage of triangulation to enhance the validity of the research. Based on the research objective and research questions, the research design of this thesis employed a convergent parallel mixed methods research design in which quantitative and qualitative data were collected concurrently; analysed independently; and integrated in the discussion. The next chapter presents the research methods used in the study.

CHAPTER SEVEN

RESEARCH METHODS

7.1 Introduction

This chapter explains the research methods used to ascertain answers to the research questions of the study, using a mixed methods research design that combines both qualitative and quantitative data. This chapter outlines the procedures data collection and data analysis. Section 7.2 outlines the procedure of the interviews, including rationale for interviews, design of the interview guide, sample selection for interviews and how the interview data was processed by employing thematic analysis. Section 7.3 explains the rationale and design of the questionnaire, including sample selection, and data collection. Section 7.4 describes the ethical considerations of the research. Section 7.5 concludes the chapter.

7.2 Interviews

Interviews are one of the most important qualitative data collection methods, and have been widely used in conducting field studies and ethnographic research (Qu & Dumay, 2011). Scott and Garner (2013) define an interview as a research method to obtain data through the experiences and perceptions of individuals or groups. They are particularly useful in uncovering the life narrative behind an interviewee's experiences (Doody & Noonan, 2013). Researchers can follow a line of questioning to gain understanding about a topic (Doody & Noonan, 2013).

There are three different forms of interviews: structured; semi-structured; and unstructured (Collis & Hussey, 2009; Silverman, 2013). Structured interviews are designed to be used with a specified set of research questions (Bryman, 2012) in which the interviewer exercises a relatively high level of control over the interview conversation (Rowley, 2012). By contrast, unstructured interviews feature a relatively low level of control over the interview conversation (Rowley, 2012). In semi-structured interviews, the interviewer has a list of research questions, with the flexibility to pursue other topics that arise during the interview (Collis & Hussey, 2009). Such interviews are not limited to the prepared questions. The researcher is able to develop follow-up questions during the interview (Collis & Hussey, 2009).

Traditionally, interviews were conducted face-to-face (Novick, 2008). Scholars have argued that this ‘natural encounter’ is necessary for the interviewer to build and maintain rapport with respondents (Gillham, 2007). This method of interviewing creates a relaxed and friendly environment for the interview that is critical in stimulating respondents to speak freely and openly about the given topic. This is viewed as essential for gathering rich in-depth data (Hermanowicz, 2002). The use of face-to-face interviewing allows researchers to obtain the points of views of respondents and allows some flexibility to adjust and explain the questions, particularly when respondents appear reluctant to answer due to a lack of understanding as to the meanings of questions or are reluctant to disclose sensitive information (Curran & Blackburn, 2000). Most importantly, it enables respondents to provide responses in their own terms and in the way that they think and use language (Qu & Dumay, 2011). It proves to be especially valuable if the researchers are to understand the way the respondents perceive the social world under study (Qu & Dumay, 2011). Although Sri Lanka has a high level of literacy, SME owners may be unfamiliar with terminology as well as regarding interviewers with suspicion. Therefore, semi-structured face-to-face interviews seem the ideal method to examine users and uses of SME financial information and obtain perceptions on accounting standards for SMEs.

7.2.1 The design of the interview guide and its administration

An interview guide was developed based on the research questions of this study and issues identified in the literature. The initial interview questions were derived from previous studies (for example: Collis & Jarvis, 2000; Conseil National de la Comptabilité, 2008; Dang-Duc et al., 2008; Eierle & Haller, 2009; Maingot & Zeghal, 2006; Ploybut, 2012). These initial questions were adjusted to fit with the context of the study. Separate interview questions were generated for preparers, users, and the standard setter. The main issues addressed in the interview instruments, were the same for all respondent groups. However, some additional aspects were included for a particular group of respondents. For example, the questions concerning the reasons for adopting the accounting standard *IFRS for SMEs* were included in the interview questions for the standard setting authority, and questions concerning preparation of financial statements were included in the interview questions for accountants and owners of SMEs. The interview instrument was constructed in English and then translated into Sinhala. Sinhala is the native language of the respondents' and most of the SME owner-managers are not fluent in English. After translation, the drafts of interview instruments, in both Sinhala and English, were discussed with academics from the financial and accounting disciplines (especially academics with an interest in financial reporting by SMEs), to access the face validity of the interview instrument. The interview guide for the three groups (SME owners and accountants, users of SME financial information, and standard setter) including the Sinhala version for owner-managers and accountants of SMEs are provided in Appendix B.

Pre-testing the interview instrument was carried out with an owner-manager and an accountant in Sri Lanka who were preparers and users of SME financial information. The purpose of this pre-testing was to ensure that respondents were able to understand the questions. This pre-testing not only resulted in a number of improvements to the interview instrument in terms of wording and question order but also provided the researcher an opportunity to learn how to administer the face-to-face interview. The first version of the interview guide included the following opening question: "How do you see the business environment for SMEs at the present time…"? On hearing this question, the two respondents became very reticent and appeared overwhelmed. Accordingly, the opening question was replaced with "Tell me about your business…". This question proved to be a very satisfactory opener and was usually sufficient to generate discussion.

Interview appointments were arranged by telephone and through e-mails. All interview sessions were conducted face-to-face in the respondents' offices. Upon agreeing to take part, each respondent was sent a covering letter (see Appendix C) which outlined the purpose of the interviews. Topics to be covered in the interviews were sent to the respondents in advance of the interview, if requested. Supplying this information to the respondents enabled them to prepare themselves to provide relevant information. This procedure served to increase the validity of the information provided (Saunders, Lewis, & Thornhill, 2009). All respondents were assured of confidentiality and anonymity as communicated in the Participant Information Sheet (Appendix D). Before starting the interview, the Participant Information Sheet was given to the respondent and a signed consent form obtained (Appendix E). Respondents were asked about their preferred language for conducting the interview. This ensured that the respondents were put at ease and understood the questions being asked. Interviews were conducted either in Sinhala or English and varied in length between 30 to 50 minutes. To facilitate analysis, notes were made during the interview and the whole discussion was tape recorded (with the respondents' permission).

7.2.2 Sample selection for interviews

David and Sutton (2004) suggest it is possible to decide the appropriate sample size according to the experience of the researcher and the resources available in terms of cost and time. As suggested by the literature (see, for example, Collis, 2008; Collis & Jarvis, 2000, 2002; Dang-Duc et al., 2006; Dang-Duc et al., 2008; Deakins & Hussain, 1994; Maingot & Zeghal, 2006; Page, 1984; Rennie & Senkow, 2009; Sian & Roberts, 2009), interviews were conducted with three major user groups namely: owner-managers of SMEs, bank lending officers, and income tax officers. Internal accountants of SMEs were also interviewed because they directly involved in preparing the financial information and supporting the owner-managers.

In addition, participants were also invited from CASL as the sole authority responsible for setting the accounting standards in the country. Therefore, they could provide useful information from their perspective on SME financial reporting, particularly the adoption of *IFRS for SMEs* (example: Albu et al., 2010; Albu et al., 2013). It is also important to take into consideration government institutions that actively participate in setting policies to the SME sector. Accordingly, three government institutions were contacted. However, a representative from one government institution declined to be interviewed as he did not have available time during the interview period. Table 13 indicates the number of interviews undertaken with each group and the Table 14 sets out the number of interviews with SME owner-managers from business entities (Appendix F provides demographic data of interviewees).

Table 13 : Number of interviews with each group

Group	**Code**	**Subtotal**
Owner-managers	OM	23
Accountants	AC	6
Bank lending officers	BLO	5
Income tax officers	ITO	3
Standard setter	SS	2
Government institutions	GI	2
Total		41

Table 14 : Number of interviews with SME owner-managers.

Business sector	**Number of Business entities**
Manufacturing	13
Trading	1
Service	9
	23
Number of employees	
5-15	5
16-39	7
40-99	11
	23
Business age (years)	
1-10	6
11-25	9
>25	8
	23

The SME owners and accountants for the interviews were selected using a snowball sampling technique. Snowball sampling has been used to gain access to participants in several studies of SMEs (see, for example, Davidson, Fielden, & Omar, 2010; File & Prince, 1998; Halabi & Carroll, 2015; Holgersson, 2013; Minh & Hjortsø, 2015; Samujh, 2011). In snowball sampling the researcher accesses informants through contact information that is provided by other informants (Hogarth & Wójcik, 2016; Noy, 2008; Sumit & Kerry, 2013). Snowball sampling assists researchers in enriching sampling clusters, and accessing new participants and social groups when other contact avenues have dried up (Davidson et al., 2010; Noy, 2008). The initial selection for accountants and owners of small and medium enterprises drew upon researcher's own contacts and the introductions provided by friends and relatives.

Heterogeneity was built into the design to compensate for the non-probability nature of the sample (File & Prince, 1998; Hogarth & Wójcik, 2016) by selecting SME owners from business entities with different characteristics as shown in Table 14. Gaining access to SME owners and accountants took much longer in time than anticipated as they initially viewed the researcher's efforts with suspicion. However, through respondents' recommendations, access was obtained to other respondents.

The bank lending officers were selected from private and government banks in Sri Lanka. The initial list of private and government banks was prepared and ranked based on loans granted to the SME sector (Ministry of Finance and Planning, 2013). This search of banks produced a list of 5 government banks, and 8 private banks. Copies of an introductory letter explaining the purpose were sent to all head offices of those banks and a request made for representatives to participate in the research study. The contacts resulted in six agreements to participate. Five interviews were completed.

The researcher obtained the approval from the Deputy Commissioner General of Human resources at the Inland Revenue Department of Sri Lanka to contact income tax officers. Three income tax officers gave their consent to participate in the study. The standard setter in Sri Lanka was contacted to request interviews from officers at the technical division. As a result, two officers at the technical division of the standard setter of Sri Lanka agreed to participate in the interviews. The researcher contacted the two government institutions in Sri Lanka. Representing two government institutions, two directors in charge of SMEs gave their consent to participate in the study.

7.2.3 Follow-up interviews

Follow-up interviews were conducted in 2017 in order to obtain feedback on the proposed financial reporting framework, which was developed as part of this thesis and based on the findings from the first round of interviews. These follow-up interviews were conducted to enrichen, update and validate the proposed financial reporting framework for Sri Lankan SMEs. Since the CASL introduced another tier of accounting standards for SMEs subsequent to the first set of interviews, respondents' perceptions of this latest accounting standard were also obtained.[30]

Twenty-two respondents were contacted for follow-up interviews via e-mail and telephone, but only eight agreed to participate (see Table 15). Accordingly, eight semi-structured telephone interviews were conducted. A telephone interview is defined as a strategy for obtaining data which allows interpersonal communication without a face-to-face meeting (Carr & Worth, 2001). Telephone interviews are necessary when interviewer and respondents are located in different geographical locations (Diouf & Boiral, 2017; Farooq & De Villiers, 2017; Stephens, 2007). This is the case for this thesis, since the interviewer was located in New Zealand and research participants were located in Sri Lanka. Telephone interviews were conducted using Skype. The Skype software allows calls to be made to landline telephone and mobile telephone numbers (Farooq & De Villiers, 2017) at low cost. Follow-up interview questions (see appendix G for the follow-up questions for users of SME financial information and the standard setter in Sri Lanka) were sent in advance of the interview. This allowed respondents to go through the proposed framework in detail and make informed comments and suggestions for modifications.

Table 15: Follow-up interviews with each group

Group	**First round of interviews**	**Follow-up interviews**
Owner-managers	23	2
Accountants	6	1
Bank lending officers	5	3
Income tax officers	3	1
Standard setter	2	1
Government institutions	2	-
Total	**41**	**8**

[30] Sri Lanka introduced Tier 3 of accounting standard known as (the *Sri Lanka Accounting Standards for Smaller Entities*) with effect from 1 January 2016.

7.2.4 Data analysis for interviews

Analysis of the interview transcripts was carried out using NVivo version 11. The use of the NVivo software facilitated the process of organising, re-arranging and managing the considerable amount of qualitative data. However, the use of NVivo requires the manual handling of data at various points (Jones & Diment, 2010). The research adopted thematic analysis (Boyatzis, 1998; Braun & Clarke, 2006) for analysing interview data. Thematic analysis is a method for "identifying, analysing and reporting patterns or themes within data" (Braun & Clarke, 2006, p. 79). Boyatzis (1998) and Braun and Clarke (2006) claim that thematic analysis is independent of, and can be applied across, a range of theoretical, ontological and epistemological approaches. As a method of analysis, thematic analysis is consistent with the pragmatic philosophical assumptions underlying this thesis. Braun and Clarke (2006) identified six phases of thematic analysis as presented in Table 16.

Table 16: Phases of thematic analysis

Phase	**Description of the process**
1.Familiarising yourself with your data	Transcribing data (if necessary), reading and re-reading the data, noting down initial ideas.
2.Generating initial codes	Coding interesting features of the data in a systematic fashion across the entire data set, collating data relevant to each code.
3.Searching for themes	Collating codes into potential themes, gathering all data relevant to each potential theme.
4.Reviewing themes	Checking if the themes work in relation to the coded extracts (Level 1) and the entire data set (level 2), generating a thematic 'map' of the analysis.
5.Defining and naming themes	Ongoing analysis to refine the specifics of each theme and the overall story the analysis tells, generating clear definitions and names for each theme.
6.Producing the report	The final opportunity for analysis. Selection of vivid, compelling extract examples, final analysis of selected extracts, relating back of the analysis to the research question and literature, producing a scholarly report of the analysis.

Source: Braun and Clarke (2006, p. 87)

All six stages were used to analyse the interview transcripts:

Phase one: Familiarise yourself with your data

Braun and Clarke (2006) highlight the importance of being immersed in the data to become familiar with its scope and boundaries. Transcribing verbal interview data is an excellent way to gain familiarity with the data and should be viewed as an important data analytic phase (Bird, 2005). All 49 interviews were therefore transcribed. This thesis adopted the verbatim approach in transcribing the interviews in order to develop a deeper understanding of the respondents' views. Interviews took place in Sinhala were translated and transcribed into English. The transcription process enabled the researcher to obtain greater familiarity with the data and gave opportunity to be more engaged with the data. The transcription was checked while re-listening to the tape to ensure that any important information had not been missed. Transcriptions were read repeatedly and any initial ideas for coding were noted as they arose (Braun & Clarke, 2006).

Some respondents requested to see their transcription once they were completed. Complete transcriptions were sent to these respondents and three other randomly selected participants to confirm whether or not the transcriptions represented their views. On average, between 8 to 10 hours were required to transcribe each interview with the transcript length varying from 8 pages to 12 pages. Once transcription was complete, all interview transcripts were imported to NVivo. Interview transcripts were stored in internal sources in NVivo (see figure 4 below for an illustration).

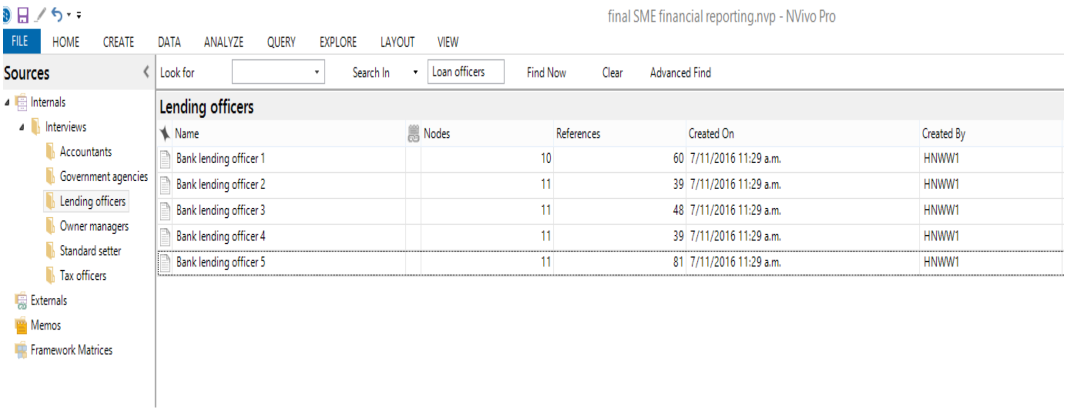

Figure 4: An example of interview transcripts imported to NVivo

Phase two: Generating initial codes

After transcription of recorded interviews, coding, the second phase of analysis was undertaken. Codes identify a feature of the data that appears interesting to the analyst, and refer to “the most basic segment, or element, of the raw data or information that can be assessed in a meaningful way regarding the phenomenon” (Boyatzis, 1998, p. 63). Braun and Clarke (2006, p.84) say “researchers cannot free themselves of their theoretical and epistemological commitments, and data are not coded in an epistemological vacuum”. Text segments that were deemed to be meaningful and relevant to the research question were highlighted and attached to a node (code) created in the NVivo (see figure 5 below for an illustration). In NVivo, codes were entered as ‘nodes’ and form the basis for categorising the data. Nodes are ‘containers’ for categorising the projects, ideas, or topics the researcher is interested in (Richards, 2009). This process was repeated for all interview transcripts. When any type of node is opened in NVivo, all the relevant references can be seen in one place. Thus, NVivo facilitates to reflect on the data, develop ideas, and discover patterns.

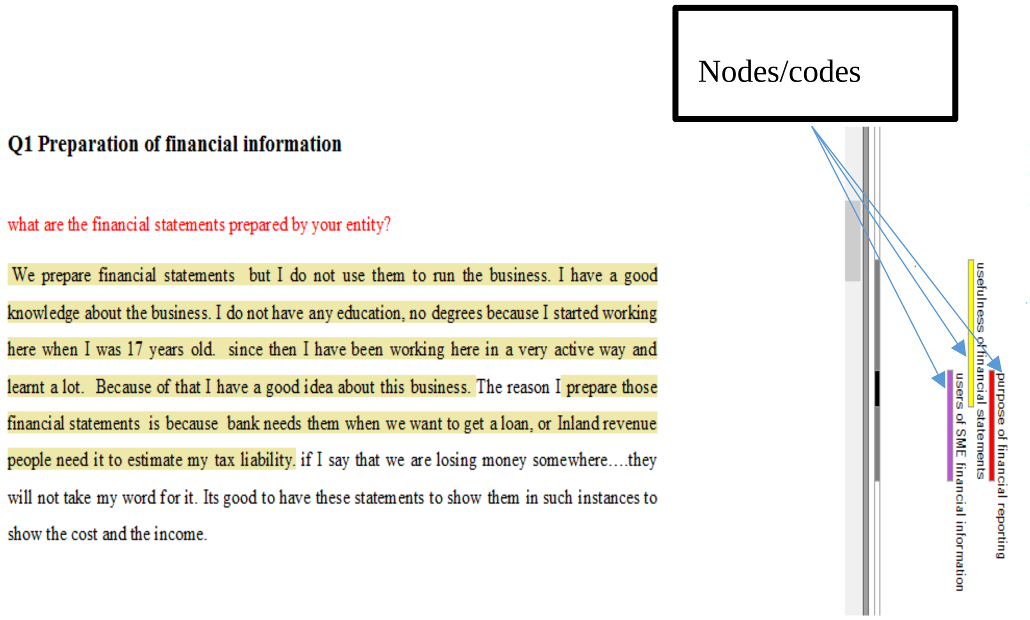

Figure 5: An example of ‘coding’ in NVivo

Phase three: Searching for themes

Phase three begins when all data have been coded and collated. This involves categorising the different codes into potential themes and assigning the relevant coded extracts to the specific themes (Braun & Clarke, 2006). Codes were sorted into potential themes using NVivo and some codes were combined to form the main themes of the analysis. This phase ends when a set of themes and sub themes have been linked to the extracts of data (Braun & Clarke, 2006). Sub-themes were created by combining codes that were alike and share similar or common features. In NVivo, nodes and sub-nodes were created in a hierarchical structure that contains parent and child nodes (sub-node). For example, to narrow the node 'use of financial information by owner-managers', a number of child nodes were created such as: purpose of using entity's financial information; separate set of accounting records for management; use of management information for decision making; and usefulness of financial statements.

These child nodes were then analysed, narrowed, and coded into child node categories. For example, the child node of use of management information for decision making was coded into types of management information and usefulness of management information. It was an on-going process and required naming and renaming nodes (see figure 6 below for examples of parent and child nodes). At this stage, some codes were identified that were not directly fit into the main themes. Therefore, a 'theme' called 'miscellaneous' was created to house codes temporarily (Braun & Clarke, 2006). At this point, the importance of individual themes was considered. However, "without looking at all the extracts in detail (the next phase) it is uncertain whether the themes hold as they are, or whether some need to be combined, refined, and separated, or discarded" (Braun & Clarke, 2006, pp. 90-91).

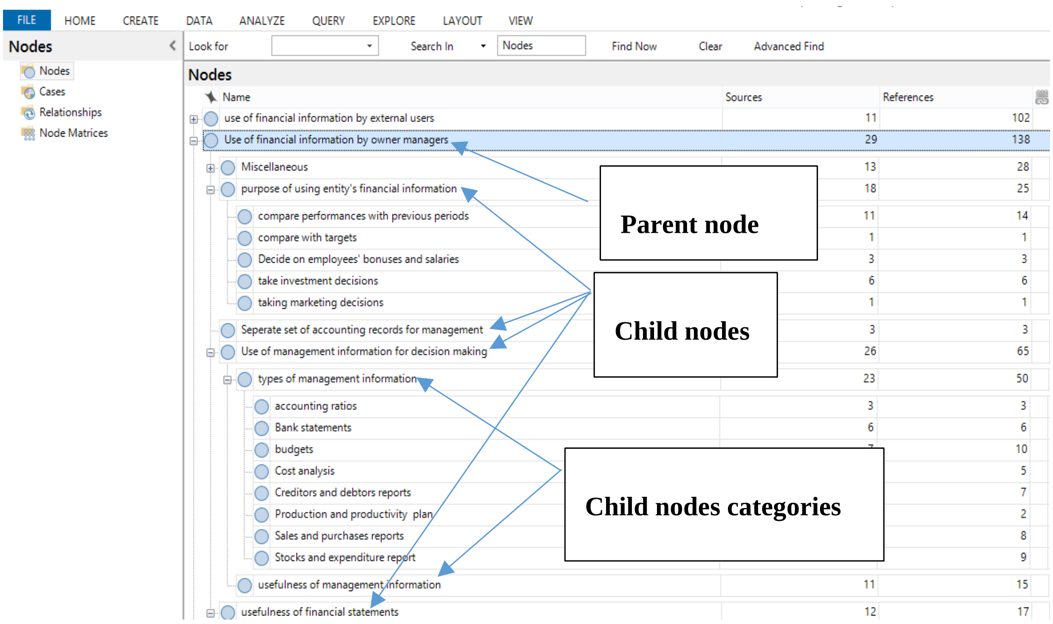

Figure 6 : Examples of parent and child nodes created in NVivo

Phase four: Reviewing themes

This phase involves two levels of reviewing and refining themes (Braun & Clarke, 2006). Level one involves reviewing at the level of the coded data extracts (Braun & Clarke, 2006). Accordingly, all themes and sub themes were read and checked to make sure that the segments of texts were matched with the themes they were attached to. Some data extracts that did not fit into themes were removed.

Level two involves a similar process, but to the entire data set (Braun & Clarke, 2006, p. 91). All the transcripts were re-read critically to make sure that all relevant text had been properly attached to themes and sub themes. During this process, any relevant text that had not previously been coded was allocated to the themes and sub themes already identified. Once the themes, sub themes appeared to satisfactorily reflect the transcript data set, and no substantial revision seemed necessary, phase 4 was deemed complete.

Phase five: Defining and naming themes

The fifth step of thematic analysis was to arrive at a thematic map of the data and to start defining themes, subthemes, and their meanings (Braun & Clarke, 2006). A number of themes and sub themes were created as a result of reading all transcripts, analysing, and coding (see appendix H). Boyatzis (1998, p. 31) stresses that the name of themes should be: "(a) conceptually meaningful to the phenomenon studies; (b) clear and concise, communicating the essence of the theme in fewer words possible; and (c) close to data". Braun and Clarke (2006, p. 93) advise "names need to be concise, punchy, and immediately give the reader a sense of what the theme is about". Figure 7 illustrates some of the themes and subthemes generated for analysis of the first research question of the study.

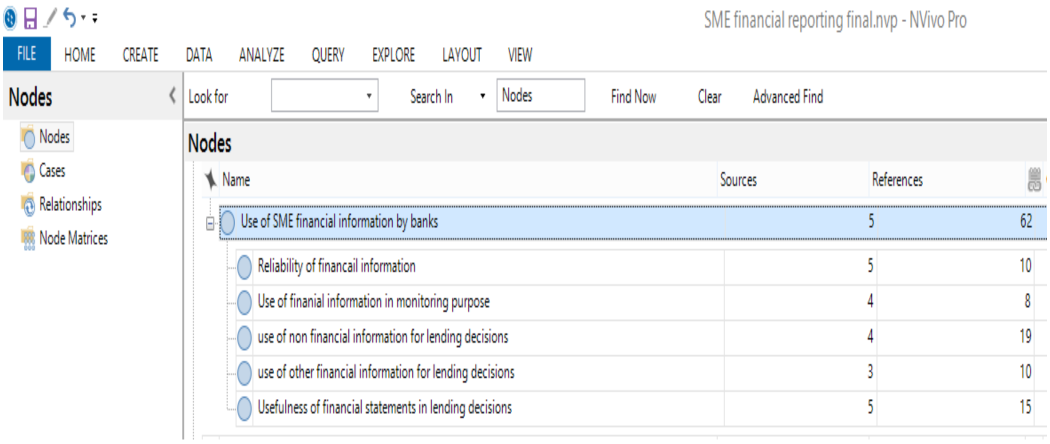

Figure 7 : An illustration for themes and sub themes created in the study

Phase six: Producing the report

This is the last phase of the thematic analysis as elucidated by Braun and Clarke (2006). It consists of writing up the story revealed by the thematic analysis. According to Braun and Clarke (2006), the write up should be a concise and coherent account of the story with sufficient text extracts to demonstrate evidence of the themes. The output of this phase is produced in the chapter 9 on qualitative data analysis.

7.3 Questionnaire survey

The survey allows a study of the perceptions of a large number of persons who are geographically dispersed (Bryman & Bell, 2011). The aim of this thesis is to identify users of SME financial statements and their information needs, to develop a financial reporting framework for Sri Lankan SMEs. A questionnaire survey is an efficient means of data collection when a value, opinion, or belief is the subject of interest (Nazari, Kline, & Herremans, 2006; Robson, 2011). A questionnaire survey permits "data to be collected from a representative sample across many industries and geographical regions where small companies have activities" (Collis & Jarvis, 2002, p. 102). It is also a most direct approach used to investigate the information needs of users (Beattie & Pratt, 2002).

The questionnaire survey has commonly been employed in accounting research (Collier & Wallace, 1992; Van der Stede, Young, & Chen, 2005). The literature review, shows a substantial amount of research on SME financial reporting was conducted through questionnaire surveys (see for example: Collis, 2008; Collis & Jarvis, 2000, 2002; Dang-Duc et al., 2006; Dang-Duc et al., 2008; Deakins & Hussain, 1994; Maingot & Zeghal, 2006; Page, 1984; Rennie & Senkow, 2009; Sian & Roberts, 2009).

Questionnaires can be administered by mail, by interview (face-to-face), by telephone or web-based (Bowling, 2005; Szolnoki & Hoffmann, 2013). Postal questionnaires involve the researcher posting the questionnaire and covering letter to the sample, and enclosing a stamped addressed envelope for the return of the completed questionnaire. The literature indicates that postal surveys typically produce low response rates, frequently 10 per cent or less (Sian & Roberts, 2009). Therefore, a sample bias problem arises, as these respondents may not accurately represent the population. There are various ways in which the response rate may be improved. For instance, questions should be clear, unambiguous, and non-controversial (Dillman, 2011). A Web-based questionnaire permits access to large sample sizes at a low cost of administration (Sue & Ritter, 2007). However, this data collection technique suffers from a lower response rate and technical issue such as spam filters (Bryman & Bell, 2011; Sue & Ritter, 2007). It is also restricted in sampling coverage as the selected samples must have access to the Internet or email addresses (Fielding, Lee, & Blank, 2008).

The researcher initially decided to use both postal and web based questionnaires. A web based questionnaire was constructed and hosted by an online survey service provider, called Qualtrics. However, during the first three weeks of data collection, the high rate of inactive email addresses and no response were experienced. The web survey was abandoned as it seemed to be unpopular among the owners and accountants of SMEs in Sri Lanka.

7.3.1 The design of the questionnaire instrument

The questionnaire survey was conducted with owner-managers and accountants of SMEs and the same questionnaire was used for both groups. The questionnaire was developed based on the research questions and issues identified in the literature. Some questions were adopted from the questionnaires used in the previous research (such as: Collis & Jarvis, 2000; Conseil National de la Comptabilité, 2008; Dang-Duc et al., 2008; Eierle & Haller, 2009; Maingot & Zeghal, 2006; Ploybut, 2012). The development of questionnaire instrument was presented in Appendix I. The questionnaire comprised four main parts:

Part I - General information

Part II - Preparation of financial statements

Part III – Users and uses of financial information

Part IV – Accounting standards for SMEs

The questionnaire used both closed and open-ended questions. Closed questions provide a fixed number of alternative answers (Saunders et al., 2009) while open-ended questions give respondents the freedom to provide their answers in their own words (Fink, 2003). Most of the questions were closed-ended with multiple choices and with a rating scale, to facilitate the different perceptions of respondents. The questionnaire was designed with clear and simple formats and instructions placed at the beginning of all sections and on the top of every answer box. In addition, the questionnaire was accompanied by a covering letter explaining the purpose and significance of the research and emphasising the contribution the respondents would make to the research by filling out the questionnaire. The benefit that the respondents might receive from participating in the survey, such as their contribution to financial reporting reform was emphasised to increase the interest of the respondents in the research. The respondents were guaranteed anonymity and confidentiality of their answers and the research findings would be available to the respondents on request. The questionnaire was also sent with a self-addressed free-post envelope to facilitate the return of the questionnaire. Furthermore, follow up letters were sent to all respondents approximately four weeks after the first request. A copy of the questionnaire is presented in Appendix J.

The draft questionnaire was originally constructed in English and then translated into Sinhala (see Appendix K) as it was felt that owners and accountants of SMEs will be more comfortable in answering questionnaire in their own first language. Table 17 provides an example for a Sinhala translation. The English draft was reviewed by the supervisory panel of this research thesis. After the Sinhala version of the questionnaire was developed, the feedback and comments from two Sri Lankan accounting practitioners were obtained. Some minor corrections were completed and the Sinhala version was approved as an accurate reflection of its original English version and pilot tested before it was used for the survey.

Table 17: Example of a Sinhala translation of the questionnaire

	කිසිදාක නැත	කලාතුරකින්	සමහර විට	නිතරම	බොහෝ විට
ලැයිස්තුගත නොවන සමාගම් වල ආයෝජන (Investment in non-listed companies)					
ලැයිස්තුගත සමාගම් වල ආයෝජන (Investment in listed companies)					
ඒකාබද්ධ ව්‍යාපාර (Joint venture)					
ආයෝජන දේපල (Investment property)					
ඉදිකිරිම් කොන්ත්‍රාත් (Construction contracts)					
සමාගම තුළ පර්යේෂණ හා සංවර්ධන ව්‍යපෘති (Research and development projects within the company)					
රාජ්‍ය ප්‍රතිපාදන (Government grants)					
විදේශ මුදල් භාණ්ඩ හා සේවා මිළ දී ගැනිම /විකිණීම (Purchase/sale of goods and services in foreign currencies)					
විදේශ විනිමය අනුපාතයට ණය සහ ණය ගැනීම් (Foreign exchange rate loans and borrowings)					
පාරිභෝගික ඇණවුම් හෝ සැපයුම් කරුගේ ප්‍රතිඵලයක් ලෙස විදේශ විනිමය අවදානම (Foreign exchange risk resulting from a customer order or a supplier)					

7.3.2 Pilot testing

The term 'pilot studies' refers to mini versions of a full-scale study, as well as the specific pre-testing of a particular research instrument such as a questionnaire or interview schedule (Teijlingen & Hundley, 2002). One of the advantages of conducting a pilot study is that it can give advance warning about where the main research project could fail, where research protocols might not be followed, or whether proposed methods or instruments are inappropriate or too complicated (Teijlingen & Hundley, 2002, p. 33).

The main purpose of the pilot test was to achieve clarification of the questions and questionnaire instructions. The pilot testing was performed by distributing the questionnaire to a small sample of respondents. A draft of the questionnaire, accompanied by a covering letter (see Appendix L), and the Participant Information Sheet (Appendix M) explaining the purposes and method of the survey was delivered to the first 32 SMEs and 35 accountants in the sampling frame. The questionnaire used for the SMEs were addressed to the owner-managers of the entities and the questionnaires for accountants were addressed to the accountants of SMEs. In the period of four weeks, 7 questionnaires from SME owner-managers and 3 questionnaires from SME accountants returned with response rates of 22 per cent and 8.5 per cent respectively.

It was observed from the pilot test that the response rate for the survey with SME accountants was low when compared to the survey with SME owner-managers. After reviewing each response from the surveys, it was evident that some respondents were not fully reading the questions. For example, in a question in which more than one answer was permitted, several respondents selected all answers even though some answers did not seem to apply to them. The survey with the SME owner-managers also indicated that respondents have difficulties with the questions asking respondents to state their agreements with costs and benefits of the accounting standard *IFRS for SMEs*. Consequently, questions on *IFRS for SMEs* were skipped by some respondents. A number of missing answers were observed in both surveys for the question on annual turnover. It seemed that they did not want to disclose their annual turnover. For ease of understanding, the revision of question wording into less technical language was suggested from the respondents. Consequently, the majority of the changes made were to wording, length, and format of the questionnaire.

The second pilot study was run in September 2015 with a sample of 50 SME owner-managers and 50 SME accountants selected from the sampling frame. After conducting three follow ups, 12 and 4 responses were received respectively with 11 out of the12 were usable. The response rates were around 24 per cent and 8 per cent respectively. When compared to the first pilot, there were no skipped close-ended questions. However, most of the open-ended questions were skipped. No issue of technical concern was noted in the pilot testing. The respondents seemed to understand the content of the questionnaire quite well and no mistakes were found in any questionnaires returned. All of the questionnaires received from two pilot tests were included in the analysis of data.

7.3.3 Sample selection for questionnaire survey

Identifying the sampling frame was a difficult because of the lack of a comprehensive database of SMEs in Sri Lanka. The most appropriate choice was the database available from the Department of Census and Statistics in Sri Lanka (Department of Census and Statistics, 2013). The profiles of SMEs in this database include the number of employees, industry classifications, mailing addresses (both e-mail and postal), and contact phone numbers. This database was used to select SMEs for the questionnaire survey. For the purpose of this thesis, a SME is an entity with 5 to 99 employees (see chapter three) having no public accountability. Public companies, state owned enterprises, and financial institutions were excluded. This definition of SMEs however, does not distinguish between legal forms for example, private companies, or sole proprietorship.

The IASB believes that the *IFRS for SMEs* is suitable for all entities that do not have public accountability, no matter the size of the organisation (International Accounting Standards Board, 2009a). Sanath Fernando, a member of the IASB Implementation Group of *IFRS for SMEs* (the advisory body to the IASB on SME financial reporting), emphasises that in the event an SME was aspiring to become a bigger company, a sound financial reporting is essential, and the *IFRS for SMEs* helps with this aspiration (Daily FT, 2014). For these reasons, sole proprietorships, and partnerships were included in the sample. This accords with prior research on *IFRS for SMEs* (see for example, Aboagye-Otchere & Agbeibor, 2012; Eierle & Haller, 2009; Kiliç et al., 2016; Van Wyk & Rossouw, 2009).

The sample was selected from the Western and Southern provinces in Sri Lanka. More than 50 per cent of Sri Lankan SMEs are located in these two provinces and contribute more than 50 per cent of the total employment for the region. (Department of Census and Statistics, 2013). In the sampling frame there were 9,456 SMEs representing the Western and Southern provinces (Department of Census and Statistics, 2013).

The Department of Census and Statistics of Sri Lanka uses 15 economic categories of SMEs in their database. To select a sample that is representative of each economic section, a categorical variable "economic section" was used for stratification. A list of SMEs in each stratum was made available by the Department of Census and Statistics. The sample was selected from each stratum using a simple random sampling technique. The final samples included 1,498 SMEs with the SME owner-managers and 957 SMEs with accountants. Accordingly, 1498 questionnaires were addressed to SME owners-managers and 957 questionnaires were addressed to accountants of SMEs. Owner-managers were surveyed since they were responsible for day-to-day activities of SMEs and make business decisions based on financial information. Internal accountants of the SMEs were also surveyed because they directly involved in preparing the financial information and supporting the owner managers. Where the SMEs outsource their accounting work, their external accountants, were not included in the survey.

7.3.4 Responses from questionnaire survey

After almost six months of data collection, a total of 358 questionnaires were returned, generating 323 usable questionnaires, of which 231 were from SME owners and 92 were from SME accountants. Table 18 provides details of the sample and responses from each survey. The overall response rate of 13 per cent. The literature shows similar studies in developed countries have experienced low response rates. For example, Eierle and Haller (2009, p. 201) experienced a low response rate of 10.3 per cent, Litjens et al. (2012, p. 235) also experienced a response rate of 11.3 per cent. In their survey with owner-managers of SMEs, Sian and Roberts (2009) achieved a very low response rate of 5.5 per cent.

Table 18: Responses from each survey

	SME owners	**SME accountants**	**Total**
Questionnaires sent out	1,498	957	2455
Questionnaires returned	252	106	358
Rejected questionnaires due to incomplete responses	12	6	18
Questionnaires filled by others	9	8	17
Usable questionnaires	231	92	323

To permit full comparability across all questions, a total of 18 incomplete responses were deleted. The respondents were asked to select their position in the organisation among the options given in the questionnaire; namely: owner, shareholder, accountant, and other. Respondents from category 'other' were deleted from the analysis as they were not included in the target group of survey in this research. Accordingly, 17 questionnaires answered by managers or employees were deleted. The incomplete responses might result from lack of understanding of the questions, as some parts of the questionnaire required a certain level of financial reporting understanding. It seemed that many responses were abandoned after the first section and some skipped the questions related to accounting standards. A total of 323 usable responses were included in the data analysis.

7.3.5 Data analysis for the questionnaire survey

One of the first techniques employed in quantitative data analysis was the quantification of the data (Pallant, 2010). This means all data needs to be converted into numerical format to be readable from the quantitative analysis software (namely, IBM SPSS for Windows, version 23). A coding scheme was used to arrange the variables tested in the study. For the missing data, two value numbers were assigned to the missing values: number "98" for missing value in optional cases (not applicable) and number "99" for missing variables if the data were required for the variables (Pallant, 2010).

It was recognised that the use of statistical tests depends on the distribution of data (Smith, 2003). The data was explored fully before the statistical tests were undertaken to decide which tests were appropriate for the data. Two types of statistical tests were considered: parametric tests and non-parametric tests. These differ in the assumptions they make about the underlying distribution of the data under analysis. Parametric statistics require that “data be drawn from normal distributions, which are smooth, bell-shaped, symmetrical curves, defined by mean and standard deviation measures” (Smith, 2003, p. 61). Non-parametric statistics “make no such assumptions regarding the underlying distribution; they describe relationships in terms of frequencies, rankings, and directional signs, rather than means and standard deviations” (Smith, 2003, p. 61).

Since most variables obtained from the questionnaire survey were categorical (nominal and ordinal) in nature, non-parametric tests for association and/or difference between two or more independent samples, such as the Chi-square test, the Mann-Whitney U test, Kruskal-Wallis test, were employed for the analysis (Pallant, 2010). The non-parametric Mann-Whitney U test was used to test the difference between two groups (between SME accountants and SME owner-managers). This test is suggested when the data are ordinal, the sample size is small, when there is no requirement of equal numbers in the two conditions, and when there is no assumption of normality (Laeven & Woodruff, 2007). Analysis was undertaken based on, three size clusters: small SMEs (between 5 to 15 employees); medium SMEs (between 16-39 employees); and large SMEs (between 40-99 employees). The Kruskal-Wallis test was used to compare two or more independent populations, when the data were either ordinal or interval and not normally distributed (Bertrand & Kramarz, 2002; Pallant, 2010).

7.3.6 Treatment of missing data and conducting non-response test

Missing data may result either because the respondents provided ambiguous answers or they did not properly record the answers. “Treatment of missing responses poses problems, particularly if the proportion of missing responses is more than 10 per cent” (Malhotra, Hall, Shaw, & Oppenheim, 2006, p. 510). The pairwise detection method used because with fewer than five per cent missing values as observed in a study, pairwise detection is best (see Brown, 1994; Davidov, Schmidt, & Schwartz, 2008; Schafer & Graham, 2002). In pairwise detection, instead of discarding all cases with missing values, only the cases or respondents with complete responses are used for each calculation (Malhotra et al., 2006).

Non-response bias is treated as a major concern in survey research. Non-response bias is defined as "the variation between the true mean value of the variable in the original sample and the true mean value in the net sample" (Malhotra et al., 2006, p. 119). For this thesis, non-response bias was assessed by comparing early and late responses, because as Morgan (1974) and Wallace and Mellor (1988) suggest late respondents are likely to answer in the similar manner of non-respondents. The responses received six weeks after the first contact were assigned as early responses, all other questionnaires were considered as late responses. A chi-square test was conducted for each characteristic such as number of employees, business ages for both surveys. The test produced no significant difference between early and late responses (see appendix N). All the 323 questionnaires were considered to be appropriate for further data analysis.

7.4 Ethical considerations

This study was guided by the ethical principles on research with human participants set out by the University of Waikato. This study was granted the ethical approval by the University of Waikato (see appendix O). The objective of the study together with details about the data collection process was explained to the respondents. The respondents for both the questionnaire survey and interviews were provided with full relevant information on the study by giving them the Participant Information Sheet which details the purpose of the research, type of information collected, participants' rights, confidentiality of the information and contact information of the researcher. They were also emphasised that they could choose not to participate in the research or that they could withdraw from the study at any time. Interviews were only conducted with the prior consent of the respondents. If they agreed to participate in the study, they were given with the Consent Form to read and sign. Further, respondents were asked to choose the interview venue and time they felt most comfortable with. Any socio-cultural sensitive, emotional, or embarrassing questions, which could possibly disturb the participants, were avoided in this research.

Completed questionnaires were kept securely in a locked filing cabinet in the researcher's office. The information was only available to the researcher and the supervisors of the thesis. Digital information was kept securely stored on a password protected hard drive and computer network that was only accessible by the researcher. During the fieldwork in Sri Lanka, all the collected hard copies of information were kept safe in a locked cabinet at the researcher's home and the soft copies in a password protected file in the researcher's personal computer. Furthermore, respondents' identities remained confidential throughout the process. They are not identified in any way. Any quotations made by the respondents are identified by an interviewee number and they are identified in the reports with nonspecific titles such as "Accountant 01, Bank lending officer 01, Owner-manager 01".

7.5 Summary

This chapter provided a comprehensive picture about how the quantitative and qualitative data have been collected and analysed. The qualitative data was gathered by means of semi-structured interviews with owners and accountants of SMEs, bank lending officers, income tax officers, and the representatives from the standard setter and representatives from government institutions in Sri Lanka. A total of 41 first round interviews and 8 follow-up interviews were undertaken. NVivo was used to organise and manage qualitative data and thematic analysis was used as a primary method for qualitative data analysis.

The quantitative study was conducted using postal questionnaire surveys with owner-managers and accountants of SMEs. A total of 323 usable responses were received. Since all data were either nominal or ordinal in nature, non-parametric tests were selected for statistical analysis. The statistical Package for Social Sciences (IBM SPSS for Windows, version 23) was employed as a tool to support the statistical analysis. Narrative data collected from open questions in the questionnaire was analysed through thematic analysis. In addition, chapter has examined the ethical principles applicable to this study. These principles include:

informed consent; protection from harm; and confidentiality and anonymity. The next chapter presents the description of data and the results of the quantitative data analysis.

CHAPTER EIGHT

QUANTITATIVE DATA ANALYSIS

8.1 Introduction

This chapter describes and analyses the quantitative data collected by means of postal questionnaire surveys with owner-managers and accountants of SMEs. Data gathered from owner-managers and accountants were aggregated and analysed in order to answer this study's two research questions: How do Sri Lankan users and their financial information needs differ with regard to size of SMEs? and Do Sri Lankan SMEs need internationally comparable financial information? A cross-tabulation analysis where the responses were compared between three sizes of SMEs was undertaken to highlight differences in various aspects of SME financial reporting.

Section 8.2 of this chapter outlines the characteristics of the entities in the research sample. Section 8.3 presents the results from the analysis of users. Section 8.4 identifies the information needs of the owner-managers for SME financial information. Section 8.5 explores the effect of the size of the SME on the information users' needs. Section 8.6 conveys the respondents' perception on the need of global financial reporting standards. Section 8.7 examines the relevance of specific accounting topics in the *SLFRSs for SMEs*. Section 8.8 reveals the adoption status of *SLFRS for SMEs*. Sections 8.9 elucidates the perceptions of owner-managers and accountants of SMEs on costs and benefits of adopting the *SLFRS for SMEs*. Section 8.10 checks the awareness of and intentions to implement the Sri Lankan latest standard for smaller entities. Section 8.11 concludes the chapter.

8.2 Characteristics of the sample entities

8.2.1 Legal form, industry, age, and size

This section describes the characteristics of the responding entities by analysing the legal form, industry, age, and size of the entities. This type of exploration enhances understanding of the responses gathered during the surveys. As shown in Table 19, 44% of the SMEs in the survey took the form of sole proprietors. Firms in the manufacturing sector made up the largest group of respondents. Fewer than 2% of the sample entities were in the agricultural business. Over half of sample firms have been in business for more than 6 years. In terms of size, 39.30% of the respondent firm had 5-15 employees; 28.8% of the respondent firms had 16-39 employees; and, 31.90% of respondent firms had 40-99 employees.

Table 19: Business characteristics of the sample entities

	Number of entities	%
Business form (N=323)		
sole proprietorship	142	44.00
Registered partnership	57	17.60
Non-registered partnership	29	9.00
Limited company	95	29.40
Type of main business (N=321)		
Manufacturing	124	38.63
Agriculture	5	1.56
Service	98	30.53
Retail etc	56	17.44
Wholesale/Distribution	38	11.84
Years in business (N=321)		
Less than 1 year	14	4.36
1-3 years	57	17.75
4-6 years	70	21.81
7-10	37	11.53
More than 10	143	44.55
Number of employees (N=323)		
5-15	127	39.30
16-39	93	28.80
40-99	103	31.90
Note: Differences in the total number of samples were caused by missing data.		

8.2.2 Ownership structure

The International Accounting Standards Board (IASB) identifies "stewardship" as one of the financial reporting objectives in the accounting standard *IFRS for SMEs*. Therefore, an examination of the ownership and management of the responding entities is an important part of the analysis. Table 20 relates the number of owner-managers for each responding entity to its number of employees. Three size clusters were created to represent entities with between 5-15, 16-39; and, 40-99 employees respectively. Results of the analysis revealed that most of the responding entities have a small number of owner-managers. Only 7% of the SMEs in the sample have more than 5 owner-managers. These findings support the claims that SMEs are usually owned by a few individuals (Collis & Jarvis, 2002; Eierle & Haller, 2009). More than 60% of the entities in the 5-15 employee category has only one owner-manager, while more than 56% of the entities in the 40-99 employee category have three or more owner-managers.

Table 20: Number of owner-managers

Number of owner-managers	**Number of employees**			**All (*N*=315)**
	5-15 (*n*=126)	**16-39 (*n*=93)**	**40-99 (*n*=96)**	
	%	**%**	**%**	**%**
1	61.10	54.80	12.50	44.40
2	15.90	19.40	31.30	21.60
3-5	21.40	23.70	37.50	27.00
More than 5	1.60	2.20	18.80	7.00
	100.00	100.00	100.00	100.00

As is shown in Table 21 (below), the majority of the responding entities were owner-managed, with almost 76% of the respondents reporting that they employed no non-manager owners.[31] As found by Carsberg et al. (1985) and Marriott and Marriott (2000), low level of separation between ownership and control in SMEs in Sri Lanka. There is less likely to be an agency relationship between an owner and a manager, as the owner can monitor the actions of an employed manager on a daily basis. In addition, the stewardship role of financial reporting may be "redundant" because managers are reporting to themselves as owners (McMahon & Stanger, 1995).

Table 21 : Existence of non-manager owners

Existence of non-manager owner	**Number of employees**			**All (*N*=311)**
	5-15 (*n*=125)	**16-39 (*n*=93)**	**40-99 (*n*=93)**	
	%	**%**	**%**	**%**
Yes	21.60	16.10	35.50	24.10
No	78.40	83.90	64.50	75.90
	100.00	100.00	100.00	100.00

[31] The non-manager owners are those who do not involve in the management of the entity.

A higher proportion of non-manager owners was to be found in large SMEs. This finding is consistent with the finding in study of German SMEs by Eierle and Haller (2009). They suggest that larger entities are more likely than smaller entities to have non-participating owners. These findings suggest that principal-agent conflicts are more likely to be seen in large SMEs than in small SMEs.

8.2.3 Accounting system

Respondents were asked to identify the system they used to maintain business records. As shown in Table 22, about 38.30% of the sample SMEs had a manual record keeping system, while 28.70% used a computerised system.

Table 22 : Analysis of accounting system

Accounting system	**Number of employees**			**All (*N* = 321)**
	5-15 (*n*=126)	**16-39 (*n*=92)**	**40-99 (*n*=103)**	
	%	**%**	**%**	**%**
Manual record keeping	69.80	33.70	3.90	38.30
Computerised accounting system	12.7	18.50	57.30	28.70
Combination of manual and computerised	17.5	47.80	38.80	33.00
	100.00	100.00	100.00	100.00

As indicated in Table 22, medium and large SMEs showed a higher proportion of computerised system or combined accounting system usage than small entities did. Similarly, studies by Sian and Roberts (2009) and McMahon (1999) derive that compared to small SMEs, large SMEs are more likely to use computerised accounting systems.

8.2.4 Services provided by external accountants

In order to examine the role of external accountants, the respondents were asked to indicate the services they obtained from external accountants. Four services were listed in the questionnaire. A category "other" was also included so that to the respondents could add any other services obtained from external accountants. However, respondents to the questionnaire survey did not identify any other services provided by external accountants. The results are summarised in Table 23.

Table 23: services provided by external accountants

Services provided by external accountants	**Number of employees** 5-15 (*n*=127)	16-39 (*n*=93)	40-99 (*n*=103)	**All (*N*=323)**
	%	**%**	**%**	**%**
Bookkeeping	58.30	44.10	17.50	41.20
Preparation of financial statements	75.60	58.10	53.40	63.50
Taxation service	60.60	54.80	54.40	57.00
Audit service	23.60	22.60	64.10	36.20

The majority of the respondents use external accountants for preparing financial statements and for taxation services. Almost 64% of the respondents report that an external accountant prepared their annual financial statements. This finding is consistent with the studies of UK SMEs by Collis (2008) and the Professional Oversight Board for Accountancy (2006). Further, it was found that more than 41% of respondents obtain bookkeeping services from external accountants. The reason why a higher proportion of respondents use external accountants for bookkeeping, preparation of financial statements, and taxation services is because it is not cost effective to employ internal accounting staff to perform such accounting tasks. The complexity of accounting and taxation rules may also be a reason why expertise is needed when dealing with these areas.

Overall, the uses of outside accountants for bookkeeping and preparing financial statements was found more often in the small and medium SMEs than in the large SMEs. A smaller proportion of the large SMEs however, use external accountants for bookkeeping. It seems that large SMEs tend to hire in-house accounting staff. As a result, they were, when compared with the other two categories, less reliant on external accountants. This finding is consistent with the Professional Oversight Board for Accountancy (2006). A questionnaire survey of 600 UK company directors finds that 85 per cent of the surveyed companies use external accountants for preparing financial statements, with a higher level of support sought by small rather than medium-sized SMEs (Professional Oversight Board for Accountancy, 2006). However, this thesis establishes the majority of the large SMEs (53.40%) use external accountants to prepare their financial statements. One possible explanation is that internal staff employed in these entities were not competent enough to apply the *IFRS* in the preparation of financial statements. Another reason is that the Inland Revenue Act of Sri Lanka requires certain businesses[32] to submit financial statements prepared by an approved accountant (see section 2.6.4).

The results show more respondents from large SMEs indicate that they obtain audit services from external accountants than did those from small and medium entities. Audit requirements imposed by the Department of Inland Revenue of Sri Lanka is a reason why audit services are obtained by large SMEs (see section 2.6.4). However, the majority of respondents from each size category used outside accountants for taxation service.

8.3 Users of Sri Lankan SME financial statements

When the IASB introduced the *IFRS for SMEs* in 2009, various user groups such as shareholders, creditors, employees, and the public were identified as main users of SME financial information (International Accounting Standards Board, 2009b, p. 7). The IASB's rationale for the identification of users and uses of SME financial information is based on the decision-usefulness objective of financial reporting. Given that Sri Lanka adopted the *IFRS for SMEs* as the Sri Lanka Accounting Standards for SMEs *(SLFRS for SMEs)* without any modifications, the question of who uses Sri Lankan SME financial information is of interest.

Respondents were requested to indicate from a list of potential users, which users they viewed as main users of their financial information. Potential users were derived from the extant literature. More than one answer was permitted. As shown in Figure 8, owner-managers, bank and financial institutions, and Inland Revenue Department of Sri Lanka were identified in the top three ranked main users by over 60% of the respondents. Unsurprisingly, a large majority of respondents perceive banks to be one of the main users of SME financial information, since banks are the major source of finance to SMEs. This finding is supported by research on users of SME financial information; for example in Ireland (Barker & Noonan, 1996), in

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[32] Any partnership, or by any sole proprietorship other than any company having a turnover of not less than fifty million rupees or a net profit of not less than twenty five million rupees for the year are required to submit statement of accounts prepared by an approved accountant.

United Kingdom (Carsberg et al., 1985; Collis & Jarvis, 2000; Page, 1984), and in Canada (Maingot & Zeghal, 2006).

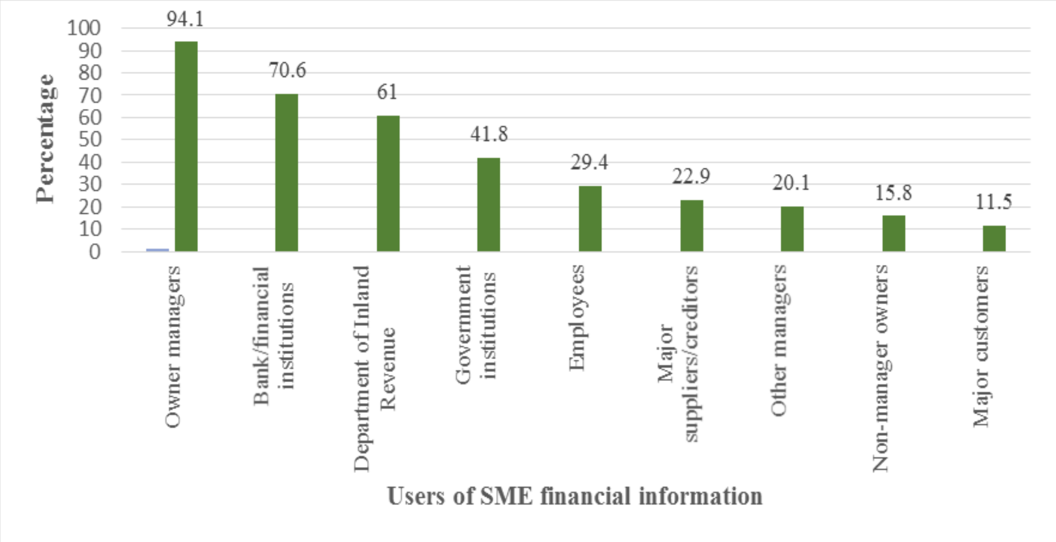

Figure 8: Users of SME financial information

While 41.80% of respondents state that government is an important user of their financial information, this appears not to be so in the UK (Sian & Roberts, 2009), where only 2.8% recognise them as a user. A relatively low proportion of respondents indicated that customers, non-manager owners, other managers, suppliers/creditors, and employees were important users. The finding with regard to non-manager owners is not surprising as majority of Sri Lankan SMEs were owner-managed. Since there is no statutory requirement for public disclosure for SME financial information in Sri Lanka, other user groups such as suppliers, and customers were not identified as users.

The IASB claim that the financial statements produced for the use by owner-managers or by tax authorities are not necessarily general purpose financial statements (International Accounting Standards Board, 2009b) and it excluded the specific needs of these two key users. It could be concluded that a less decision-usefulness perspective on the SME financial information exists in Sri Lanka. It appears that the general purpose financial reporting model advocated by the IASB is not appropriate for Sri Lankan SMEs.

8.4. Financial information needs of owner-managers of SMEs

In the SME financial reporting literature, and also in this thesis, owner-managers were identified as a main user group of SME financial information. Therefore, it is important to identify the purposes for which owner-managers of SMEs use their businesses' financial information. Owner-managers were, therefore, asked to identify these purposes. Eight purposes were listed in the questionnaire, along with the 'other' category which was added to help owner-managers to identify any other uses they made of financial information. Figure 9 illustrates the purposes for which the owner-managers of SMEs use financial information.

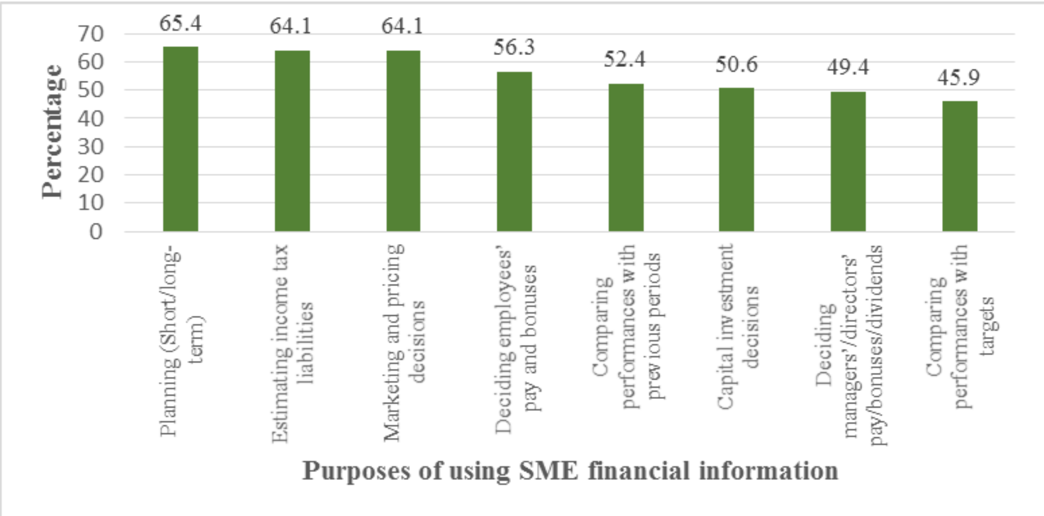

Figure 9: Purposes for which owner-managers of SMEs use SME financial information

More than 65% of all owner-managers indicated that they used financial information for planning purposes. More than 64% used financial information for estimating income tax liabilities and taking marketing and pricing decisions. Over half of the respondents employed financial information when deciding employees' pay and bonuses, comparing performances with previous periods, and making capital investment decisions. Nearly 50% of owner-managers use financial information to decide managers' or directors' remuneration. This contrasts with findings of Sian and Roberts (2009), where about 63.7% of respondents regard financial statements as unimportant to decide on directors' pay or bonuses.

Respondents were asked to rate the usefulness of specific financial reports when it came to making managerial decisions. A summary of the responses received from owner-managers is presented in Table 24. As Collis and Jarvis (2000) and Sian and Roberts (2009) report, the profit and loss statement, the balance sheet statement, and the cash flow statement were perceived to be useful.

Table 24: Owner-managers and the usefulness of financial reports

Financial report	***N***	**Responses (% of total respondents)**					**Mean**
		Not useful				**Very useful**	
		1	**2**	**3**	**4**	**5**	
Balance sheet	226	6.20	11.90	16.40	36.70	28.80	3.70
Profit and loss statement	227	0.90	0.90	4.80	26.40	67.00	4.58
Cash flow statement	221	17.20	10.40	10.40	24.00	38.00	3.55
Changes in equity statement	204	47.10	15.70	15.70	10.30	11.30	2.23
Notes to the financial statements	203	38.40	19.70	14.30	16.30	11.30	2.42

The profit and loss statement was deemed to be the most useful report. In contrast, Sian and Roberts (2009) find the cash flow statement to be the most useful financial report, followed by the balance sheet, and the income statement. The most likely reason for the profit and loss statement's popularity with many respondents lies in its usefulness for estimating tax liabilities. This finding accords with the responses given to the question that asked about the purposes for which owner-managers use SME financial information. The majority of owner-managers use them for estimating income tax liabilities. Given this view, it appears that the balance sheet focus of the conceptual framework, used by the IASB, is not appropriate for Sri Lankan SMEs. The cash flow statement was perceived to be second in importance. This relates to managing liquidity, which is essential to the success and survival of a SME (Collis & Jarvis, 2002; McMahon & Stanger, 1995).

Table 25 summarises the responses received from the owner-managers about the usefulness of management information for their decision making. The majority of owner-managers used budgets, management accounts, and bank reconciliations for making their business decisions. This confirms the usefulness of cash flow information (highlighted in Table 24) - 52% use bank reconciliation statements for their decision making.

Table 25: Owner-managers and the usefulness of management information

Type of management information	***No***	**Responses (% of total respondents)**					**Mean**
		Not useful				**Very useful**	
		1	**2**	**3**	**4**	**5**	
Management accounts	229	9.20	12.70	9.20	40.20	28.80	3.67
Bank reconciliation	227	8.40	13.20	26.40	37.90	14.10	3.36
Budgets	221	5.00	5.00	19.90	38.50	31.70	3.87
Variance analysis	224	28.60	26.80	21.90	13.80	8.90	2.48
Aging reports of debtor balance	223	13.90	20.20	19.70	30.90	15.20	3.13
Financial ratio analysis	197	29.90	32.00	17.30	14.20	6.60	2.36

8.5 Users and their information needs with regard to the size of SMEs

Non-parametric test such as the chi-square test, Mann-Whitney *U* test, and Kruskal-Wallis test were employed to identify any significant differences between entities and the users and uses of SME financial information. The chi-square test was performed when the data were nominal and the Mann-Whitney *U* test was used to test the difference between two groups of respondents (SME accountants and, SME owner-managers). The Kruskal-Wallis test was also used to compare three different sized entities, when the data were either ordinal or interval (Bertrand & Kramarz, 2002; Pallant, 2010).

Table 26 shows users of SME financial information in relation to entity size. The majority of the responding entities (more than 50%) from the 5-15 employee category identified owner-managers and banks as main users of financial information whereas the majority of respondents from the 16-39 employee category identified owner-managers, banks, and the Department of Inland Revenue as main users of financial information. Large SMEs (category 40-99) identified owner-managers, banks, Inland Revenue Department, and government institutions as main user of financial information.

Therefore, it is reasonable to propose that the main users of SME financial information vary according to entity size. Other researchers do not test this proposition. A chi-square test indicated that the perceptions of non-manager owners, other managers, employees, bank/financial institutions, Department of Inland Revenue, government institutions, and suppliers/creditors as main users of SME financial information vary with entity size.

Table 26: Entity size and the main users of SME financial information.

Users of SME financial information		Number of employees 5-15 (*n*=127)	16-39 (*n*=93)	40-99 (*n*=103)	All (*N*=323)	*χ2*	*df*	*p*
		%	%	%	%			
Owner-managers	Yes No	91.30 8.70	93.50 6.50	98.10 1.90	94.10 5.90	4.72	2	.095
Non-manager owners	Yes No	11.80 88.20	7.50 92.50	28.20 71.80	15.80 84.20	18.13	2	.000*
Other managers/ directors of the organisation	Yes No	8.70 91.30	11.80 88.20	41.70 58.30	20.10 79.90	44.33	2	.000*
Employees	Yes No	48.80 51.20	19.40 80.60	14.6 85.40	29.40 70.60	38.51	2	.000*
Bank/financial institutions	Yes No	63.80 36.20	66.70 33.30	82.50 17.50	70.60 29.40	10.59	2	.005*
Inland Revenue Department	Yes No	42.50 57.50	64.50 35.50	80.60 19.40	61.00 39.00	35.32	2	.000*
Government institutions	Yes No	46.50 53.50	23.70 76.30	52.40 47.60	41.80 58.20	18.50	2	.000*
Major suppliers/creditors	Yes No	30.70 69.30	20.40 79.60	15.50 84.50	22.90 77.10	7.87	2	.020**
Major customers	Yes No	16.50 83.50	9.70 90.30	6.80 93.20	11.50 88.50	5.73	2	.057

*The difference is significant at the 0.01 level ($p < 0.01$).
** The difference is significant at the 0.05 level ($p<0.05$).

Table 27 shows the different purposes for which SME financial information is used by owner-managers in relation to the three different firm size categories. More than 50% of owner-managers in the 5-15 employee category indicated that they used SME financial information to make marketing and pricing decisions, capital investment decisions, and planning decisions. Deciding income tax liabilities was not identified as a purpose of using financial information. This finding is consistent with the responses given to the question which asked about the main financial information users, because the majority of owner-managers in the category of 5-15 employees did not identify Inland Revenue Department as one of the main users of SME financial information.

Table 27: Entity size and SME owner-managers use SME financial information.

Purpose of using SME financial information		**Number of employees**			**All (*N*=231)**	$\chi2$	***df***	***p***
		5-15 (*n*=111)	**16-39 (*n*=78)**	**40-99 (*n*=42)**				
		%	**%**	**%**	**%**			
Deciding managers'/ directors' pay/bonuses/dividends	Yes No	36.00 64.00	61.50 38.50	61.90 38.10	49.40 50.60	15.16	2	.001*
Marketing and pricing decisions	Yes No	69.40 30.60	71.80 28.20	35.70 64.30	64.10 35.90	18.05	2	.000*
Capital investment decisions	Yes No	58.60 41.40	42.30 57.70	45.20 54.80	50.60 49.40	5.44	2	.066
Estimating income tax liabilities	Yes No	44.10 55.90	80.80 19.20	85.70 14.30	64.10 35.90	37.14	2	.000*
Planning (Short/long-term)	Yes No	68.50 31.50	60.30 39.70	66.70 33.30	65.40 34.60	1.40	2	.496
Deciding employees' pay and bonuses	Yes No	49.50 50.50	70.50 29.50	47.60 52.40	56.30 43.70	9.745	2	.008*
Comparing performances with targets	Yes No	32.40 67.60	47.40 52.60	78.60 21.40	45.90 54.10	26.24	2	.000*
Comparing performances with previous periods	Yes No	34.20 65.80	62.80 37.20	81.00 19.00	52.40 47.60	31.81	2	.000*
*The difference is significant at the 0.01 level ($p < 0.01$).								

More than 50% of owner-managers from medium sized SMEs (category of 16-39) used financial information for the purposes of: estimating income tax liabilities; taking marketing and pricing decisions; deciding employees' pay and bonuses; comparing performances with previous periods; Deciding managers'/directors' pay/bonuses/dividends; and, when taking short-/long-term planning decisions. The majority of owner-managers from larger SMEs (the employee category of 40 -99) indicated that they used financial information for: estimating income tax liabilities; comparing performances with previous periods; comparing performances with targets; taking short-/long-term planning decisions; and, when deciding directors' pay/bonuses/dividends. As shown in the Table 27, the chi-square test results revealed a statistically significant difference among entities in terms of their use of all the forms of the listed purposes, with the exception of using it for capital investment and planning decisions.

Table 28 : Entity size and analysis of the usefulness of financial reports.

Financial report	**Number of employees**								
	5-15			**16-39**			**40-99**		
	n	**Mean**	***SD***	***n***	**Mean**	***SD***	***n***	**Mean**	***SD***
Balance sheet	107	3.36	1.33	78	4.19	0.78	41	3.63	1.14
Profit and loss statement	107	4.68	0.74	78	4.59	0.60	42	4.29	0.77
Cash flow statement	104	3.32	1.57	76	3.45	1.51	41	4.34	1.02
Changes in equity statement	101	1.68	1.10	72	2.63	1.47	31	3.10	1.54
Notes to the financial statements	100	1.59	0.93	72	3.15	1.34	31	3.42	1.39
Note: Differences in total number of samples were caused by missing data.									

Table 28 summarises responses on the usefulness of financial reports received from owner-managers in relation to the three different firm size categories. The three most useful financial reports for both small and medium size entities are: the profit and loss statement; balance sheet; and, the cash flow statement. However, their order of importance differs for larger SMEs. Owner-managers from large SMEs perceive the cash flow statement to be the most useful financial report, followed by the profit and loss statement, and the balance sheet. Notes to the financial statements were also found more useful by the owner-managers of large SMEs than by respondents from the other two categories.

A Kruskal-Wallis test revealed that there was a significant difference between entity size and the usefulness of the balance sheet (χ^2=18.95, *df*=2, *p*=.000); the profit and loss statement (χ^2=15.17, *df*=2, *p*=.001); the cash flow statement (χ^2=13.69, *df*=2, *p*=.001); the changes in equity statement (χ^2=31.76, *df*=2, *p*=.000); and, the notes to the financial statements (χ^2=68.50, *df*=2, *p*=.000) for business decisions. A Mann-Whitney *U* test revealed that there was a statistically significant difference between SME owner-managers and accountants with regard to the usefulness of the balance sheet (Mann-Whitney *U* = 7110.50, Z= -4.39, *p*=.000); the cash flow statement (Mann-Whitney *U* = 7731.50, Z= -3.24, *p*=.001); the changes in equity statement (Mann-Whitney *U* = 4940.00, Z= -6.22, *p*=.000); and the notes to the financial statements (Mann-Whitney *U* = 4593.50, Z= -6.43, *p*=.000). A higher proportion of accountants perceived these reports to be more useful than SME owner-managers. The perceived usefulness of the profit and loss account was the most similar for both groups of respondents.

Table 29 summarises responses received from owner-managers for all three size categories on the usefulness of management information. The owner-managers of small and medium sized SMEs perceived budgets as the most useful management information, whereas owner-managers of large SMEs perceived management accounts as the most useful management information.

Table 29 : Entity size and analysis of usefulness of management information.

Type of management information	**Number of employees**								
	5-15			**16-39**			**40-99**		
	N	**Mean**	***SD***	***N***	**Mean**	***SD***	***N***	**Mean**	***SD***
Management accounts	110	3.25	1.37	77	3.84	1.00	42	4.43	0.99
Bank reconciliation	110	2.85	1.04	76	3.83	0.99	41	3.88	1.03
Budgets	106	3.58	1.10	73	4.12	0.99	42	4.14	1.00
Variance analysis	109	1.97	1.04	74	2.76	1.26	41	3.32	1.33
Aging reports of debtor balance	107	2.66	1.34	75	3.65	1.02	41	3.41	1.18
Financial ratio analysis	95	1.65	0.70	66	2.79	1.25	36	3.42	1.20
Note: Differences in total number of samples were caused by missing data.									

Further analysis using a Kruskal-Wallis test was performed to determine whether there was a significant difference between the size of an entity and the usefulness of management information. This analysis revealed a significant difference between entity size and the usefulness of management accounts (χ^2=31.84, *df*=2, *p*=.000); bank reconciliation (χ^2=48.25, *df*=2, *p*=.000); budgets (χ^2=17.21, *df*=2, *p*=.000); variance analysis (χ^2=36.08, *df*=2, *p*=.000); aging reports of debtor balances (χ^2 =27.19, *df*=2, *p*=.000); and, financial ratio analysis (χ^2=62.39, *df*=2, *p*=.000). Owner-managers from large SMEs perceive all categories of management information as more useful than owner-managers from small and medium sized entities.

In addition, a Mann-Whitney *U* test showed a statistically significant difference among SME owner-managers and accountants with regard to the usefulness of the following for business decisions: management accounts (Mann-Whitney *U* = 8611, Z= -2.27, *p*=.023); Bank reconciliation (Mann-Whitney *U* = 6666, Z= -5.02, *p*=.000); variance analysis (Mann-Whitney *U* = 5599, Z= -5.84, *p*=.000); aging reports of debtor balance (Mann-Whitney *U* = 6897.50, Z= -3.93, *p*=.000); and, financial ratio analysis (Mann-Whitney *U* = 4398.50, Z= -5.41, *p*=.000). A higher proportion of accountants than of SME owner-managers perceive these reports to be useful. The perceived usefulness of budgets had the greatest similarity across both groups of respondents.

8.6. International exposure of SMEs

To investigate the IASB's claim for the need for internationally comparable accounting information for SMEs, the international exposure of Sri Lankan SMEs was examined. The results for international exposure of SMEs are shown in Table 30.

Table 30: International exposure of SMEs

Foreign activity	**Number of employees**			
	5-15 %	**16-39 %**	**40-99 %**	**All %**
Foreign exports	**(*n*=127)**	**(*n*=89)**	**(*n*=98)**	**(*N*=314)**
No relevance (1)	96.90	69.70	48.00	73.90
Low relevance (2)	0.80	11.20	7.10	5.70
Moderate relevance (3)	0.00	7.90	12.20	6.10
High relevance (4)	0.80	2.20	15.30	5.70
Very high relevance (5)	1.60	9.00	17.30	8.60
Foreign imports	**(*n*=127)**	**(*n*=93)**	**(*n*=102)**	**(*N* =322)**
No relevance (1)	89.00	57.00	36.30	63.00
Low relevance (2)	2.40	8.60	1.00	3.70
Moderate relevance (3)	4.70	17.20	16.70	12.10
High relevance (4)	2.40	7.30	23.50	10.60
Very high relevance (5)	1.60	9.70	22.50	10.60
Foreign ownership	**(*n*=122)**	**(*n*=89)**	**(*n*=91)**	**(*N* =305)**
No relevance (1)	97.60	86.50	74.70	87.50
Low relevance (2)	0.80	2.20	2.20	1.60
Moderate relevance (3)	0.00	3.40	7.70	3.30
High relevance (4)	0.80	3.40	12.10	4.90
Very high relevance (5)	0.80	4.50	3.30	2.60
Borrowing abroad	**(*n*=123)**	**(*n*=89)**	**(*n*=90)**	**(*N* =302)**
No relevance (1)	98.40	88.80	78.90	89.70
Low relevance (2)	0.00	2.20	6.70	2.60
Moderate relevance (3)	0.80	4.50	6.70	3.60
High relevance (4)	0.80	0.00	4.40	1.70
Very high relevance (5)	0.00	4.50	3.30	2.30
Note: Differences in total number of samples were caused by missing data.				

The responses to the questionnaire reveal that for the majority of surveyed entities international activities are of minor importance. The most relevant international activity for Sri Lankan SMEs was foreign imports as indicated by 21% of respondents. Foreign financing is not important to Sri Lankan SMEs. Comparatively, large SMEs overall reveal more cross-border activities than small entities. The majority of the responding entities do not see any need to provide internationally comparable accounting information (see Table 31). The probable reason for this is that the majority of Sri Lankan SMEs are purely domestically based. Therefore, results suggest that in contrast to the IASB's perception, Sri Lankan SMEs do not accept the need to provide internationally comparable accounting information.

Table 31: Need to provide internationally comparable accounting information

Response	**Number of employee**			**All (*N*=322)**
	5-15 (*n*=127)	**16-39 (*n*=92)**	**40-99 (*n*=103)**	
	%	**%**	**%**	**%**
No need (1)	92.10	89.10	67.00	83.20
Little need (2)	7.10	7.60	13.60	9.30
Partial need (3)	0.00	2.20	9.70	3.70
High need (4)	0.00	0.00	5.80	1.90
Very high need (5)	0.80	1.10	3.90	1.90

As the analysis in Table 31 indicates, large SMEs expressed a higher need to provide internationally comparable accounting information than small SMEs. It appears that an entity's size as well as its level of international activities have an impact on an entity's need to provide internationally comparable accounting information. This finding is consistent with the study conducted by Eierle and Haller (2009) in Germany. However, the German SMEs had considerably more cross-border activities (foreign exports and foreign imports) than SMEs in Sri Lanka. Despite the importance of exports and imports reported in their study, about half of the responding entities do not see any need to provide internationally comparable financial accounting data.

8.7 Relevance of the accounting topics included in the *SLFRS for SMEs* to Sri Lankan SMEs

The IASB claims it considered addressing only those issues and transactions that are of general relevance for SMEs in order to restrict the volume and complexity of the *IFRS for SMEs* (International Accounting Standards Board, 2009a). To ascertain the relevance of specific accounting-related topics contained in the *SLFRS for SMEs* (Sri Lanka did no modifications to the accounting standard *IFRS for SMEs* when adopting it as *SLFRS for SMEs)*, respondents were asked to identify how frequently particular transactions occurred in their businesses. Table 32 summarises the responses received with regard to specific accounting-related topics.

Table 32: Frequency of specific transactions occur in SMEs

Accounting topic	**Number of employees**			**All**
	5-15	**16-39**	**40-99**	
Investment in non-listed companies	**(*n*=126)**	**(*n*=84)**	**(*n*=88)**	***(N*=298)**
Never (1)	61.9%	65.5%	52.3%	60.1%
Seldom (2)	23.8%	14.3%	20.5%	20.1%
Sometimes (3)	13.5%	16.7%	21.6%	16.8%
Often (4)	0.8%	1.2%	3.4%	1.7%
Very often (5)	0.0%	2.4%	2.3%	1.3%
Investment in listed companies	**(*n*=126)**	**(*n*=83)**	**(*n*=88)**	**(*N*=297)**
Never (1)	50.8%	63.9%	56.8%	56.2%
Seldom (2)	33.3%	16.9%	17.0%	23.9%
Sometimes (3)	15.1%	10.8%	18.2%	14.8%
Often (4)	0.0%	4.8%	5.7%	3.0%
Very often (5)	0.8%	3.6%	2.3%	2.0%
Joint venture	**(*n*=126)**	**(*n*=82)**	**(*n*=84)**	**(*N*=292)**
Never (1)	45.2%	54.9%	58.3%	51.7%
Seldom (2)	37.3%	17.1%	13.1%	24.7%
Sometimes (3)	16.7%	18.3%	15.5%	16.8%
Often (4)	0.8%	7.3%	11.9%	5.8%
Very often (5)	0.0%	2.4%	1.2%	1.0%

Table: 32 continues

Accounting topic	Number of employees			All
	5-15	16-39	40-99	
Investment property	**(*n*=124)**	**(*n*=83)**	**(*n*=89)**	**(*N*=296)**
Never (1)	14.5%	26.5%	42.7%	26.4%
Seldom (2)	26.6%	24.1%	13.5%	22.0%
Sometimes (3)	47.6%	28.9%	25.8%	35.8%
Often (4)	8.9%	16.9%	11.2%	11.8%
Very often (5)	2.4%	3.6%	6.7%	4.1%
Construction contracts	**(*n*=124)**	**(*n*=83)**	**(*n*=89)**	**(*N*=296)**
Never (1)	32.5%	46.3%	59.3%	44.2%
Seldom (2)	46.8%	18.3%	14.0%	29.3%
Sometimes (3)	17.5%	23.2%	15.1%	18.4%
Often (4)	2.4%	7.3%	10.5%	6.1%
Very often (5)	0.8%	4.9%	1.2%	2.0%
Research and Development projects within the company	**(*n*=124)**	**(*n*=83)**	**(*n*=85)**	**(*N*=292)**
Never (1)	35.5%	43.4%	49.4%	41.8%
Seldom (2)	40.3%	20.5%	14.1%	27.1%
Sometimes (3)	12.1%	20.5%	18.8%	16.4%
Often (4)	10.5%	13.3%	14.1%	12.3%
Very often (5)	1.6%	2.4%	3.5%	2.4%
Government grants	**(*n*=125)**	**(*n*=82)**	**(*n*=85)**	**(*N*=292)**
Never (1)	41.6%	70.7%	70.6%	58.2%
Seldom (2)	53.6%	17.1%	14.1%	31.8%
Sometimes (3)	4.8%	7.3%	5.9%	5.8%
Often (4)	0.0%	2.4%	9.4%	3.4%
Very often (5)	0.0%	2.4%	0.0%	0.7%
Purchase/sale of goods and services in foreign currencies	**(*n*=124)**	**(*n*=83)**	**(*n*=90)**	**(*N*=297)**
Never (1)	77.4%	63.9%	37.8%	61.6%
Seldom (2)	14.5%	7.2%	10.0%	11.1%
Sometimes (3)	1.6%	12.0%	22.2%	10.8%
Often (4)	4.0%	8.4%	18.9%	9.8%
Very often (5)	2.4%	8.4%	11.1%	6.7%

Table: 32 continues

Accounting topic	Number of employees			All
	5-15	16-39	40-99	
Foreign exchange rate loans and borrowings	**(*n*=124)**	**(*n*=83)**	**(*n*=86)**	**(*N*=293)**
Never (1)	91.1%	80.7%	61.6%	79.5%
Seldom (2)	5.6%	3.6%	12.8%	7.2%
Sometimes (3)	2.4%	7.2%	11.6%	6.5%
Often (4)	0.8%	4.8%	8.1%	4.1%
Very often (5)	0.0%	3.6%	5.8%	2.7%
Foreign exchange risk resulting from a customer order or a supplier	**(*n*=119)**	**(*n*=79)**	**(*n*=87)**	**(*N*=285)**
Never (1)	68.9%	64.6%	56.3%	63.9%
Seldom (2)	15.1%	12.7%	10.3%	13.0%
Sometimes (3)	11.8%	10.1%	11.5%	11.2%
Often (4)	4.2%	6.3%	12.6%	7.4%
Very often (5)	0.0%	6.3%	9.2%	4.6%
Note: Differences in total number of samples were caused by missing data.				

The results suggest the majority of the entities surveyed do not have any engagement with most of the accounting- related topics, shown in Table 32. Generally, the accounting issues that are of some relevance for SMEs are: purchase/sale of goods and services in foreign currencies: and investment property. The purchase/sale of goods and services in foreign currencies occurred often or very often for 16.50% of the participating entities, and 15.90% of the entities encountered investment property often or very often.

The accounting topics that were more relevant for large SMEs were the purchase/sale of goods and services in foreign currencies, and foreign exchange risk resulting from a customer order or a supplier. Investment property and the purchase/sale of goods and services in foreign currencies were the more relevant accounting topics for medium SMEs. Research and development projects within the company, and investment property were seen to be of greater relevance for small SMEs.

As might be expected, medium and large SMEs encountered government grants, purchase/sale of goods and services in foreign currencies, foreign exchange rate loans and borrowings, and foreign exchange risk resulting from a customer order or a supplier more often than small SMEs. This result agreed with the responses to the question of the international exposure of SMEs, in which the large SMEs were engaged in more cross-border activities than the small SMEs were.

In summary, the results from analysis of the data reveal that most of the participating SMEs did not engage in complex transactions, most probably because SMEs are more likely to be focusing on survival than on growth and profit maximisation. Moreover, it appears that Sri Lankan SMEs do not invest directly in other businesses and limited to a single product-line or business purpose and domestically based. Therefore, the IASB's efforts to omit topics that were considered to be irrelevant, or of little relevance, to SMEs do not fully reflective of the financial reporting needs of SMEs in Sri Lanka. Similar results were obtained by Aboagye-Otchere and Agbeibor (2012) who find that topics covered by the *IFRS for SMEs* are irrelevant to SMEs in Ghana.

8.8 Adoption of the *SLFRS for SMEs*

To investigate adoption status of *SLFRS for SMEs*, respondents were asked to indicate if they would adopt the standard. Figure 10 shows the adoption status of the responding entities. More than 57% of the surveyed entities do not adopt or implement the *SLFRS for SMEs*. As might be expected, large SMEs were more likely than other two categories to use the *SLFRS for SMEs.* The limited number of international transactions by SMEs and the accounting topics in the *SLFRS for SMEs* are not relevance to them provide possible reasons for the rejection of the *SLFRS for SMEs* by the majority of SMEs in Sri Lanka.

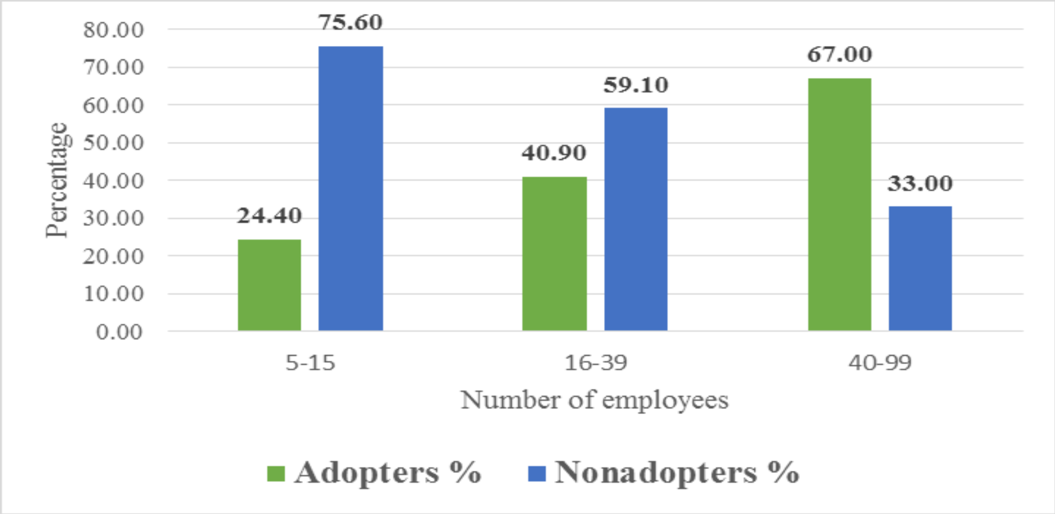

Figure 10 : Adoption status of *SLFRS for SMEs*

8.9 Costs and benefits of adopting the *SLFRS for SMEs*

The IASB assert that the *IFRS for SMEs* is based on the full *IFRS* with modifications to reflect the needs of users of SMEs' financial statements and cost-benefit considerations (International Accounting Standards Board, 2009a). To identify the costs and benefits associated with the provision of information and to ascertain how the respondents perceive those costs and benefits, those who adopted the *SLFRS for SMEs* were asked additional questions. Therefore, subsequent analysis on costs and benefits of *SLFRS for SMEs* was based on the responses given by the adopting SMEs.

8.9.1 Costs of using the *SLFRS for SMEs*

Six elements involved in the costs of the preparation and provision of financial statements identified in the literature were presented to the survey respondents. They were asked to identify costs relevant to their entities and all those who had adopted the accounting standard *SLFRS for SMEs* were surveyed about the significance of the standard. The respondents were asked to rate the significance of each cost element using a 5-point Likert-type scale where 1 indicated not significant and 5 indicated very significant. The results are summarised in Table 33.

Table 33 : Significance of costs of preparing *SLFRS for SMEs* financial statements

Type of cost	***N***	**Responses (% of total respondents)**					**Mean**
		Not significant			**Very significant**		
		1	**2**	**3**	**4**	**5**	
Costs of training accounting and IT staff	136	5.10	16.20	39.97	29.40	9.60	3.22
Costs of hiring qualified accounting staff	135	3.70	12.60	42.20	34.10	7.40	3.29
Costs of obtaining external technical advice and payments to accounting firms	134	3.70	11.20	21.60	56.00	7.50	3.52
Costs of changing accounting software and systems	128	5.50	12.50	39.80	29.70	12.50	3.31
Costs of information acquisition	128	6.30	10.20	25.00	50.80	7.80	3.44
Costs of taking tax advice	137	5.10	14.60	38.00	28.50	13.90	3.31

As can be seen from Table 33, more than half of the responding entities indicated that the costs of obtaining external technical advice from and making payments to accounting firms, and the costs of information acquisition were the most significant (indeed very significant) costs incurred when preparing financial statements in accordance with *SLFRS for SMEs*. This finding most probably reflects the fact that the majority of the entities surveyed use external accountants to prepare and audit their financial statements (Carsberg et al., 1985; Kitching et al., 2011; Marriott & Marriott, 2000; Professional Oversight Board for Accountancy, 2006). This finding further confirms that the internal accounting staff employed in these SMEs are not competent to implement the standard when preparing financial statements (Halbouni, 2005).

Further analysis on the views of the SME owner-managers and the accountants was performed to assess whether there is a significant difference between these groups. A Mann-Whitney *U* test suggested that there was a statistically significant difference in the views of the SME owner-managers and accountants on the cost of taking tax advice (Mann-Whitney U = 1875, Z= -1.97, p=.049). The accountants, however, placed more importance on the cost of taking tax advice than the SME owner-managers.

8.9.2 Benefits of preparing financial statements in accordance with *SLFRS for SMEs*

The respondents were asked about the benefits they might gain from the preparation of financial statements in accordance with *SLFRS for SMEs*. Seven statements regarding the benefits of *SLFRS for SMEs* were presented to the respondents. These were the benefits identified in the literature and by the International Accounting Standards Board (IASB). Table 34 presents the results of this analysis.

Table 34: Benefits from *SLFRS for SMEs* compliant financial statements

Type of benefit	***No***	**Responses (% of total respondents)**					**Mean**
		Not beneficial			**Very beneficial**		
		1	**2**	**3**	**4**	**5**	
To compare financial statements	138	4.30	10.10	25.40	39.10	21.00	3.62
To fulfil tax declaration	138	4.30	2.20	18.10	52.90	22.50	3.87
To provide easy access to finance	131	-	3.10	19.80	51.90	25.20	3.99
To serve administrative/statistical purposes of the government	131	3.80	9.90	32.80	38.20	15.30	3.51
To support loan applications	125	4.80	5.60	18.40	40.80	30.40	3.86
To tender for business projects/contracts	125	5.60	13.60	24.80	36.80	19.20	3.50
To meet your internal management needs	132	6.80	4.50	22.00	38.60	28.00	3.77

The main benefit that the respondents perceive is easy access to finance. This benefit was selected by more than 77% of the respondents. It was followed by fulfilling tax declaration (75.40%), and supporting loan applications (71.20%). Respondents from large entities were more likely to perceive these benefits than the respondents from medium and small entities. Respondents from medium entities were also more likely to than the respondents from small entities to perceive these benefits. According to IASB, one of the objectives of *IFRS for SMEs* is to improve the comparability of financial information of SMEs. However, this benefit was placed fourth in importance by Sri Lankan SMEs.

Mann-Whitney *U* tests was performed to test the difference between the views of the SME owner-managers and those of accountants. Table 35 shows that there was a significant difference between the views of the two groups in the following areas:

the benefits of being able to compare financial statements; to fulfil tax declaration; to serve administrative/statistical purposes of the government; to tender for business projects/contracts; and, to meet internal management needs.

Table 35: Perceptions of SME owner-managers and accountants on the benefits

Benefits	Position	*N*	Mean Rank	Sum of Ranks	Mann-Whitney	*Z*	*p*
To compare financial statements	Owners	77	54.47	4194.00	1191.00	-5.19	0.000*
	Accountants	61	88.48	5397.00			
To fulfil tax declaration	Owners	77	62.06	4779.00	1776.00	-2.69	0.007*
	Accountants	61	78.89	4812.00			
To provide easy access to finance	Owners	75	63.64	4773.00	1923.00	-0.90	0.368
	Accountants	56	69.16	3873.00			
To serve administrative/statistical purposes of the government	Owners	76	56.53	4296.50	1370.50	-3.53	0.000*
	Accountants	55	79.08	4349.50			
To support loan applications	Owners	75	62.95	4721.00	1871.00	-0.02	0.983
	Accountants	50	63.08	3154.00			
To tender for business projects/contracts	Owners	75	57.97	4348.00	1498.00	-1.98	0.048**
	Accountants	50	70.54	3527.00			
To meet your internal management needs	Owners	76	52.93	4023.00	1097.00	-4.98	0.000*
	Accountants	56	84.91	4755.00			

Note:
*The difference is significant at the 0.01 level ($p < 0.01$).
** The difference is significant at the 0.05 level ($p<0.05$).
Differences in total number of samples were caused by missing data.

In all cases, accountants tend to perceive the items as more beneficial than the owner-managers of the SMEs. Although the difference between the SME owner-managers and the accountants on the benefits of providing easy access to finance and supporting loan applications are not significant, it can be inferred from the mean ranks that there is a difference in the perceptions of these two groups. It would appear that accountants tend to place more importance on these benefits than do owner-managers.

8.9.3 Relationship between the costs and benefits

Apart from the identification of costs and benefits, the study also attempts to examine the respondents' perception of the relationship between the costs and benefits of preparing financial statements in accordance with *SLFRS for SMEs*. Respondents were asked how they perceived the relationship between the costs and benefits producing compliant financial statements. Four options were presented to the respondents and Table 36 presents the results.

Table 36 : Relationship between the costs and the benefits

Cost-benefit relationship	**Number of employees**						**All (*N*=136)**	
	5-15 (*n*=30)		**16-39 (*n*=38)**		**40-99 (*n*=68)**			
	n	**%**	***n***	**%**	***n***	**%**	***n***	**%**
The benefits exceeds the costs	5	16.70	7	18.40	8	11.80	20	14.70
The benefit fit with the costs	12	40.00	12	31.60	14	20.60	38	27.90
The costs exceeds the benefit	13	43.30	17	44.70	41	60.30	71	52.20
No idea	0	0.00	2	5.30	5	7.40	7	5.10
	30	100.00	38	100.00	68	100.00	136	100.00

The majority of the respondents (52.20%) believe the costs exceed the benefits. Similar results were obtained in the study conducted by Chand et al. (2015). The majority of respondents in their survey strongly agreed with the statement that the costs of complying with *IFRS for SMEs* are far greater than the corresponding benefits. It appears that the *SLFRS for SMEs* has not succeeded in reducing financial reporting costs associated with preparing financial statements of SMEs in Sri Lanka. Thus, IASB has failed to balance benefits and costs as they claimed for the *IFRS for SMEs*. Since the *IFRS for SMEs* was developed based on the full *IFRS* using the top-down approach, it seems to be a challenge for Sri Lankan SMEs to implement.

8.9.4 Additional exemptions for the *SLFRS for SMEs*

It is apparent from the responses shown in Table 37 that the respondents generally know virtually nothing about the additional exemptions to *SLFRS for SMEs*. This finding may have been shaped by their lack of knowledge of *SLFRS for SMEs* and, thus, their inability to comment on it. However, nearly 46% of respondents agreed with a need for additional exemptions to *SLFRS for SMEs*. This finding further confirms the complexity of the *SLFRS for SMEs* for Sri Lankan SMEs.

Table 37 : Perception on the requirement to provide additional exemptions to the *SLFRS for SMEs*

Response	**Number of employees**						**All (*N*=133)**	
	5-15 (*n*=28)		**16-39 (*n*=38)**		**40-99 (*n*=67)**			
	n	**%**	***n***	**%**	***n***	**%**	***n***	**%**
Yes	11	39.30	20	52.60	30	44.80	61	45.90
No	1	3.60	2	5.30	4	6.00	7	5.30
No idea	16	57.10	16	42.10	33	49.30	65	48.90
	28	100.00	38	100.00	67	100.00	133	100.00

8.10 The new accounting standard: SLFRS for Smaller Entities

Sri Lanka developed a new accounting standard for SMEs known as Sri Lanka Accounting Standards for Smaller Entities (SLFRS for Smaller Entities). This became operative for financial statements covering periods beginning on or after 01 January 2016. Table 38 illustrates the respondents' awareness of the *SLFRS for Smaller Entities*. All of the respondents who did not adopt the accounting standard *SLFRS for SMEs* were requested to indicate their awareness of the new standard. Only 32 per cent of the respondents claim to be aware of this new accounting standards for 'smaller entities' in Sri Lanka.

Table 38 : SME size and awareness of the *SLFRS for Smaller Entities*

Category	**Employee number**							
	5-15 (n=95)		**16-39 (n=54)**		**40-99 (n=32)**		**All (N=181)**	
	n	**%**	**n**	**%**	**n**	**%**	**N**	**%**
Yes	31	32.60	14	25.90	13	40.60	58	32.00
No	64	67.40	40	74.10	19	59.40	123	68.00
	95	100.00	54	100.00	32	100.00	181	100.00

Respondents were asked whether they would opt to implement the *SLFRS for Smaller Entities*. Table 39 indicates the majority of the respondents (54%) are undecided, while 22.2% per cent of the respondents say they will take professional advice before deciding. The uncertainty might be caused by their lack of knowledge and lack of awareness of this new accounting standard.

Table 39 : SME size and Analysis of potential implementation of the SLFRS for Smaller Entities

Category	**Employee number**						**All N=176)**	
	5-15 (n=91)		**16-39 (n=53)**		**40-99 (n=32)**			
	n	**%**	**n**	**%**	**n**	**%**	**N**	**%**
Yes	6	6.60	5	9.40	5	15.60	16	9.10
No	13	14.30	7	13.20	6	18.80	26	14.80
Undecided	55	60.40	28	52.80	12	37.50	95	54.00
Take professional advice	17	18.70	13	24.50	9	28.10	39	22.20

8.11 Summary

This chapter analysed the quantitative data collected by questionnaire surveys. It presented information on the characteristics of Sri Lankan SMEs, of their size, legal form, age, and industry. It also provided insights into the ownership, management, and accounting function of responding SMEs. The results reveal most of the responding entities were owner managed. From a theoretical perspective, this finding suggests there is little scope for an agency relationships between owner and managers. This has important implications for the relevance of the conceptual framework for SMEs, since it is based on stewardship and the needs of external investors.

The majority of the small SMEs used manual accounting systems to keep accounting records, whereas the majority of the large SMEs used computerised systems to keep their accounting records. A lack of competent internal accounting staff has resulted in many SMEs turning to external accountants to obtain accounting services such as the preparation of financial statements (63.50%) and taxation services (57%).

The results of the quantitative data tend to support the findings in the literature that indicate the number of users of the financial information of SMEs is limited. The perceived main users of SME financial information were owner-managers, bank and financial institutions, and tax authorities. However, a considerable number of respondents (nearly 42%) indicated that government institutions were one of the users of SME financial information.

Many respondents use their SME's financial information for management and other purposes. The top three purposes for which owner-managers use SME financial information are: planning purposes (65.40%); estimating income tax liabilities (64.10%); and, making marketing and pricing decisions (64.10%). The most useful financial statement for decision making was the profit and loss statement, followed by the balance sheet, and cash flow statement. Apart from financial information, the majority of the respondents used management accounting information in their decision making.

The majority of the small SME responding entities identify owner-managers and banks as the primary users of financial information. By contrast, the majority of respondents from the 16-39 employees category identified owner-managers, banks, and the Department of Inland Revenue as the main users of financial information. Large SMEs (40-99 employees) identify owner-managers, banks, the Department of Inland Revenue, and government institutions as the main users of SME financial information. Therefore, as can be seen from the results, the perceived main users of SME financial information vary according to entity size.

More than 50% of owner-managers in the 5-15 employee category indicated that they used SME financial information to make marketing and pricing decisions; capital investment decisions; and, planning decisions. More than 50% of the owner-managers in the medium SMEs (16-39 employees) use financial information for the purposes of: estimating income tax liabilities; taking marketing and pricing decisions; deciding employees' pay and bonuses; comparing performances with previous periods; deciding managers'/directors' pay/bonuses/dividends; and, taking planning (short/long-term) decisions. The majority of the owner-managers from large SMEs (40 -99 employees) indicate they use financial information for: estimating income tax liabilities; comparing performances with previous periods; comparing performances with targets; taking planning (short/long term) decisions; and, deciding directors' pay/bonuses/dividends. The most useful financial report for both small and medium SMEs is the profit and loss statement. Owner-managers from large SMEs ranked the cash flow statement as the most useful financial report.

It is found that the all types of international activities were of minor importance to Sri Lankan SMEs. As a consequence, these entities did not see any need to provide internationally comparable accounting information. Large SMEs are active in more cross-border activities and indicate a higher need to provide internationally comparable accounting information than did the small SMEs.

The results reveal that most of the participating SMEs did not engage in complex transactions. Thus, many of the topics contained in the *SLFRS for SMEs* are not relevant to them. Owing to these reasons, the majority of entities surveyed did not adopt the accounting standard *SLFRS for SMEs*. As might be expected, large SMEs were more likely to adopt *SLFRS for SMEs* than were SMEs in the other two smaller categories.

The costs of obtaining external technical advice from and making payments to accounting firms are the most significant costs incurred when preparing financial statements in accordance with *SLFRS for SMEs*. The main benefit the respondents perceive is easy access to finance. However, the majority of respondents (52.20%) believe the costs of preparing financial statements in accordance with *SLFRS for SMEs* exceed the benefits.

The majority of respondents were not aware about the new accounting standard for smaller entities and they are undecided about implementing it. Test results suggested that there is a significant difference between SME owners and the accountants on the awareness of new accounting standards for SMEs. As it might be expected, most of the accountants were aware of the new accounting standard.

The next chapter describes the results of the qualitative data analysis.

CHAPTER NINE

QUALITATIVE DATA ANALYSIS

9.1 Introduction

This chapter presents and discusses the results from the thematic analysis of qualitative data pertaining to the two research questions of this thesis. The users of SME financial information and the uses to which this information is put are outlined. The need for international comparable accounting information is examined and the adoption process, awareness and knowledge of the *SLFRS for SMEs* is explored. Costs and benefits as viewed by the interview respondents are then revealed. The perceptions of the respondents from the 41 interviews of owner-managers and accountants of SMEs, bank lending officers, income tax officers, and representatives from the standard setter in Sri Lanka and the government institutions are presented in this chapter. Section 9.2 discusses the findings of qualitative data in relation to users of SME financial information. Section 9.3 shares the views on the uses of SME financial information by the three respondent groups (owner-managers, lending officers and income tax officers). Section 9.4 considers the perceptions of respondents on the need for international financial reporting standards for SMEs. Section 9.5 examines the adoption process, awareness and knowledge of *SLFRS for SMEs*. Section 9.6 presents the perception of respondents about the costs and benefits of preparing financial statements in accordance with *SLFRS for SMEs*. Section 9.7 concludes the qualitative data analysis.

9.2 Users of SME financial information

Users of Sri Lankan SME financial information was investigated by obtaining the perception of owner-managers and accountants of SMEs, bank lending officers, income tax officers, and representatives from government institutions and the standard setter in Sri Lanka. In line with prior research, (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Maingot & Zeghal, 2006; Page, 1984), owner-managers in this study agree they use SMEs financial information for their business decisions and thus identify themselves as users of

SME financial information. The following quotes confirm owner-managers are users of SME financial information.

> We are the decision makers of the entity and we want to check on taxation, and cash flow. I make decisions based on financial information (Owner-manager 01).
>
> For decision making I monitor sales and get an update daily. Also, monthly we get a P&L and the financial ledgers as well (Owner-manager 15).
>
> Myself and my wife use financial information of the business. She handles the debtors and creditors ledger and gives a report daily (Owner-manager 16).

As most of the SMEs had a limited number of owners and were owned and managed by family members, non-manager owners were not identified as users of SME financial information. Consistent with the findings of Page (1984), Carsberg et al. (1985), Collis and Jarvis (2000), Sian and Roberts (2009), and Dang-Duc et al. (2006) all owner-managers identify the Inland Revenue Department as one of the main users of their financial information. They say:

> There is no point of preparing these (end of year) financial statements. Just doing these reports to pay taxes to the government (Owner-manager 15).
>
> Main purpose of their (financial statements) preparation is to submit the tax return to the Inland Revenue Department (Owner-manager 06).
>
> Our accounting firm prepares those (financial statements) for regulatory requirements. I mean submit to the income tax department (Owner-manager 08).

These statements indicate that for most owner-managers, financial statements are prepared by their external accounting firms as a 'legal' document to be submitted to fulfil legal requirements, particularly for taxation. Thus, they do not make use of these financial statements for their business decision making. Income tax officers explain that submitting financial statements is a legal requirement for SMEs, and that every SME is required to submit statement of accounts prepared by an approved accountant. Some SMEs are required to submit audited financial statements based on the size of their turnover and/or profits. Income tax officers are one of the users of SME financial information:

> Most often, they (SMEs) give the financial statements as it is a requirement of the return but providing cash flow statement is not a compulsory requirement for SMEs (Income tax officer 01).
>
> Yes, we need SME financial information. As per our law, SMEs who maintain more than Rs250 million turnover have to submit the audited financial statements. Others need to submit financial statements to review their performance but should not be audited (Income tax officer 02).

As Barker and Noonan (1996), Maingot and Zeghal (2006), Rennie and Senkow (2009), and Sian and Roberts (2009) argue banks are also identified as one of the main users of SME financial information by all owner-managers of the study. They have to submit their financial information to banks when they want to use loan facilities. Some owner-managers seem to have developed good relationships with their banks because they had transacted with these banks for a long time. However, they were also required to submit financial information when obtaining loans. Banks are identified as users of SME financial information:

> I applied Rs2.5 million loan from my bank to get the main equipment for my business. Bank asked my financial statements and I submitted financial statements prepared by the external accountant (Owner-manager 03).
>
> We have been dealing with this particular bank for years now from the inception of the business. So, they have a connection with us and our borrowing gets approved within shorter time period. But, whenever the manager or bank staff change, they need to build that understanding from the beginning again. Whenever we go for a financial facility, they have been requesting for our financial details (Owner-manager 06).

Banks as users of SME financial information was also confirmed by the responses from the bank lending officers:

> When financing a SME, the first thing we consider is the nature of the business they are operating in and second, if the business is registered. The third thing we consider is the business volume and the management tools that they are using. Fourth, the management accounts and financial accounts that they are preparing (Bank lending officer 01).

> When giving a loan for a working capital requirement, or a renovation or expansion, we use their financial reports to calculate the gearing and other ratios to evaluate their repayment capacity and the effect that a loan will have on them (Bank lending officer 03).

Two government institutions state they use SME financial information when they administer and approve certain SME fund schemes obtained from international donor agencies such as the Asian Development Bank and the World Bank. Thus, government agencies are users of SME financial information:

> We normally get the loans from donor agencies such as ADB and World Bank and we have not an arm to distribute. So, we give that loan as a sub-loan to the selected banks. Before giving the loans to SMEs, they have to get our approval. When we approve the loans, they have to send the documentation, including financial records, to us. We study the SME financial records at that time (Government institution 01).

> We have a Project Management Unit, which works with ten credit participation institutions. That means ten banks to implement this loan scheme at the interest rate of 8%. The SME can apply for Rs10 million. So in that case we are analysing their case especially for their business plan because to recommend to the banks. So, there is a two-way approach. SMEs can come and lodge their application either here or in the bank. An Operation Level committee established in the Ministry will recommend to the bank to grant the loan. For that purpose, SMEs need to submit their financial information. Why we are doing this is to ensure the loan scheme is reaching the real SMEs not for other purposes (Government institution 02).

Additionally, some owner-managers who registered their businesses under the Board of Investment of Sri Lanka identified that Board and the Sri Lanka Customs as users of their financial information. Owner-managers say it is a regulatory requirement to submit their financial information as Sri Lanka Customs requests turnover and bank details from SMEs when they renew the custom registration.

In order to obtain business permits and government contracts, SMEs are required to submit their financial information to government organisations such as Defence Ministry, and provincial councils. Moreover, owner-managers state they have to provide their financial information to government organisations when they want to get supplies from or sell goods to government organisations. It is a common practise among government institutions to ask for financial information when they transact with SMEs. SMEs provide their financial information to these government organisations to provide assurance they would be able to undertake the particular task or pay for the goods obtained. Government institutions are users of SME financial information:

> The Defence Ministry and provincial council check on our income because they provide the permits (Owner-manager 12).

> When we are getting new business from the government agencies, they need about 3 years of financial information to check our strength (Owner-manager 23).

Non-governmental suppliers and customers are not identified as users of SME financial information by owner-managers. Even SMEs who undertake international transactions do not receive any requests to provide financial information to their foreign suppliers or customers.

> No, they (suppliers and customers) cannot ask for our financial information because we are not a public company. Only thing is we might give an overview of the company and things like that for them to know that they are dealing with a reputed company with good standing but we don’t give financial information (Owner-manager 20).

> I don’t think suppliers want our financial information. In my 16 years, I have sent it to maybe two people (Owner-manager 21).

> No, suppliers do not ask for our financial information. Our suppliers have agents in Sri Lanka who promote us as customers. Each shipment is about Rs7million. When we open a LC, the bank has to be given something. We have to mortgage something to the bank to get the goods (Owner-manager 19).

It appears that suppliers and customers tend to use alternative methods to ensure the credibility of SMEs and thus, they do not request financial information. SME accountants were asked who they consider to be the main users of financial information. Both internal and external users, including owner-managers, banks, government institutions, and the Inland Revenue Department, are identified by the accountants. The perception of the users of SME financial information, by representatives from the standard setting authority of Sri Lanka, is consistent with the perceptions of owner-managers and accountants. Accountants did not identify non-manager owners, suppliers, and customers as users of SME financial information. They comment:

> We do not prepare these financial statements for public purposes, it is for internal users and for some limited external users. We give them to banks when we get loans and Inland Revenue department as it is a regulatory requirement. Other than that, it is only the directors who refer to them. Our suppliers and customers do not request for our financial reports. This is the customer behaviour in the local market a cheaper price and the quality of the products are what matters (Accountant 01).

> When we are called for tenders and quotations from government organisations, we have to submit our financial statements, and the recent months P and L, and cash flow data (Accountant 04).

However, the perceptions of owner-managers and accountants on government institutions as a user of SME financial information is not reflected by respondents from the standard setter.

> Actually, according to my understanding and from information we have gathered from different participants, different people basically, the main users of financial information of SMEs would be the owner itself and mainly the bankers and Inland Revenue authorities. Those are the main users. Therefore, whatever the financial statements they are preparing should be target to their requirements according to my understanding (Standard setter representative 01).

Owner-managers, banks, and the Inland Revenue Department are identified as the main users of SME financial information. This finding is consistent with the findings of previous research into users of SME financial information (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Maingot & Zeghal, 2006; Page, 1984). While the majority of owner-managers and accountants state that banks are important users of SME financial information, this appears not to be so in other developing countries. Dang-Duc et al. (2006) finds only a minority of respondents identified banks as important user of SME financial information.

Certain government institutions are found to be users of SME financial information. The owner-managers reveal they had to provide their financial information to government institutions when they sell to or purchase goods and services from government agencies. Moreover, Ministries in Sri Lanka require SMEs to provide their financial information when they apply for SME loans that are funded by foreign donor agencies such as the World Bank and Asian Development Bank. Ministries administering such loan programmes require SMEs to provide their financial information. This finding contradicts earlier research in developed countries (Collis & Jarvis, 2000; Sian & Roberts, 2009) but is consistent with research from a developing country suggesting that government institutions are a user of SME financial information (Dan-Duc et al., 2006).

Non-manager owners are not important users of SME financial information. The majority of Sri Lankan SMEs were owner-managed and consequently non-manager owners would be insignificant users of SME financial information. This finding endorses the view that the role of financial statements in stewardship reporting is less relevant to SMEs as there is no separation between ownership and control (Collis, 2008; Collis & Jarvis, 2000; McMahon & Stanger, 1995).

Overall the findings do not agree with the list of financial statement users identified by the IASB in the *IFRS for SMEs* which includes banks; vendors; credit rating agencies; customers; and shareholders who are not also managers of SMEs (International Accounting Standards Board, 2009b). According to IASB, financial statements prepared solely for owner-managers and for the tax reporting are not necessarily general purpose financial statements (International Accounting Standards Board, 2009a). The relevance of the *IFRS for SMEs* in meeting the financial reporting needs of Sri Lankan SME users' is questionable as the *IFRS for SMEs* was developed for different users.

9.3 Use of SME financial information

The 'use of SME financial information' theme reports respondents' perceptions of uses of SME financial information in decision making. The following sections explore the usefulness of SME financial information for owner-managers, bank lending officers, and income tax officers.

9.3.1 Use of financial information by owner-managers

Owner-managers were asked to indicate their overall perception of the usefulness of SME financial statements for their decision-making. Owner-managers generally agree their financial statements have little decision making value, since they are prepared for the purposes of compliance. Owner-managers consider the financial statements are too complex, outdated and cannot be understood because of lack of knowledge in accounting. The Profit and loss statement, to calculate tax liability, is the only useful financial statement.

> I cannot use the one prepared by the accounting firm for taking business decisions. I use the financial statement as a legal document to be submitted for certain purposes only. I do not use it for decision making within the company, because I find their format not suitable for my needs and it's very hard for me to understand. It does not give up-to-date financial information about the company. I do check the profit and loss account as to check on tax liability (Owner-manager 04).

There are several reasons for why owners hold a negative attitude towards financial statements. As reported in the literature, (Argilés & Slof, 2003; Bunea et al., 2012; Halabi et al., 2010; Sian & Roberts, 2009), owner-managers indicate that unfamiliarity with the subject, and the complicated accounting rules are the reasons for their negative perceptions. The ability to read financial statements, understand accounting terms and jargon as well as the language used by accountants is problematic for SME owners (Nandan, 2010).

Additionally, it appears that owner-managers maintain separate sets of records internally and use them for decision-making. They are aware that internally prepared documents provide them with the real picture of the business entity whereas financial statements prepared for taxation are prepared to minimise the tax liability. Consequently, the financial statements are useless for business decisions:

> We cannot show 100% accurate reports in this country. Now take the VAT it was increased by 4% but we cannot increase the price of our products. The US dollar value was 95 when I started. Now its 140 so that affects our imports. Because we have a credit period of 60 days by the time, we settle the bill the US dollar has increased. Therefore, we have to hide certain information but in management, we use the correct figures (Owner-manager 19).

> As a practice banks ask for financial statements but they know that we prepare at least three reports: one for the bank; one for the tax; and one for our use (Owner-manager 15).

> A separate set of accounts is prepared by my accounts executive for manufacturing division and the selling division, which are located in two different places. These are used by me for decision making (Owner-manager 02).

> I prefer to use the reports prepared internally. I do not rely on the reports prepared by the accounting firm (Owner-manager 14).

Almost all of the SME owner-managers use internal management information for making business decisions. It appears management information is easy to understand and is relied upon to provide accurate, detail, and up-to-date information about the entity's business operations:

> The management report helps me to take my ground level decisions to go on with the business day to day (Owner-manager 11).

> Management accounting information is most useful because we are not accountants. We understand management accounts easier, it's a bit more to our audience whereas financial accounts are more to an accounting audience. The internally prepared management information is not technical like financial statements and are up-to dated (Owner-manager 08).

Owner-managers' view on the usefulness of management information for decision making is confirmed by the SME accountants. They say they prepare management information for owner-managers for decision making:

> We prepare the management accounts for internal decisions. Only for compulsory compliance purposes, we do the financial statements (Accountant 01).

> He (owner) mostly prefers to look at the management accounts because he is daily involved in the business (Accountant 03).

> If we go for a standard format, first of all the owner can't understand, secondly, he does not like them. So, we have to adjust whatever he wants since he is our employer. He is using the monthly management accounts. If you take the interest of the accounts as a percentage, he is 90% more interested in the management accounts than in the financial statements (Accountant 06).

SMEs require adequate and sophisticated management accounting techniques and systems to manage scarce resources (Nandan, 2010). They need timely, accurate and reliable management accounting information (Greenhalgh, 2000; Marriott & Marriott, 2000; Nandan, 2010).

Many owner-managers place high importance on managing the cash flow position of the business. Owner-managers believe cash flow reports, and bank statements are useful documents to monitor the cash flow of the business as it shows how the cash movements and when cheques [33] have been presented. SMEs prepare management information daily, weekly, and/or monthly according to their own preferred format. Monitoring cash flow of the business is a major concern of owner-managers:

> We have our own system of recording financial information. I have instructed my management and the workers to prepare a book to record daily sales. It comes with printed sheet so they have to write it down on that particular book which helps me to get the information about the most demanded food item. As well as they prepare a separate book for daily expenses. At the end of the day, I check these two books so I can get an idea on daily cash flow position of the business (Owner-manager 03).

> We do not need the financial statements because I have a track of our daily performance. I check the online bank statements about three times a day so that I have a track of it. I know what is in the bank and about collections, due dates and payments. Apart from that, I check the invoices sent and the pending payments so I can follow up on payments. It’s an Excel sheet - I analyse that report for debtors (Owner-manager 04).

> He (the owner) is most concerned about the cash flow. He is asking daily “what is the cash position of the company”? (Accountant 03).

In addition to these reports, owners of large SMEs (with employees between 40 and 99) use budgets and accounting ratios for their decision making. Owner-managers

[33] Cheques are the most extensively used non-cash based payment instrument and is widely accepted by the business sector in Sri Lanka.

of SMEs in the manufacturing sector use cost analysis reports, production and productivity plans for their decision making. The responses from owner-managers show they use financial information mainly to monitor the performances of the business and to compare sales, profits, and costs with previous periods. Some owner-managers use their financial information to make investment decisions such as investing in land and buildings. Other owner-managers use internal financial information for deciding employees' bonuses and salaries.

> I compare our financials against the last 5 or 10 years to understand the progress of the business. So that I can set forecast and set targets. I check our performance last year and see where we went wrong and prepare the track for the next year (Owner-manager 01).

> My ultimate objective is to invest and go for a value addition where three containers I can cut down into one container and make the same amount of profit from one container than doing three. So, I'll be more than happy if I can reach that but to reach that I will have to collect money for a long period of time to build a standard cool room facility. Financial information of the business is very important when taking this type of investment decisions (Owner-manager 11).

> I use them mainly to check how to increase the wages I pay my employees. I have this goal to make this business very productive under the 5S system.[34] This is because I want this business to be the most productive as a recycling business and also I want my employees to be one of the highest paid employees in the country in this business (Owner-manager 13).

> In my company, I have a daily incentive system. Instead of paying bonuses, I have given them a specific target. For an example, if you do more than Rs60,000 in sales per day, whatever you do over Rs60,000 will be compensated. I have introduced such a system as it will curtail malpractices as well because employees are focussing on achieving the target. They know that

[34] The 5S methodology is one of the best tools for generating a change in attitude among workers and serves as a way to engage improvement activities within the workplace (Rod, Ron, & Kaoru, 2008). The 5S name corresponds to the first letter of five Japanese words – Seiri, Seiton, Seiso, Seiketsu, Shitsuke – as well as their rough English equivalents – Sort, Set in order, Shine, Standardise, Sustain (Jaca, Viles, Paipa-Galeano, Santos, & Mateo, 2014). This methodology instills good habits related to company organisation and cleanliness (Jaca et al., 2014).

> if they achieve above the target, as high as possible, they get higher incentives. For these reasons, I use my company's financial information (Owner-manager 03).

Contrary to research conducted in developed countries (Carsberg et al., 1985; Collis & Jarvis, 2000; Sian & Roberts, 2009), owner-managers believe that financial statements have a limited use for making business decisions. Legal compliance was the main driver for preparing financial statements, particularly for taxation. Owner-managers report the information in the financial statements is difficult to understand and not suitable for their decision-making. They prepare a separate set of accounts for their internal use. Financial statements prepared for taxation were not reliable for decision-making as they were prepared to hide the true results of the SME.

Owner-managers of this study have ready access to the internal financial information of the entity and find management information very useful for making their business decisions. They place considerable importance on managing their cash flows. They place importance on managing liquidity, as that is critical to the success and survival of a SME (Collis & Jarvis, 2002; McMahon & Stanger, 1995). Research suggests management and ownership in SMEs are rarely separated (Canadian Accounting Standards Board (2007); Collis, 2008; Collis & Jarvis, 2000; Page, 1984). This implies that owner-managers can daily observe the behaviour of an employed manager (McMahon & Stanger, 1995) as they have access to internal financial information (Canadian Accounting Standards Board, 2007).

9.3.2 Use of financial information by bank lending officers

The bank lending officers were asked if the financial statements of SMEs were useful for their lending decisions. In contrast to the IASB's view on the usefulness of SME financial statements for lending decisions (International Accounting Standards Board, 2009a, p. 16), there was a general consensus among bank lending officers that the financial statements provided by SMEs have limited use for lending decisions. Bank lending officers believe the accounting information included in the SME financial statements does not provide them with a true picture of the entity's financial position as they were prepared for tax purposes. Lack of knowledge of SME owners on financial reporting was also considered as a main reason for not preparing proper financial statements. Some bank lending officers hold the view that SMEs prepare financial statements only when they need a loan. Consequently, bank lending officers place low reliance on the SME financial statements when they make lending decisions:

> We get financial statements to check how they are performing, but just because the numbers are presented, we do not depend on them fully. SMEs are inclined to hide information, and this practice is facilitated by their political connections. Owners know how to deal with these matters. We have corrupt officers everywhere. You know we have that type of culture in Sri Lanka. If you give some bribe to these officers, they will do anything for you. This a serious situation in Sri Lanka (Bank lending officer 01).

> The biggest problem we face in Sri Lanka is that most SMEs do not maintain good accounts because the lack of knowledge and the rules and regulations. Most SMEs do not have financial reports because they have no knowledge. Sometimes it is a family entity with the family being employed in the business or it is one or two people doing the full operation. The need for financial reports comes only when they need a loan. They are also scared of taxation. Therefore, they try to manipulate their financial information. Even if a company brings their own information, we do our own reports because we do not rely on their reports (Bank lending officer 02).

The bank lending officers' perception of the usefulness of SME financial statements for making lending decisions was consistent with the views given by owner-managers. Both believe financial statements have limited use for obtaining bank facilities, as banks do not entirely depend on the financial statements. One owner-manager commented on this issue:

> Most of these banks do not like the reports that these Chartered Accountants prepare because you pay them about Rs20,000 and they will manipulate the information the way you want. I asked for a loan of Rs3 million recently and the only thing they checked was the books I maintain. I normally record my daily transaction in separate books. I handed over these books in the morning and in the evening got the ok on the loan. I asked them if they wanted the reports done by a Chartered Accountant, but they said what I give them is more than enough (Owner-manager 13).

Bank lending officers generally agree that audited financial statements do enhance the reliability of SME accounting information. However, the credibility of auditors who carry out the audits is a concern, because the audits of SME financial statements can be undertaken by either registered auditors or small and mid-tier audit firms in Sri Lanka. Registered auditors are neither required to comply with the Code of Ethics and Continuing Professional Development (CPD) requirements nor subject to the investigation or disciplinary action of a professional accountancy organisation or other similar regulator (Wickramasinghe, 2015).

In addition, there is a low level of compliance with auditing standards by small and mid-tier audit firms due to their limited technical capacity (Wickramasinghe, 2015; Yapa et al., 2017). Small and mid-tier audit firms find it difficult to bear the cost of implementing auditing standards due to competitive pricing from registered auditors (Wickramasinghe, 2015). Similarly, staffing, knowledge management, keeping up-to-date through professional development and stress are known challenges faced by small and mid-tier audit firms in general (Alam & Nandan, 2010; Ciccotosto et al., 2008). Consequently, bank lending officers prefer financial statements audited by reputable Sri Lankan audit firms. One bank lending officer states:

> The audited financial statements are not reliable and not enough to evaluate their real income and current state. Most customers try to show a reduced income. If their audited financial statements show Rs100 million turnover, they actually do Rs200 million turnover. Quality of the audit is a matter. If it is done by a reputed audit firm, then we do consider it. Otherwise, we obtain extra documents to verify the figures (Bank lending officer 03).

It appears that the major financial information used in lending decisions to SMEs relates to profitability, cash flows, and gearing. However, bank lending officers do not depend on financial statements to obtain this information due to incorrect figures in the financial statements:

> … the main ratios we calculate are the gross profit ratio, net profit ratio, and the working capital gap. Debt-equity ratio is another important ratio to check whether they are highly geared. However, the main problem is 99% of customers prepare financial statements for the tax purposes and it does not reveal true and fair view even though sometimes it includes the audit report. Normally the sales figure has been under-stated and customers do not include debt that is the facilities obtained from other banks.

> Due to these reasons, we have to get additional information from SMEs (Bank lending officer 05).

Rather than relying on the information contained in the financial statements, bank lending officers verify the accuracy of the financial statements and prepare their own reports, such as projected cash flows, profit and loss and balance sheet, by interviewing the owners and/or visiting the business premises. Most of the time they obtain sales and purchases through the internal records and documents of the business such as sales and purchase books, bills, and management accounts. It seems that management accounting information plays an important role in this regard. Some bank lending officers report they even examine electricity, water, and telephone bills to estimate production volumes of SMEs. Additionally, the banks' internal database, credit report, borrowers' character, information from SMEs' suppliers and customers, and business registrations are used for making lending decisions. Banks have the ability to obtain additional information from SMEs to make lending decisions and do not depend, on financial statements provided by the SMEs.

Although several methods were used to make lending decisions, it appears collateral is required for all types of loans. This finding is consistent with Gamage (2015) who claims that Sri Lankan banks predicate their decisions not on cash flows but on collateral when making lending decisions to SME sector (Gamage, 2015). One bank lending officer shared that they normally go for cash flow-based lending for corporate level customers and collateral base lending for SMEs:

> …corporate level companies normally do not give any collateral they usually give their financial statements so when it comes to corporate level of course, cash flow based lending but when it comes to SMEs, still it will be either against their project assets or maybe movable property (Bank lending officer 04).

The discussions with bank lending officers further reveal that they did not use SME financial statements for loan monitoring purposes. Bank lending officers indicate getting financial statements to monitor the utilisation of the loan is pointless. However, one bank lending officer said that they normally ask SMEs to submit their financial statements annually to review the progress and submission of annual financial information is a condition when they grant loans. Most of the other bank lending officers do site visits to monitor the progress of the loan. The literature on the usefulness of SME financial statements for loan monitoring appears to be silent.

Generally, loans are released in instalments and before disbursing each instalment, banks carry out an inspection to satisfy themselves about the proper utilisation of funds. The frequency of the site visits depends on the individual customer. If bank lending officers foresee a risk, they arrange monthly or quarterly inspections with a regional manager. Following a visit, they prepare a visit report and include it in the customer's file. Additionally, they conduct an annual review of the facility by looking at arrears with the bank and with other banks. Following statements illustrate the loan monitoring process of two banks:

> … once we gave the loan, we do not check their financial information regularly. That is only done at the point of deciding the loan. Once it is given, we just check the rhythm of their business and how they are doing. Once a year we get them to visit the person who approves the proposal. We do a visit and get a visit report which is included into the file. We also do a review of the facilities to see if there are arrears in other banks and the arrears they have with our bank (Bank lending officer 01).

> … we are coming back to the same problem. If we can't rely on their financial statements we will not ask, pointless. We will do our own evaluation. We will visit and we will do our own evaluation and see where they stand. Even after granting or disbursing a loan, there will be inspections. We normally grant the loan in instalments. If it is only one single activity to purchase a machinery of course then it will be a single disbursement but what normally happens is the requirement will be partly for working capital, so the fund allocation will be in stages for various purposes. So before disbursing each instalment, we will be carrying out an inspection to see, to satisfy ourselves with regard to proper utilisation of funds (Bank lending officer 04).

Bank lending officers placed low reliance on the financial statements of SMEs when making lending decisions, they gathered information they needed through site visits and interviews with the owners. This finding is consistent with Dang-Duc et al. (2008) in Vietnam, who found that small entities' financial statements were not very useful in loan decision making. Site visit and direct communication with clients, for example, were used as alternative sources of information (Dang-Duc et al., 2008). By contrast, research conducted in developed countries indicates that financial statements play an important role in bank lending decisions (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Maingot & Zeghal, 2006; Page, 1984)

Bank lending officers place little importance on the audited financial statements. They access and use management information for making lending decisions. This finding contradicts earlier findings in developed countries (Berry & Robertson, 2006; Deakins & Hussain, 1994; Duréndez Gómez-Guillamón, 2003) and developing countries such as Jordon (Abu-Nassar & Rutherford, 1996). Although research shows financial statements plays an important role in lending decisions, there is no evidence on their role as means of monitoring borrowing.

Overall, the findings suggest that the decision usefulness of SME financial statements for making lending decisions and monitoring borrowing was limited largely due to the tax oriented financial reporting practices among SMEs in Sri Lanka.

9.3.3 Use of financial information by income tax officers

Income tax officers were asked if the SME financial statements were useful for their job. Consistent with the perceptions of bank lending officers, income tax officers express a major concern over the credibility of SME financial statements. They are aware that financial statements for tax purposes understate the profits. They have reservations about the external accountants who prepare the SME financial statements; particularly about the qualifications of the external accountant:

> … there is third-party involvement like an accountant to prepare SME financial statements. Most of the time he is not a Chartered Accountant. Usually someone below that level does the accounts and brings them to us. Therefore, there is a room for misinterpretations. When we query them, they are unable to answer our questions. When we use the technical analysis of ratios, we find some abnormal findings in their financial statements. With or without their knowledge, the accounts are manipulated and we find these out when we use the technical analysis of ratios.
>
> If the accounts are not accurate, what taxpayers tell us is different to what their financials are telling us and there is a discrepancy.

> In such a situation, the taxpayer is faced with many issues, as they do not know the reasons for the discrepancy or might not be able to defend their accounts (Income tax officer 01).

SME financial reporting in Sri Lanka is influenced by the accountants who provide services to this sector. Apart from the credibility of SME financial statements, inadequate detailed information in the financial statements is also a major concern for Income tax officers when they carry out the assessment of tax liabilities of SMEs. Therefore, SMEs are asked to submit detailed information about such as turnover, expenses, creditors and debtors. Income tax officers say that producing a cash flow statements is not a compulsory for SMEs.

> Most of the cases we cannot get adequate information from SME financial statements because it's a summary for the whole-year transactions. We are not in a position to get a decision from that. In addition to the financial statements, they are also required to provide the detailed financial information; that means break ups related to both balance sheet and income statement …. We go through those documents and if we have any suspect or any doubt then we query from taxpayers (Income tax officer 02).

The SME financial information is compared with other SMEs in the same industry to reveal any abnormal findings, as income tax officers are aware about the industry trends and mark ups. Further, they acquire information from creditors, debtors and other government agencies (such as the Registrar of motor vehicles, and the Land Registration Department), and make site visits to cross-check the data contained in the financial statements. However, if they come across with any abnormal findings, they generally request additional information from taxpayers.

Income tax officers do not solely depend on the SME financial statements for assessing income tax. The lack of credibility of SME financial statements and inadequate detailed information in the financial statements were seen as major reasons for low reliance on SME financial statements. Income tax officers use their powers to obtain additional information to make their tax assessments. The credibility of accountants who provide accounting and auditing services to SMEs is also a major concern of income tax officers.

These findings contrast with the reliance on SME financial information by tax authorities as discussed in the literature. According to the International Federation of Accountants (2006) and Barker and Noonan (1996) the major uses of SME financial statements by the tax authorities include: determining gross profit; assessing directors' fees; and expenses; and to determine whether a company's financial statements have a qualified auditor report.

9.4. Need for international comparable accounting information

Owner-managers and accountants were asked to express their overall perception of the usefulness of international accounting standards for SMEs. International accounting standards are not well perceived by the most of owner-managers and accountants of SMEs. They were not certain about the usefulness of such accounting standards for SMEs. Thus, they comment negatively on the role of international accounting standards for SMEs. One accountant said that they followed accounting standards only for compliance purposes:

> We need these international accounting standards only for compliance purposes. Other than that, I cannot see any use of this. Actually, I don't know … like may be after two to three years, you can really see the outcome. Since it was recently introduced, I cannot give an opinion (Accountant 02).

It appears that business matters are the greatest concern of owner-managers. Complexity and limited usefulness of the statutory financial statements for making business decisions were major reasons for their negative perceptions on the international accounting standards. They believed that accounting standards are impractical and do not add any value to their business:

> An entrepreneur has no value for these international accounting standard things. Farmers back in the day did not rely on modern ways of forecasting weather. Instead, they look at the behaviours of birds and animals to predict the weather. See it is something that comes from within. You need to be very practical to get ahead in business. These accounting standards are good for the second-generation business people… the ones who have inherited the business from their parents… the ones who have no practical feel of what they are doing. If you inherently have the business feel within you, there is no need for such accounting standards. People who rely on such documents lose sight of reality. A business should be like a river not a drain.…. These international accountings standards are like drains. The business person should have their business close to their heart… people

> who rely on this accounting side they just sit in front of the computer trying understand numbers and their business suffers as a result (Owner-manager 13).

Owner-managers and accountants also believe financial statements should satisfy the needs of those who use these reports. It appears international accounting standards have limited use for taxation and management purposes. Owner-managers do not perceive any use for accounting standards in preparing accounts for users of SME financial information:

> I can't see why there should be international accounting standards. It is the Inland Revenue or some authority who wants to review your financial reports, then it has to be in that readable form so that they could understand the financials of the entity. That's what it should be. For management purposes, I do not think we need these accounting standards (Owner-manager 21).

The above explanation given by the owner-manager indicate that they do not have users who make decisions based on the financial information prepared in compliance with international accounting standards. Similarly, Paseková et al. (2010) establish that the majority of SMEs in the Czech Republic and Ukraine use accounting just to provide data which are necessary for tax calculation. SMEs in both countries are only weakly interested in reporting under the *IFRS for SMEs* (Paseková et al., 2010).

However, owner managers and accountants who are members of Institute of Chartered Accountants of Sri Lanka (CASL) commented positively on accounting standards and had adopted the *SLFRS for SMEs* for their financial reporting. They believe accounting standards give uniformity and discipline to financial information produced by SMEs. They hold the opinion that adopting international accounting standards would be beneficial if an entity might need to move to the next level of operations. A member of CASL comments positively about the accounting standards for SMEs:

> Adoption of international accounting standards for financial reporting is good because we have financial discipline. It is important that these accounting standards are maintained as it works as a guide on how to do the financial reporting. Accordingly, we have adopted this accounting standard for our financial reporting (Accountant 03).

An owner manager (who is a member of the CASL) also expresses a positive view:

> Technically, I am not an expert on *SLFRS for SMEs* because I am not dealing with that. However, I think it was simplified and it is not complex (Owner-manager 22).

Consistent with the previous research conducted in developed countries by Eierle and Haller (2009) and the Conseil National de la Comptabilité (2008) most of owner-managers and accountants do not perceive any benefit from internationally comparable accounting information. Many owner-mangers and accountants consider that most SME transactions are within domestic markets and that international activities, such as foreign exports, ownership, and borrowings, were not relevant to most of them. They perceive the reporting requirements of the *SLFRS for SMEs* as an additional burden on them. Lack of resources, capabilities, and assistance or incentives from the government are considered as barriers for them to engage in international activities. All these reasons have been identified by other researchers as barriers for engaging in international activities by SMEs (see, Burpitt & Rondinelli, 2000; Coviello & McAuley, 1999; Shaw & Darroch, 2004; Ward, 1993). The barriers that cause the greatest problems are those relating to limited resources and lack of government assistance or incentives. Owner-managers described lack of government support as follows:

> I do not see that these people (government) are taking any proper solid decisions to support SME businesses to upgrade to the international level (Owner-manager 11).

> I do not think there is a need to provide these types of accounting information because it does not provide us any benefit. We like to do exports but we have no link for that. I have tried to send my tyres to Gambia but there is no support for this. Government should introduce assistance programs to SME sector. I think if we are doing a foreign business, we might need these international accounting standards. Otherwise useless (Owner-manager 17).

It appeared that some owner-managers struggle to survive their business and hence international activities are of minor importance. One owner manager shares his struggles:

> With all these business stresses, I got diabetes. I have glaucoma in one eye and I lost my vision. I continue this business just to

> make some money. After the business started to decline, I felt there was no use to invest anymore. Therefore, my plan now is to finish paying the loan. I have no intention to expand my business internationally (Owner-manager 16).

Owner-managers and accountants reveal few SMEs engage in foreign exports. However, SMEs engaging in exporting and importing goods and/or services do not receive any requests from their foreign customers or suppliers to provide accounting information prepared in compliance with international accounting standards. Purchases of goods and services was the principal cross border activity:

> We deal with foreign suppliers as we import our raw materials (Accountant 01).
>
> We import because the main raw materials like the tomato ketchup and the soya flour for food that we import from China and other countries (Owner-manager 22).
>
> We only deal with imports so our suppliers are not interested on checking our financial information (Owner-manager 06).
>
> We are dealing with foreign suppliers through banks. I think banks would give a guarantee about the payments and stuff so if the supplier is worried about the payment then they will obviously ask for a guarantee with the banks (Owner-manager 07).

Instead of requesting SME financial information, foreign suppliers/customers check the SMEs web sites, industry information, ISO certifications and bank guarantees. However, information required by these buyers/suppliers varies according to the foreign markets they deal with:

> It depends on the foreign market that you cater to. I am sure if you are catering to US, Germany, UK and European countries, it (international accounting standards) would support you but mine is just to China. Chinese people do need a health certificate; they do not request our financial information (Owner-manager 11).
>
> The buyers from Japan usually need to see our industry before they can trust us to do business. They do not go by the financial statements we prepare (Owner-manager 15).

Atik (2010) claims entities which have foreign partners or export activities are more likely to adopt international financial reporting standards, but an accountant with a foreign owner in his business reports that he does not experience a demand for financial reporting in compliance with international reporting standards;

> We have a foreign ownership. One of our owners is from Japan. He is not interested of international accounting standards. I think they do not follow IFRS for SMEs (Accountant 02).

In contrast to the IASB's perception, Sri Lankan SMEs do not see a need to provide internationally comparable accounting information. This finding is consistent with the previous studies conducted by Eierle and Haller (2009), the Conseil National de la Comptabilité (2008), and Aboagye-Otchere and Agbeibor (2012). It is noted that international activities are of little relevant to Sri Lankan SMEs. Business matters and the survival of the business are prime concerns of Sri Lankan owner-managers and their internationalisation is limited as they are constrained by limited resources and lack of government assistance.

9.5 Adoption process, awareness and knowledge of *SLFRS for SMEs*

Respondents discussed the adoption process of *SLFRS for SMEs*. It appeared from the discussion with the representatives of the standard setter in Sri Lanka that they did not receive an adequate number of comments about the accounting standard during the review process of the *SLFRS for SMEs.* They did not reveal the number of comments received or the source of those comments. The exposure draft of the standard was posted on the standard setter's web site to solicit the views from interested parties before adopting *SLFRS for SMEs*. The standard setter representative explains the adoption process:

> Once we have a particular accounting standard, there would be an exposure draft. Similarly, we sent exposure draft of *SLFRS for SMEs* to all the interested parties from the universities to industries, and to the members. It was made available in the web site as well. We generally organise a round table discussion. However, comments received for the *SLFRS for SMEs* were comparatively low. I think our people are not proactive enough to comment on a particular accounting standard. That is our culture. Once the accounting standard is readily available and finalised, they want to know how to get ready for it, that is the mentality. We have to change that definitely. Actually, it is basically based on the comments we have received from our members, Chambers and other entities. Once we issue the

> accounting standard, we do training. Participation in these training programmes is good (Standard Setter- representative 01).

There seems to have been no comments from the government institutions that are involved in setting policies for the SME sector. It appears that the standard setter did not encourage ‘other interested parties’ such as government institutions to participate in this process. Instead, they relied heavily on comments given by their members and members of the accounting standard committee. It could be said that approval or support for the *SLFRS for SMEs* was not invited and comments not particularly welcomed:

> We have the authority to set accounting standards in Sri Lanka. The Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 has given the permission to do so. There is no need to take the approval from the Ministry of Finance or anybody. Because it is a one-time approval, they have given from the Act. The Ministry of Finance is not involved in this process. Actually, we have delegated this task to the Accounting Standards Committee. It has the capacity (experience and calibre) to do that. The composition of the committee is very good (Standard Setter - representative 01).

> They (standard setter) did not consult us before adopting this accounting standard (*SLFRS for SMEs*). However, we are engaged in the implementation part. I mean, we facilitate the implementation of this standard (Government institution 01).

It appears from the above quote that users’ views on the *SLFRS for SMEs* were not represented during the review process. This finding raises an important question relating to the decision usefulness of accounting information prepared in compliance with *SLFRS for SMEs* due to inadequate user involvement in the accounting standard setting process (Durocher et al., 2007; Harding & McKinnon, 1997). As a result, standards may be unworkable in application, overly costly, or even inconsistent with basic concepts (Tandy & Wilburn, 1992).

One respondent from the standard setter emphasised the importance of research on users of SME financial information to figure out their financial reporting needs. He believes that academics could be involved in this process:

> … if academics can support this decision by way of research it’s a great help for us to make our future decisions in relation to

> promulgation of accounting standards for SMEs. Actually, I think the discussion we had and the way you analyse the data would be very important. Now once you discuss this matter, the layers of accounting standard and how we are going to capture SMEs into this whole framework is very useful. What I want to emphasise is basically do this analysis and give the feedback to us. Because it is an independent feedback we are getting, then we can further fine tune our financial reporting standard, and the promulgation process. Actually, we are expecting that support from the academics (Standard Setter - representative 01).

The standard setter conducted various seminars and awareness programmes on the accounting standard *SLFRS for SMEs* for owner-managers and accountants of SMEs, and small and mid-tier audit firms who carryout audits of SMEs. The standard setter of Sri Lanka received a grant of US$500,000 from the World Bank to improve the awareness and skills in *SLFRS for SMEs* among SME accountants and to strengthen the skills and competencies of small and mid-tier audit firms (Sunday Observer, 2012). A representative from standard setter explains:

> We got a grant from the World Bank. It covered four parts: quality assurance; capacity building of SMEs and small and mid-tier audit firms; the third one is to increase adoption of the IFRS; and the fourth was on public sector accounting standards. Under the capacity building for SMEs and small and mid-tier audit firms, we developed a separate project manual and we conducted seminars and workshops to SMEs on how to apply *SLFRS for SMEs* and to small and mid-tier audit firms on how to apply auditing standards for SMEs (Standard Setter- representative 02).

Also, the standard setter received funds from the, German Development Cooperation (Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH) to achieve inclusive development of the SME sector (Institute of Chartered Accountants of Sri Lanka, 2017). The GIZ project with the standard setter focuses on conducting regional seminars on *SLFRS for SMEs* as well as training programmes on basic accounting and bookkeeping for SMEs (Institute of Chartered Accountants of Sri Lanka, 2017). Throughout the project, a help desk was also established to support SMEs and small and mid-tier audit firms while technical materials, guidance notes, application guidance and practice notes on *SLFRS for SMEs* were also published for the benefit of SMEs and small and mid-tier audit firms. One respondent from the standard setter described the institutional support received from international donor agencies:

> We recently entered into an agreement with GIZ, a donor agency for SMEs. GIZ wanted to build the capacity and to provide assistance for SMEs. With their support, we have initiated so many projects recently. The first one is on making the awareness of the *SLFRS for SMEs*. So we had seven regional seminars on *SLFRS for SMEs.* Asian Development Bank funded seminars and workshops conducted to teachers and SMEs. With the support of ADB, we conducted regional seminars on the SME standards and we trained 300+ SMPs on how to use the audit manual (Standard Setter - representative 02).

It appears that the standard setter also receives technical assistance from the IASB when implementing the accounting standard *SLFRS for SMEs*:

> If we have a query, we will certainly write to the IASB seeking assistance. Then they (IASB) are giving advice on how to apply these particularly standards in the accounting context, and what is the accounting treatment. I think support from them is also quite enough (Standard Setter - representative 01).

> We get technical assistance from the IASB. Actually, one board member of the IASB and the chairman of SME implementation group came here and they did a training session on how to apply the SME standard. We are getting their updates and technical resources that are available in their websites. We are keeping in touch with them and we write to them when have a clarification. One of our senior members is in the implementation group of the *IFRS for SMEs* (Standard Setter - representative 02).

The IASB and the standard setter in Sri Lanka play an active role to promote the adoption of the *SLFRS for SMEs* and provide training and seminars to CASL members. In addition, these institutions also educate CASL members by providing interpretations and guidance on the standard.

Though the standard setter in Sri Lanka conducted seminars and workshops on *SLFRS for SMEs*, there is a low level of awareness about the *SLFRS for SMEs* amongst owner-managers of SMEs. Only four owner-managers, have accounting related qualifications and even they have limited knowledge of the accounting standards. The awareness of the existence and implementation of the *SLFRS for SMEs* is extremely low despite all the expenditure on publicity and training.

> Until you mentioned it I had no idea about this standard. This is the usual case here; they bring something that is practised elsewhere and implement it here (Owner-manager 15).
>
> Honestly, I was of the impression that they were using the Sri Lanka accounting standards, the usual accounting standards that they would use for public limited companies and I was not aware up until you told me that there is a separate set of accounting standards for SMEs which I should start studying (Owner-manager 05).
>
> I do not have a clear idea about the standards and I have not been trained on it. Whatever I know is the information I have searched for. It's rare that these audit firms provide us that information. They should make us aware. Even the chartered institute is not close to the SMEs, the government is useless …. everything is politicalised. I think we have to go to the grassroots and train (Owner-manager 01).

Some of the owner-managers and accountants had been made aware by their external accountants about *SLFRS for SMEs*. It appears that the decision to adopt *SLFRS for SMEs* was taken not by them but by their external accounting firms:

> Yes, I know that there is a new accounting standard for SMEs. My accounting firm X (name of a small and mid –tier audit firm in Sri Lanka) informed me about this. I think we need to follow that standard, as it is a legal requirement. Therefore, I asked my accounting firm to prepare my financial reports as per these rules and submit to the relevant authorities on my behalf (Owner-manager 17).
>
> One of the chartered accountancy firms in Sri Lanka prepares our audited financial statements. They mentioned about this requirement. I'm not interested of knowing all these. They (name of a small and mid-tier audit firm in SL) are experts in the field and they know what to do. They prepare my accounts and advise me accordingly (Owner-manager 19).
>
> When it (*SLFRS for SMEs*) was introduced, we were informed by our audit firm. We had a chat and learnt that we were going to adopt this accounting standard. We always seek advice from them (Accountant 02).

It seems that SME accountants, including members of CASL, were aware of the *SLFRS for SMEs* and some of them did participate to the training programmes conducted by the standard setter. However, they still have a limited knowledge about the *SLFRS for SMEs*. They are not interested of knowing all of the accounting details and rules in the *SLFRS for SMEs* as only few of them are applicable to their businesses.

> I participated to the training workshops conducted by the standard setter but I do not think it was successful. I have not studied the entire book but I have gone through the sections that are required (Accountant 04).
>
> I do not have much of a technical knowledge of these but I'll tell you that these standards should be done in way to support SMEs. I think most of these standards are not practiced by these SMEs, its only public limited companies. We practice the basic what is required by the Inland Revenue Department (Accountant 01).
>
> Yes, I am aware of this accounting standard (*SLFRS for SMEs*) but only few of them (accounting standards) are relevant to our business. We do not have complex transactions. So then we are using only very few standards. We seek assistance from our audit firm (Accountant 03).

Similarly, it appears that there is a limited knowledge among income tax officers and bank lending officers on the *SLFRS for SMEs*:

> I am not too familiar with these standard (Bank lending officer 01).
>
> Our tax officers are not competent with that *SLFRS for SMEs* because not all our officers are Chartered Accountants (Income tax officer 02).

The above findings agree with Albu et al. (2011) who claim that a lack of IFRS knowledge is one of the challenges faced by developing countries when implementing international accounting standard. Lack of training programmes arranged by professional bodies is considered to be the most serious obstacles to implementation of the international accounting standards (Uyar & Güngörmüş, 2013).

9.6 Costs and benefits of *SLFRS for SMEs*

The costs and benefits of financial reporting can be associated with preparers of financial statements, users of financial statements, auditors, and standard setters (Litjens et al., 2012). The costs and benefits of financial reporting are met when the benefits derived from information exceed the costs borne or imposed upon the enterprise in the preparation of financial statements (International Accounting Standards Board, 2009b, p. 14). The following two sections describes respondents' perceptions about the costs incurred and benefits received from preparing financial statements in compliance with *SLFRS for SMEs*.

9.6.1 Perceived costs of *SLFRS for SMEs*

As owner-managers are not familiar with or not aware of the *SLFRS for SMEs,* they could not comment on the specific cost of adopting *SLFRS for SMEs*. However, in general, owner-managers believe that preparing financial statements in compliance with international accounting standards is a burden. The main costs of the application of *SLFRS for SMEs* as perceived by the owner-managers and accountants were related to accounting and auditing fees:

> *SLFRS for SMEs* are costly because the financial service fees are very high. We need external accountants' assistance to prepare financial reports according to the requirements but we are worried about the professional fee. We have to submit audited financials to income tax as well. For that, also we have to incur some money. Recently they have increased their charges as well. If the government or Institute of Chartered Accountants of Sri Lanka controls it, it is reasonable. Most people do not understand these things. It has to be a reasonable amount. It is very high at the moment. Professionals should not be just the money focus (Owner-manager-01).
>
> I think their fees are very unfair not reasonable at all. However, we have to get that service. We do not have an option as we do not have such expertise in house (Owner-manager-04).
>
> An external firm prepares our accounting reports. They charge a lot for this. I do not know why. If they train our accountant, I am sure he could prepare balance sheet, P &L, and everything according to these accounting standards (Owner- manager-02).

Consistent with the previous research on SME financial reporting (Carsberg et al., 1985; Kitching et al., 2011; Marriott & Marriott, 2000; Professional Oversight Board for Accountancy, 2006), it seems that most of the SME owner-managers depend on their accounting firms to comply with financial reporting requirements. They do not have the in-house accounting expertise and therefore rely heavily on outside accounting expertise, which results in higher fees (Eierle & Haller, 2009). They say:

> We use to consult our auditors when we have accounting and tax matters. We are not in touch with the current trends with regard to taxes and accounting standards (Owner-manager 22).
>
> Financial statements are prepared by the accounting firm and they prepare them for regulatory requirements (Owner-manager 08).
>
> I have an accountant but she is not a chartered accountant. We submit the file of accounts to the external accounting firm. They prepare financial reports including all notes. Once our accounts done, they are the people who file the tax return to the Income Tax Department (Owner-manager 06).

SMEs often do not have internal qualified accountants to prepare financial statements in accordance with the international accounting standards and have to depend on external accountants. Implementing international accounting standards require technical experts from the accounting environment. This causes additional problems, there because there are not enough chartered accountants in Sri Lanka to meet the needs of the country (as discussed in section 2.6.2),

> I mean even to apply these accounting standards, we need qualified accountants. We cannot recruit qualified people because of their cost. We have to depend on external accountants to prepare these reports for us. I think companies should be categorised according to their capabilities. So, financial reporting requirements should be according to those respective categories (Owner-manager 06).
>
> You need to get trained staff which will be expensive to maintain. I think these standards should be customised to our needs and people should be educated on these standards (Owner-manager 14).

> It is better to train the accountant on these accounting standards so they can produce these reports internally. All the bosses cannot study the accounts (Owner-manager 10).

SMEs often have difficulties in obtaining competent persons because of their inability to offer competitive salaries and benefits (Jennings & Beaver, 1997). But, a different view is expressed by owner managers who are members of CASL.

> I find the costs that we incur are moderate. I am quite senior in my profession and quite active so when they try to throw a figure at me, they are generally careful (Owner-manager 21).

> Yes, our advantage is they are also our friends but they charge so what we feel is they give an additional service because of our relationship and always we can call and in a friendly manner we can get what we want. Therefore, the situation is different to other companies (Owner-manager 22).

Some owner-managers and SME accountants express concerns about particular accounting treatments and methods included in the *SLFRS for SMEs*. Similar to the findings of Eierle and Haller (2009) and Chand et al. (2015), owner-mangers of this study find the use of fair value accounting in *SLFRS for SMEs* imposes significant additional costs. They were of the opinion that fair value calculations were complex and time consuming. Getting specialists to perform valuations and prepare reports are a major cost involved in fair value accounting:

> We have to get assistance from our chartered accountants for fair value related calculations. You know whatever the services we obtained, we have to pay for them (Accountant 06).

> According to these standards, debtors and investments are discounted. I do not know how we categorize what discounted means. I think we show the debtors at a lesser amount. So it is complex. It is not easy. We have to get help from the chartered accountants. Asking them is the easy way they can explain it better. I think it is too complex for SMEs (Accountant 05).

One owner-manager, who is a member of CASL, also comments:

> Our accountant has to waste a lot of time to calculate gratuity calculation. We have to provide for that and there is some formula for calculation. Our accountant is saying, “the auditors are not doing it, I have to do it” and then he takes about one whole day doing it. So, these are things that if standards have to be

maintained they have to be done in a simple way (Owner-manager 20).

In addition, income tax officers believe valuers and valuation techniques for fair value calculations adopted by SMEs might not provide reliable information as Sri Lanka is not an active market. Reliability of this type of information is questionable as income tax officers were not in a position to verify the accuracy of these estimates and there is room for managerial bias in estimates. Further, no data base of qualified valuers in Sri Lanka exists:

> Sri Lanka is not a transparent market. We are not in a position to measure these values are correct or not. It's a big issue. We do not have a database of the valuers to check whether they are qualified (Income tax officer 02).

Similarly, Kumarasiri and Fisher (2011) identify specific challenges of concern to Sri Lankan auditors with regard to fair value accounting. These concerns include: lack of auditor knowledge, the prevalence of inactive markets, difficulties associated with the variation in techniques used to ascertain fair values across different industries, general complexities in ascertaining fair values, and the incorporation of future events and conditions into valuations.

Overall, there was a general consensus for simplified financial reporting requirements for SMEs. Undue burden and costs resulting from the application of *SLFRS for SMEs* was a major reason for advocating a simpler accounting standard for SMEs. Owner-managers and accountants believe that financial reporting requirements should be developed based on the nature of the business and other capabilities of SMEs:

> A company like M… I mean they are doing like millions of transactions even for a month and my one is it's like a shark and a small fish. You cannot apply the same criteria to the entities who are in the two extremes. I mean when you look at the business you can see small entrepreneurs, medium entrepreneurs, large entrepreneurs likewise it has been categorised according to their capabilities (Owner-manager 03).

> I think you can't ask all SMEs to adhere with these accounting standards. You will find half the things are blank and it's a waste of time. You have to tailor-made for your own purpose. Because all the accounts are for you to understand. They have to do a

> research and identify who should apply these complex rules (Owner-manager 21).
>
> If you take me and company X (a name of a larger SME), we both have to go through the same accounting standards. Other than that, I feel that it's really good if they can look into the SME sector and come up with a different set of financial reporting requirements at least by looking at the volumes that they do. Otherwise, you are sending different level businesses through a uniformed set of rules, which is not right. It is like one common exam for grade 1s, grade 5s and grade 10s to sit (Owner manager-11).

Bank lending officers are also of the view that compliance with accounting standards is not necessary for making lending decisions to SMEs. They believe that if they had simpler formats, the majority of customers would use them and not fear submitting accurate information to bank when seeking loan facilities. Bank lending officers do not require financial statements prepared in accordance with complex accounting standards when making lending decisions to SMEs. Instead, they prefer a simple format that could be used to get accurate financial data on turnover, cash flows, cost of sales, expenses, and the profits. Some of them believe that international accounting standards were not applicable to most of the Sri Lankan SMEs. They contend these accounting standards should be modified to reflect the local business environment:

> …most local companies here are different to the SMEs overseas. You cannot just apply standards used overseas here. They should do a research and get some idea and provide some exceptions, modifications to these standards. Most of the legal things we follow were brought here during the colonial times and there were no changes done to suit our culture. That is the reason it doesn't work here. We have to do customisation to suit our businesses if we are to use such standards. We have enough educated people in the accounting field who can help in this customisation and to add exceptions and modifications to suit different SMEs operating here (Bank lending officer 03).
>
> To assist the bank or the loan application you don't require very complicated standards. We just want the turnover, what are the costs they have, cost of sales and also the profit, what is the profit. You can tell actually the profit margin, he has an idea regarding the sales but they have not recorded the things so we just want the turnover, the cost of sales, gross profit and finally the net profit. If he pays some taxes then what are the tax payments like?

> So beyond that we do not need information so the turnover, cost of sales like that. Using that information, we can project the financial statements (Bank lending officer 05).

Consistent with the views of bank lending officers, income tax officers also prefer a simple format for SME financial reporting. Income tax officers believe that just by applying these accounting standards, they cannot get the information they need. One income tax officer advocates that the Inland Revenue department should design a proper simplified format for SME financial reporting with input from the standard setter in Sri Lanka.

> I do not think just by applying accounting standards you can get the information. We will get more genuine information if the format is simplified. I think it is better if we can liaise with the Institute of Chartered Accountants of Sri Lanka and develop something more simplified for SMEs (Income tax officer 01).

> I think in our case it's good to have a simplified format for SME financial reporting because it is easy to check them with simple standards. You know that not all our officers are chartered accountants, they have various degrees. If it is simplified, it is easy to understand (Income tax officer 02).

Respondents from government institutions believe that international accounting standards are suitable for large SMEs, who have resources and capabilities to implement such standards. They emphasise the need for having a simple financial reporting system for small SMEs. However, they believe that there should be a proper financial reporting culture within SMEs:

> If you give one set of accounting standards for all SMEs, I don't think some small entities are able to follow this, as they haven't resources. If they have not resources, they have to hire the resources to prepare these things, which may be another burden for their cash flow. So that, we should introduce some simple recording formats for them (Government institution 01).

> I think smaller SMEs do not have the capacity to adopt accounting standards like larger SMEs. Some of them even not familiar to maintain a simple accounting system. However, I think that financial reporting culture has to be planted to develop their business in future (Government institution 02).

Representatives from two government institutions in Sri Lanka believe that the small SMEs should be allowed to use a simple format to match with their resources and capabilities. They recognise the size of the enterprise has an impact on the cost of producing financial statements; that costs are proportionally higher for small SMEs (Jarvis & Collis, 2003b). As small SMEs are unable to spread the costs across large scale of operations, they are typically subject to proportionately higher costs than large firms (Kitching, 2006; Stainbank & Tafuh, 2011).

9.6.2 Benefits of *SLFRS for SMEs*

The IASB claims SMEs would see benefits, such as improved access to finance and comparability of financial statements from the use of *IFRS for SMEs*. In agreement with the IASB's view, the standard setter in Sri Lanka believes that *SLFRS for SMEs* would add credibility to SME financial statements, improve access to finance, and provide useful financial information to make decisions:

> … initially we had only the IFRS full version. IFRS full version is complex, and it is for the publicly interested entities. At that time, the global context also identified a similar problem of the complexity of IFRS for non-publicly accountable entities. Therefore, we decided to adopt *SLFRS for SMEs* an equivalent to *IFRS for SMEs* as the second layer of accounting standards. … with proper recording of financial information, SMEs could analyse the financial success of the organisation and really think about the way forward of the organisation. This kind of accounting standards would give credibility to SME financial statements and ease access to finance (Standard Setter-representative 01).

However, many owner-managers and accountants do not think their SMEs would realise these benefits and they were not certain about the benefits of adopting *SLFRS for SMEs*.

> No additional benefits. It's a clear presentation (Accountant 02).

> No more benefits both same way, a few more notes only no? So, same way no income statements, only change some words sometimes (Accountant 03).

> There could be benefits if you really look at a proper set of standards not to import an international standard into a country and say "now do it". I don't think that is going to work. Somebody can research and do a standard (Owner-manager 21).

In contrast to the IASB's and the local standard setter's position, both favouring adoption of the *SLFRS for SMEs* as a way to gain access to finance, the owner-managers did not perceive "easy access to finance" as a benefit of adopting *SLFRS for SMEs*. According to their views, collateral was the main barrier they experienced when attempting to gain access to finance:

> When you listen to budget speeches and press releases and interviews about ministers it's beautiful, it's lovely but I don't see that these people are supporting SMEs to overcome barriers in accessing finance. I do not see even banks doing anything. Even the interest rates are still at 12% and 13%. They take all your assets to give something. I don't hear any bank give anything without proper collaterals or taking over assets. I can increase the capacity if I have another cool room. Now to put up another cool room I need at least Rs3.5million. The bank cannot fund me Rs3.5 million because they are asking me to come up with some sort of a collateral. The amount I earn is sufficient for me and for the workers but to do something new and more and bring down more money to this country, why do I have to suffer so much? Do I have to surrender my hard-earned land or the house to get that? I'm not ready to do that (Owner-manager 11).

> I think you should publish this. Banks will give loans on jewellery, vehicles or on houses or property but will not give loans based on a person's skill. They do not even consider what we have as securities. The government should look at the nature of the business and recognise something that can be used as security. For instance, a 'mould' that we have will not be considered as security but we have invested in it. The ministry of industries gives loans with interest concessions. This got approved for us but when we approached the bank they wanted us to produce some form of security such as properties (which we do not have). To run the business what we need is working capital. We are stuck looking for working capital. Though facilities exist, getting these facilities is not easy (Owner-manager 09).

The need for collateral appears to be a major obstacle for SMEs in Sri Lanka as the banks largely adopt collateral-based lending to SMEs. The issue of collateral-based lending to the SME sector is also evident from a representative of government institution, who reports:

> Access to finance is the biggest issue for SMEs as banks require them to produce collateral when they grant loans. They are not shifted from still that traditional banking to development banking. The government has to take some initiatives, still implementation

> side is lagging from banking side. Through the last budget, government also took some actions to solve this issue to some extent right. We proposed to develop the guarantee fund. Government gives the guarantee on behalf of the SME, if he or she or fails to repay the loan, we pay that loan to some extent 75% or something. We made a proposal to develop that government guarantee scheme. Based on that proposal we discussed with the ADB also and they agreed to support that development fund (Government institution 01).

The International Accounting Standards Board (2009a, p. 16) believes that the consistent application of a global financial reporting standard improves the comparability of financial information, which in turn would result in improvement in the "efficiency of allocation and pricing of capital". However, none of the interviewees identified comparability of financial information as a benefit of *SLFRS for SMEs*.

9.7 Summary

This chapter presents the findings of the qualitative data obtained through interviews. As with previous SME financial reporting studies, the range of user groups of SME financial information is found to be limited in number. It is apparent that legal compliance is the main driver for preparation of financial statements by SMEs. The Inland Revenue Department is identified as one of the main users of SME financial information. Apart from Inland Revenue Department, other main users of SME financial information as perceived by owner-managers, accountants and standard setting authority of Sri Lanka, are owner-managers, and banks. Responses by bank lending officers and income tax officers confirm that they use SME financial information for their decision-making. Owner-managers perceived government institutions also use SME financial information.

The financial information requirements of those user groups are varied, depending on their decision-making purposes. However, it was surprising that the decision usefulness of SME financial statements for bank lending and income tax purposes were limited. Bank lending officers and income tax officers do not rely on SME financial statements to meet their information needs. Both have a major concern over the credibility of SME financial statements. They believe accounting figures in the SME financial statements are adjusted to minimise the tax obligation. The quality of the auditors and accountants, who provide services to Sri Lankan SMEs, are a major concern of both user groups. Additionally, it was surprising to find that bank lending officers do not find the auditor's report useful in their decision making. However, bank lending officers prefer audited financial statements but only if audited by a reputable audit firm. Similarly, income tax officers have concerns about the quality of SME financial statements prepared by non-chartered accountants. Thus, the competency of accountants and auditors appears to have a significant impact on the quality of SME financial statements. Bank lending officers and income tax officers tend to obtain additional information from SMEs before they make decisions concerning the SMEs affairs.

It appears that the major sources of financial information used in lending decisions to SMEs are related to profitability, cash flows, and gearing. However, bank lending officers generally obtain financial information by interviewing the owner-managers and paying site visits to the companies. Income tax officers ask for additional detailed financial information from SMEs and obtain other information from various sources such as suppliers, customers and their internal databases.

SME owner-managers believe that statutory financial statements are not useful for making business decisions when compared to management information. This is because financial statements are prepared with tax motivation and thus, do not provide the true picture of the business entity. A lack of accounting knowledge among owner-managers and the outdated financial information in the financial statements were also referred to as impediments to decision making. The Profit and loss statement was deemed to be the most useful financial report as they use it for estimating income taxes. There appears to be a low or no separation between ownership and control of SMEs. Therefore, owner-managers are involved in the management and day-to-day operations of the entity. They have access to entity's internal financial data and thus, do not depend on the financial statements to make business decisions.

Global accounting standards for SMEs was not well perceived by owner-managers and accountants of SMEs. However, owner-managers and accountants who are members of CASL perceive global accounting standards are useful and had adopted them for their financial reporting. Owner-managers reveal that most of the cross-border activities such as foreign exports, foreign ownerships, and foreign borrowing are of little relevance to SMEs. Lack of resources, lack of capabilities, and lack of assistance and incentives from the government are seen as barriers preventing them engaging in international activities. Foreign imports are the most relevant international activity. However, foreign suppliers do not request for internationally comparable accounting information from SMEs. Therefore, owner-managers and accountants do not perceive any benefit from producing internationally comparable accounting information. They perceived it as a burden imposed on them.

Findings reveal that the standard setter in Sri Lanka did not receive sufficient comments on the exposure draft of *SLFRS for SMEs* from the users of SME financial information during the review process of the accounting standard. It was apparent that the standard setter did not attempt to obtain comments on the *SLFRS for SMEs* from the government institutions responsible for making policies for the SME sector in Sri Lanka before adopting the accounting standard in Sri Lanka. The standard setter received technical assistance from the IASB and foreign aid from international donor agencies to implement *SLFRS for SMEs* in Sri Lanka. Discussions with the representatives from the standard setter reveal that they conducted workshops and seminars for SME owner-managers, accountants, bank lending officers and income tax officers on the *SLFRS for SMEs*. However, owner-managers, accountants, bank lending officers, and income tax officers are still unaware and have limited knowledge about the *SLFRS for SMEs*.

Owner-managers believe that they were not in a good position to assess the costs and benefits of *SLFRS for SMEs* because they were unaware of or have limited knowledge about the financial reporting regulations and accounting standards. However, there is a general agreement among owner-managers that the main costs of the application of *SLFRS for SMEs* are related to accounting and auditing fees. Many SMEs do not have the in-house accounting expertise and use external accountants to prepare financial statements in compliance with *SLFRS for SMEs* and for filing tax returns. Fair value accounting is a concern for SME accountants when preparing financial statements compliance with *SLFRS for SMEs*. Income tax officers suggest the use of fair value concept in the *SLFRS for SMEs* make it impractical in Sri Lanka. Further, income tax officers are not in a position to assess the quality of the valuers due to absence of a database of qualified valuers in Sri Lanka.

The standard setter believes that adoption of the *SLFRS for SMEs* would give credibility to SME financial statements and ease access to finance. However, many owner-managers and accountants are not convinced of benefits derived from preparing financial statements in accordance with *SLFRS for SMEs*. Owner-managers do not perceive adoption of the *SLFRS for SMEs* would ease access to finance, as the lack of collateral is the major obstacle for getting access to finance. Similarly, one representative of the government institution believes that collateral-based lending is the major barrier for SME trying to access finance. Income tax officers and bank lending officers assert that if SMEs apply the *SLFRS for SMEs*, they cannot get the information they require. Overall, there was a general consensus among owner-managers, bank lending officers, income tax officers, and representative of government institutions of Sri Lanka for simplified financial reporting requirements for SMEs rather than unmodified implementation of the *IFRS for SMEs*. The next chapter presents the discussion of findings from both the questionnaire survey and interviews.

CHAPTER TEN

DISCUSSION

10.1 Introduction

The purpose of this chapter is to discuss the combined results of the two different research methods to explore answers to the following two research questions of the study: How do Sri Lankan users and their information needs differ regarding size of SMEs? and Do Sri Lankan SMEs need internationally comparable financial information? A financial reporting framework for Sri Lankan SMEs is developed based on the findings discussed in this chapter and will be set out in Chapter 11.

The chapter is organised as follows. Section 10.2 discusses the institutional pressures influencing Sri Lanka's decision to adopt the *IFRS for SMEs*. Section 10.3 and 10.4 discuss the findings regarding Sri Lankan SME users and their financial information needs, using results from both the quantitative and qualitative data. Section 10.5 investigates the relevance of *SLFRS for SMEs* to Sri Lankan SMEs considering the need for internationally comparable accounting information, the relevance of the specific topics and the cost-benefit issues. Section 10.6 concludes the chapter.

10.2 Institutional pressures on the adoption of *IFRS for SMEs* in Sri Lanka

Institutional pressures, such as coercive, normative, and mimetic pressures, have been seen to influence the adoption of *IFRS for SMEs* in other countries. The adoption of the *IFRS for SMEs* in Sri Lanka is examined at both country and firm level to see how and if these pressures are evident.

Coercive pressures

Accounting systems of Sri Lanka were greatly influenced by the British who created the Crown Colony. However, subsequent development in the accounting system were directly subject to internatonal influences such as the World Bank and the International Monetary Fund (IMF). Sri Lanka joined the World Bank in 1950, and since then the World Bank's assistance is aimed at helping Sri Lanka reach its development goals and provides financing and technical help (World Bank, 2005). The World Bank's current portfolio in Sri Lanka consists of 18 projects with a total net commitment value of USD2.1 billion (World Bank, 2017). The –26-year civil war that ended in 2009 was one of the main reasons for Sri Lanka's high dependence on foreign aid. Indeed, in per capita terms, Sri Lanka became the world's leading aid recipient (Arunatilake et al., 2001).

In return for their financial assistance, the World Bank and the IMF insisted on certain financial reporting practices to be complied with. For example, the IMF announced that the second review of the loan disbursement reached a staff-level agreement with Sri Lankan authorities subject to submission of a new Inland Revenue Act to the Parliament by June 2017 (World Bank, 2017). However, the most direct influence to adopt the International Financial Reporting Standards (*IFRS*) came from the World Bank. The World Bank directly coerced changes by forcing the standard setter in Sri Lanka to adopt the *IFRS* as promulgated by the IASB. The World Bank pushed the Institute of Chartered Accountants of Sri Lanka (CASL) to adopt the *IFRS* through the "*Review of accounting and auditing frameworks in Sri Lanka*" (World Bank, 2004, p. 14).

Interview results reveal that the standard setter received a grant from the World Bank to implement some of the key recommendations of their review and to facilitate the adoption process of *IFRS for SMEs* in Sri Lanka. This observation is consistent with Irvine (2008) and Mir and Rahaman (2005) who claim that the decision to adopt *IFRS* would not be driven by the needs of local organisations and the suitability of *IFRS* for local companies, but would rather imposed on them by international organisations such as the Asian Development Bank, IMF and the World Bank (Irvine, 2008; Mir & Rahaman, 2005).

Besides the World Bank, the standard setter also received pressure from the IASB to adopt *IFRS for SMEs*. Interview findings reveal that the standard setter received technical assistance from the International Accounting Standards Board (IASB) for *IFRS for SMEs*. One board member of the IASB and the chairman of the SME implementation group conducted workshops and training sessions on *IFRS for SMEs* to preparers and auditors of SME financial statements in Sri Lanka.

Developing countries, such as Sri Lanka that have been experiencing pressure from the World Bank, may be reluctant to resist the efforts of the IASB to promote *IFRS for SMEs*. The IASB's project on *IFRS for SMEs* has been criticised for lack of input from developing countries in the discussions leading to the formulation of the standard (Bohušová & Blašková, 2012; Chand & Cummings, 2008; Devi & Samujh, 2014; Singh & Newberry, 2009). Therefore, it is reasonable to believe that the IASB excluded consideration of the position of SMEs in most developing economies. Thus, the process used to persuade countries to adopt the *IFRS* issued by the IASB is argued as being more about political and social dimensions of globalisation than it is about the alleged economic benefits of *IFRS* convergence (Chua & Taylor, 2008; Rodrigues & Craig, 2007).

The above explanation is consistent with the institutional account of coercive isomorphic pressure (DiMaggio & Powell, 1983; DiMaggio & Powell, 1991). DiMaggio & Powell (1983) argue that isomorphic pressures can occur in a coercive manner and could emerge from formal and informal pressures exerted on organisations by powerful players upon which weak organisations are dependent. There is evidence to suggest that international organisations have used foreign aid and loans as a coercive mechanism to push for accounting harmonisation in less developed countries (Irvine, 2008; Joshi & Ramadhan, 2002; Mir & Rahaman, 2005; Sharma & Lawrence, 2008; Sharma et al., 2014). Sri Lanka was dependent on international donor agencies such as World Bank for financial assistance. Therefore it becomes apparent that Sri Lanka's decision to adopt *IFRs for SMEs* was primarily due to coercive pressure stemming from resource dependence (DiMaggio & Powell, 1983; Lawrence et al., 2009; Mir & Rahaman, 2005; Oliver, 1991; Sharma et al., 2010, 2014; Tsamenyi et al., 2006). The World Bank became a source of coercive pressure for the adoption of *IFRS for SMEs* in Sri Lanka, as has been the experience in other countries; for example in Jordan (Al-Omari, 2010), in United Arab emirates (Irvine, 2008) and in Bangladesh (Mir & Rahaman, 2005). It is also apparent that the standard setter was under pressure from the IASB to accept *IFRS for SMEs.* Barbu and Baker (2010) and Irvine (2008) claim that the IASB pressurises countries around the world to adopt the *IFRS.*

Following the pressures from the World Bank and the IASB, CASL was the next influential player who exerted coercive pressure on SMEs to adopt *IFRS for SMEs*. In its capacity as the country's sole authority in promulgating accounting and auditing standards, the CASL made a decision to converge fully with on accounting standards and all pronouncements issued by the IASB. Accordingly, CASL decided to adopt *IFRS for SMEs* as "Sri Lanka Accounting Standards for Small and Medium Entities" (*SLFRS for SMEs*) without any modification. This reinforces the theory that coercive pressures are exerted through rules and regulations set up by regulatory agencies, such as accounting and audit standard-setting institutions (Boolaky & Soobaroyen, 2017).

The standard setting process is not transparent and seems to be dominated by the partners and members of the Big Four audit firms in Sri Lanka. This could be because CASL is predominantly represented by the partners and managers of Big Four audit firms in Sri Lanka and they utilise their authority in the council to make decisions on accounting standards (Yapa et al., 2017). The interview findings disclose that the standard setter did not encourage nor consult government institutions that are directly involving in setting policies to the SME sector, to participate in this process. There appears to have been very little consultation with various interested parties before adopting the *IFRS for SMEs* in Sri Lanka. Intended user groups of *IFRS for SMEs* did not take part in the review process of the accounting standard. Sri Lankan culture, which does not question the higher authority, provides a reason for the low responses to the exposure draft issued by CASL. Evidence indicates that government intervention into accounting standard setting in Sri Lanka is low.

Normative pressures

Small and mid-tier audit firms who provide accounting and auditing services to SME clients also appear as influential players on SME decision to adopt *IFRS for SMEs*. This result is consistent with the findings from Jones and Higgins (2006) that show external auditors are rated as the most important party to be involved in the *IFRS* implementation process. Professional accountants played a significant role in the implementation of market-oriented public sector practices in Fiji (Sharma &

Lawrence, 2005), and were instrumental in the adoption of international accounting standards in Bangladesh (Mir & Rahaman, 2005). There is consensus in the literature that the Big Four accounting firms play an important role in the globalisation of accounting and represent the normative pressures within the accounting society (Al-Omari, 2010; Irvine, 2008). However, small and mid-tier audit firms prepare and audit most SMEs' financial statements in Sri Lanka (Wickramasinghe, 2015; Yapa et al., 2017). The findings from the interviews indicate that small and mid-tier audit firms influenced and advised SMEs to adopt *IFRS for SMEs* for their financial reporting. This is because auditors work closely, as advisors, with the SME accountants when preparing SME financial statements in compliance with *IFRS for SMEs*. When the audit firms make a recommendation to adopt international financial reporting standards, SMEs see it as something to comply with to be able to survive. For these reasons, it could be argued that small and mid-tier audit firms exert normative institutional pressure on Sri Lankan SMEs to adopt *IFRS for SMEs*.

This finding is consistent with research by Joshi and Ramadhan (2002), Albu et al. (2011), and Chua and Taylor (2008) who argue that the external auditor is the most dominant party involved in the *IFRS* adoption process. DiMaggio and Powell (1983) identify professionals as key sources of normative isomorphic pressures. This pressures arises from fulfilling professional expectations or adopting practices that matches with group norms (DiMaggio & Powell, 1991). Normative isomorphism occurs when the norms of society and professional bodies influence the practices of organisations (Scapens, 2006). In Sri Lanka, the professional bodies influence the practices of SMEs through the actions of the auditors.

It was interesting to note that firms which were owned and managed by members of CASL and had members of CASL in the position of accountant adopted *IFRS for SMEs* for their financial reporting. This is because owners could exert both coercive and normative pressure to adopt *IFRS for SMEs*. On one hand, owners act as powerful stakeholders upon whom the organisation is dependent (Deegan & Samkin, 2013) and on the other hand, fulfil their obligation through professional membership (Carpenter & Feroz, 2001; Touron, 2005). Their opinions, and resultant actions, may be influenced by their desire to maintain professional membership of a recognised accounting body (Carpenter & Feroz, 2001; Touron, 2005). It is claimed that professional institutions have influences to disseminate norms, influence the field and otherwise direct other members (Tuttle & Dillard, 2007).

Mimetic pressures

Mimetic institutional pressures refer to the copying and duplicating of successful organisational behaviour by other organisations (DiMaggio & Powell, 1983). Prior research (see, for example, Hassan et al., 2014; Irvine, 2008; Judge et al., 2010) presents evidence that mimetic isomorphism, as a result of emulating other countries, predicts *IFRS* adoption. Research (see, for example, Hassan et al., 2014; Irvine, 2008) also notes relationships with the country's trading partners had on *IFRS* adoption. However, findings of this thesis does not support the mimetic institutional pressures both in the Sri Lankan and the SME contexts. Since Sri Lanka is one of the first countries to decide the adoption of *IFRS for SMEs*, there are no reasonable evidence to support a proposition that the adoption decision is influenced by other developing countries in the region.

Findings from both the questionnaire survey and interviews reveal that international activities are of minor importance for most of SMEs. Despite the relevance of exports and imports to large SMEs, about half of them do not receive any requests from their trade partners to provide internationally comparable accounting information. The probable reason for this finding is that nine countries (USA, Germany, Italy, Belgium, Netherland, France, India, China, and Japan) of the top 12 trading countries of Sri Lanka did not adopt the *IFRS for SMEs*. Therefore, it is argued that the decision to adopt *IFRS for SMEs* is not influenced by the trade partners of Sri Lanka.

Similarly, an SME's decision to adopt *IFRS for SMEs* is not likely to be influenced by other SMEs in the same field. SME business practices are rarely visible to public and their financial statements are not publicly available. As a result, SMEs do not tend to copy accounting practices of their competitors. For these reasons, mimetic pressures are not be evident in Sri Lanka.

In summary, the coercive pressures are the strongest factor which drove the adoption of *IFRS for SMEs* both at country and individual firm levels. Specifically, coercive pressures from the World Bank and the IASB on Sri Lanka and coercive pressures from the CASL on individual SMEs are apparent from the findings of this thesis. Coercive institutional pressures are the most obvious, since in an institutionalised environment there is an "elaboration of rules and requirements" including "pressures for conformity to public expectations and demands" (Oliver, 1991, p. 101). Normative pressures seemed to occur at the individual organisational levels from small and mid-tier audit firms in Sri Lanka. No mimetic influences were identified at both country and SME levels.

Notwithstanding the institutional pressures exerted on individual organisations, results from the questionnaire survey and the interviews reveal that actual adoption of *SLFRS for SMEs* is low. One possible reason is that the *SLFRS for SMEs* is relatively a new accounting standard for SMEs. Another reason is that the *Companies Act No.7 of 2007* of Sri Lanka does not include a simplified financial reporting framework for SMEs (Wickramasinghe, 2015, p. 56). The World Bank recommended amendments to the requirements of the *Companies Act No.7 of 2007* to include a differential financial reporting framework defining categories of companies and prescribe the accounting and auditing review requirements for each category (Wickramasinghe, 2015, p. 56). However, due to the absence of an effective implementation of legal and institutional framework, the adoption of *SLFRS for SMEs* is not likely to result in increasing transparency and accountability in Sri Lanka.

10.3 Users of Sri Lankan SME financial information

When developing the International Financial Reporting Standards for SMEs (*IFRS for SMEs*), the IASB identified various user groups such as shareholders, creditors, employees and the public as main users of SME financial information (International Accounting Standards Board, 2009b, p. 7). In justifying their position, the IASB argues that the information needs of users of SME financial statements are similar in most ways to those of users of publicly accountable entities' financial statements (International Accounting Standards Board, 2004). However, it is claimed by researchers, that SME users and their financial information needs are rarely connected to evidence although, they have emerged through a consultative process over time (Coetsee, 2010; McCartney, 2004; Young, 2006).

It has been claimed that users of SME financial information differ from the users of large companies' financial information (Devi & Samujh, 2015; Di Pietra et al., 2008; Evans et al., 2005). Confirming this notion, the findings from both the questionnaire survey and interviews of this study indicate that the main user groups of Sri Lankan SME financial information are owner-managers, banks and the Inland Revenue Department. Banks have been identified as one of the main users of SME financial information since they are the main capital providers to the SME sector in Sri Lanka. The Inland Revenue Department is also a main user of SME financial information as they require SMEs to provide their financial statements together with the annual tax returns for assessment of income taxes. This finding concurs with the literature (Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Page, 1984).

However, According to the findings from the questionnaire survey, government institutions are a main user group of SME financial information reported by the large SMEs (40 to 99 employees). This finding differs to the research findings from developed countries (Collis & Jarvis, 2000; Sian & Roberts, 2009) but is consistent with one developing country study (Dang-Duc et al., 2006). Sian and Roberts (2009) find that government institutions are not important users of UK SME financial information. However, in a Vietnam study, Dang-Duc et al. (2006) ascertain the main use of SME financial information was for taxation and administrative purposes by the government agencies. The interviews with owner-managers and accountants of Sri Lankan SMEs reveal that they have to provide financial information to government institutions in certain circumstances.

SMEs are required to provide financial information to government institutions when they supply and/or sell goods and services to them. Moreover, discussions with the representatives from two government institutions that make policies for the SME sector confirm that they use financial information when they administer specific loan schemes that are funded by the World Bank and the Asian Development Bank. Sri Lanka receives foreign aid from agencies such as the World

Bank and the Asian Development Bank and they do require certain standards of financial accountability from their aid recipients (Mir & Rahaman, 2005; Singh & Newberry, 2009). For an example, when the World Bank provided funding for development projects in Fiji and it was conditional upon annual audited reports being submitted to the World Bank (Lawrence et al., 2009).

In contrast to the IASB's views, findings from both the questionnaire survey and the interview data reveal that suppliers, customers and employees are not important users of Sri Lankan SME financial information. Similarly, Sian and Roberts (2009) conclude from their research that SMEs do not report their financial information in order to satisfy the needs of customers and suppliers. Non-manager owners were also not identified as an important users of Sri Lankan SME financial information, an observation which supports the findings of others' research (Collis & Jarvis, 2000; Dang-Duc et al., 2006; Di Pietra et al., 2008; Evans et al., 2005). This is not unexpected because most SMEs are owner managed and the management and ownership in SMEs is rarely separated (Collis & Jarvis, 2002; Eierle & Haller, 2009). This finding confirms that in Sri Lanka the role of financial statements in stewardship reporting is less relevant to SMEs.

None of the literature to date reports on research that analyses users and their needs for SME financial information based on entity size. Following analysis of the data generated from the questionnaire survey in three size categories, it is revealed that the number of users identified become less as the size of the SMEs decrease. Results show that the small SMEs (5-15 employees) have a much fewer number of users than the medium and large SMEs. This implies that the preparation of financial statements in accordance with complex accounting principles is unnecessary and costly for small SMEs. Small SMEs' financial information is mainly used by owner-managers and banks. The Inland Revenue Department was not identified as a user of financial information of small SMEs. The probable reason for this is that for many small SMEs, financial statements are prepared and sent directly to the Inland Revenue Department by their external accountants. Discussions with owner-managers and accountants further confirm that the Inland Revenue Department is a user of SME financial information, irrespective of the size of the business. Medium SMEs (16-39 employees) identify owner-managers, banks and the Inland Revenue

Department as the main users of financial information. Large SMEs identify owner-managers, banks, the Inland Revenue Department and government institutions as the main users of financial information.

Overall, the findings regarding users of SME financial information do not agree with the IASB's list of users identified in the *IFRS for SMEs* (International Accounting Standards Board, 2009b). The numbers of users of SME financial information are few, probably as there is no statutory requirement for public disclosure for SME financial information in Sri Lanka. These findings indicate that the needs of owner-managers and tax authorities should be taken into consideration in the standard-setting process. Since owner-managers and the Inland Revenue department are the main users of Sri Lankan SME financial information, the general purpose financial reporting model is deemed to be inappropriate for SME financial reporting in Sri Lanka. This raises an important question about the relevance of the existing conceptual framework for SME financial reporting in Sri Lanka since it is largely based on the large and/or listed companies' template (Devi & Samujh, 2014; Di Pietra et al., 2008; Evans et al., 2005).

10.4 Uses of SME financial information

The decision-usefulness objective of financial reporting suggests that financial reporting should provide useful information for users to help them make their decisions (International Accounting Standards Board, 2009b). General purpose financial information is based on the presumption that users need similar information. If these users do not consider financial statements useful and reliable, then reporting has no value. The principal users of SME financial are; owner-managers, bank lending officers and income tax officers. The findings of their uses of SME financial information are discussed here.

10.4.1 Use of SME financial information by owner-managers

The primary objective of preparing SME financial statements as perceived by owner-managers is to meet the legal requirements, particularly for taxation. It was further revealed from the discussions with owner-managers that accounting figures provided in the financial statements are altered in order to minimise the tax liability.

Because the figures may not show the real financial situation, using information provided to tax authorities for making business decisions is limited. Lack of accounting knowledge, and lack of detail and up-to-date financial information are also found to be reasons for not depending on the financial statements for decision making.

The income statement is perceived to be the most useful financial report. Estimating income tax liability was the reason for the popularity of income statements among owner-managers. This again confirms that tax reporting is the primary objective when preparing SME financial statements. Consequently, it appears that a balance sheet focused conceptual framework for accounting is not appropriate for Sri Lankan SMEs. Findings from both the questionnaire survey and interviews with owner-managers reveals that management information is useful for making business decisions. The reason for this is that the most SMEs are owner managed and thus, owners can get easy access to internal records and management reports of the business. The owner-manager characteristic implies that the owners can observe the behaviour of any employee on a daily basis (McMahon & Stanger, 1995). Collis and Jarvis (2000) assert that most SME owners or shareholders have access to financial information for controlling and monitoring purposes, a situation which makes the stewardship role of financial reporting to owners “redundant”. However, in the IASB’s accounting standard *IFRS for SMEs*, the stewardship role of financial statements is designed to show the results of the stewardship of management for the resources entrusted to management (International Accounting Standards Board, 2009b). It is claimed that stewardship plays an important role in information dissemination when the owners are not the managers of the entity (Mala & Chand, 2015). However the stories shared by the owner-managers confirm that the role of financial statements in stewardship reporting is less relevant to SMEs as there is no separation between ownership and control (Collis, 2008; Collis & Jarvis, 2000; McMahon & Stanger, 1995).

From the survey of SMEs, it appears that budgets, management accounting information and bank reconciliation are ranked in the top three most useful management reports. Discussions with owner-managers further confirm the usefulness of bank reconciliations, budgets and other management accounts for making their business decisions. The top three purposes for which owner-managers use SME financial information as found in the questionnaire survey are for planning purposes, estimating income tax liabilities, and taking marketing and pricing decisions. Interview data reveal that owner-managers use financial information mainly to monitor the performance of the business and compare sales, profits and costs with previous periods. Some owner-managers use their financial information to take investment decisions such as investing in land and buildings and deciding on employees' bonuses and salaries.

By contrast, Collis and Jarvis (2000) find that financial information is useful when deciding on directors' pay and bonuses. Further, Collis and Jarvis (2003) claim that owner-managers use financial information for the purpose of budgetary planning, exercising control over company activities and making informed decisions and judgements.

Findings from the questionnaire survey show that the profit and loss statement is the most useful financial report for making business decisions of owner-managers of small and medium SMEs. Whilst the cash flow statement is the most useful financial report for making business decisions of owner-managers of large SMEs. Thus, it appears that owner-managers of small and medium SMEs are more concerned about the profitability of the business while owner-managers of large SMEs are more concerned about the survival of the business. However, discussions with owner-managers reveal that internally generated cash flow reports are useful sources of decision making regardless of the size of the SME. This demonstrates the importance placed on managing liquidity, as it is critical to the success and survival of a SME (Collis & Jarvis, 2002; McMahon & Stanger, 1995).

10.4.2 Use of SME financial information by bank lending officers

Research conducted in developed countries establishes that financial statements plays an important role in bank lending decisions (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000; Maingot & Zeghal, 2006; Page, 1984). Financial statements are key sources of information in the internal rating process of German Banks (Zuelch & Burghardt, 2010). Similarly, McMahon (1999) finds that periodic financial statements and future oriented financial statements were provided to financial providers when seeking debt or equity finance by Australian SMEs.

In contrast to the above findings from developed countries, bank lending officers place little reliance on the financial statements of SMEs when making lending decisions. The finding is consistent with Dang-Duc et al. (2008) in Vietnam. Moreover, in line with Dang-Duc et al.'s (2008) study, bank lending officers make site visits and have direct communication with clients to get access to internal financial information. The financial information used in lending decisions to Sri Lankan SMEs relates to profitability, cash flow and gearing. The importance of cash flow, profitability and gearing information in lending decisions was also highlighted in the literature (Berry et al., 1993; Berry et al., 2004; Zuelch & Burghardt, 2010). What is different to the literature, is that bank lending officers have access to and use management information for making lending decisions to Sri Lankan SMEs. It appears not to be so in the UK (Deakins & Hussain, 1994). Consistent with the findings of Gamage (2015), the bank lending officers make their lending decisions to the SME sector largely based on collateral. For this reason, access to bank finance is one of the major concerns among SME owners in Sri Lanka.

In contrast to developed countries such as United States, United Kingdom, and Spain (Baker & Cunningham, 1993; Berry & Robertson, 2006; Duréndez Gómez-Guillamón, 2003) and developing countries such as Jordan (Abu-Nassar & Rutherford, 1996), bank lending officers place little importance on the audited financial statements when making lending decisions to SMEs. This is not consistent with what is reported in the literature. Abu-Nassar and Rutherford (1996) provide evidence that user groups in Jordan place great importance on the information contained in the auditor's report. Similarly, Baker and Cunningham (1993) discover that loan officers in the USA had more confidence in the audited financial statements. However, bank lending officers were concerned about the quality and credibility of the registered auditors and small and mid-tier audit firms in Sri Lanka who provide auditing services to SMEs. As registered auditors are not regulated, not required to comply with Sri Lanka Auditing Standards, nor compelled to undertake continuing professional development their ability to provide reliable audits is questionable (Wickramasinghe, 2015).

Additionally, there seems to be significant skill gaps and concerns about the ability of many Sri Lankan small and mid-tier audit firms to comply with the requirements of the international financial reporting standards and international auditing standards (Wickramasinghe, 2015; Yapa et al., 2017). For these reasons, bank lending officers prefer financial statements audited by reputable audit firms such as the Big Four audit firms in Sri Lanka. Bank officers place little reliance on financial statements to monitor loans. This finding is significant as although the literature shows financial statements play an important role in lending decisions, there is no evidence in the literature that financial statements are used to monitoring borrowing.

10.4.3 Use of SME financial information by income tax officers

Income tax officers do not depend on the SME financial statements for assessing income tax. Credibility of the SME financial statements and inadequate detailed information in the financial statements were seen as major reasons for low reliance on SME financial statements for calculating tax liabilities. The credibility of accountants who provide accounting and auditing services to SMEs was also a major concern of income tax officers.

As income tax officers have the power to obtain additional information for their tax assessments, the findings indicate that income tax officers obtain additional detail financial information about turnover, expenses, creditors and debtors from SMEs when they submit their annual tax return. Income tax officers compare an entity’s financial information with other SMEs in the same industry to reveal any abnormal findings, as they are aware about the industry trends and mark ups.

By contrast, research by the International Federation of Accountants (2006) and Barker and Noonan (1996) establish the major uses of SME financial statements by the tax authorities include determining gross profit, assessing directors’ fees and expenses, and to see whether a company’s financial statements were accompanied by a qualified auditor’s report.

In summary, it appears from the findings of this thesis that there exists less decision-usefulness of SME financial statements for owner-managers, bank lending officers and income tax officers. These user groups do not depend on financial statements as a basis for their decision-making. They have the ability to acquire, or access to, additional financial information of SMEs when they made decisions. Financial statements do not appear to play an important role in the management of SMEs as owner-managers acquire internal financial information easily and in a more timely manner. Therefore, the findings reveal that one set of general purpose financial statements is not appropriate to satisfy the diverse user needs.

The findings of this study reveal that SME financial reporting practices are aimed at reducing companies' tax liability. SMEs avoid taxes by adjusting figures in the financial statements. SMEs maintain separate records and different documents for different purposes and submit them as 'appropriate' for private and governmental purposes. Consequently, financial accounting information does not reflect true financial performance and position when SMEs are attempting to reduce payments on taxes.

Consequently, bank lending officers and income tax officers perceive financial reporting by SMEs to be unreliable. Inadequate legal and institutional frameworks in Sri Lanka (Freedom House, 2013) worsen the situation. The culture makes it difficult to implement accounting standards such as the *SLFRS for SMEs* in Sri Lanka. Adoption of the *IFRS* is complicated by lack of regulation and lack of enforcement within a culture of secrecy and fraud (Albu et al., 2011).

10.5 Relevance of international financial reporting standards for Sri Lankan SMEs

The IASB's arguments about the need for the *IFRS for SMEs,* and the standard itself have been the subject of considerable debate (see, for example, Aboagye-Otchere & Agbeibor, 2012; Chand et al., 2015; Devi & Samujh, 2015; Di Pietra et al., 2008; Eierle & Haller, 2009; Evans et al., 2005; Kiliç et al., 2016; Singh & Newberry, 2009). Unique characteristics, different conditions and different transactions encountered by different countries are not conducive to a global set of accounting standards for the SME sector. The following sub sections discuss perceptions of respondents to the questionnaire survey and interviews on the relevance of the *SLFRS for SMEs* to Sri Lankan SMEs.

10.5.1 Need for internationally comparable accounting information

In its 'basis for conclusions' to the standard, the IASB argues that the need for global SME financial reporting standards arises out of the international structures and activities of SMEs and their financial statement users (International Accounting Standards Board, 2009a, p. 16). When considering the financial reporting needs of private entities, the IASB (2009a) further argues that the benefits of global financial reporting standards are not limited to entities who participate in the public capital markets. Demand exists for cross-country comparability of SME financial statements due to multinational and cross-border lending, multinational trading, global credit rating and global investing in SMEs (International Accounting Standards Board, 2009a, p. 16). It is claimed that entities that undertake international activities may find the compliance with internationally accepted standards advantageous in increasing the reliability of their financial statements (Guerreiro et al., 2008; Murphy, 1999). Consistent with the IASB's view, Murphy (1999), indicates that implementation of international reporting standards is beneficial for those entities having a wide range of decision makers. However, findings from the literature on the need of internationally comparable accounting information for SMEs produce mixed results.

In contrast to the IASB's view, most respondents to both questionnaires and interviews do not support the need for internationally comparable accounting information for Sri Lankan SMEs. The finding of this study is consistent with the research conducted by Eierle and Haller (2009), the Conseil National de la Comptabilité (2008), and Aboagye-Otchere and Agbeibor (2012) but contradicts Mazars (2008), who discovers great support for international financial reporting information in Germany and France.

The negative perception of owner-managers and accountants towards internationally comparable financial information may be because the majority of Sri Lankan SMEs are purely domestically based and financed locally. The literature supports the contention that there is no benefit for entities that operate locally to follow *IFRS for SMEs* (Chand et al., 2015; Devi & Samujh, 2014, 2015; Lungu et al., 2007). Entities that try to obtain financing from international banks and other international financial institutions find it beneficial to comply with international reporting standards (Dumontier & Raffournier, 1998). The most relevant international activity for Sri Lankan SMEs was foreign imports as indicated by 21% of survey respondents and most owner-managers interviewed. Despite the various support services and development programmes provided by government departments, limited capacity, limited resources, and lack of government support and incentives were referred to as barriers for expanding SME business operations globally. Consistent with Samujh (2011), SME owner-managers surveyed in this thesis indicate that their primary concern is the survival of the business rather than the growth of the business.

In accord with the study conducted by Eierle and Haller (2009) in Germany, this thesis establishes an entity’s size as well as its level of international activities have an impact on an entity's need to provide internationally comparable accounting information. Comparatively, large SMEs reveal more cross-border activities and indicated a higher need to provide internationally comparable accounting information than do small SMEs. However, German SMEs have considerably more cross-border activities (foreign exports and foreign imports) than SMEs in Sri Lanka. Apart from foreign imports and exports, other foreign activities such as foreign ownership and borrowings are not relevant for most large Sri Lankan SMEs. Despite the export and import activities of large SMEs, about half of the responding entities do not see any need to provide internationally comparable financial accounting data. This is because foreign suppliers and customers do not request the information as envisaged by the IASB. Rather, they obtain information through their local agents, and company web sites and ask for bank guarantees. Regardless of the size of the SME, foreign ownerships and borrowings have no relevance to the majority of Sri Lankan SMEs. Therefore, the emphasis on international accounting standards due to international structures and activities is not a priority for them, because only a small percentage of SMEs have a global focus.

10.5.2 Relevance of the specific topics covered in the *SLFRS* for *SMEs* to Sri Lankan SMEs

In developing the accounting standard *IFRS for SMEs,* the IASB started from the full *IFRS* and omitted issues that were not relevant to SMEs (International Accounting Standards Board, 2009a). The IASB claimed that it considered addressing only those issues and transactions that were of general relevance for SMEs to restrict the size and complexity of the accounting standard (International Accounting Standards Board, 2009a, p. 13). However, the IASB's efforts in this direction were criticised. For example, Van Wyk and Rossouw (2009) found that some of the topics were only "partially applicable" to SMEs and SMEs were not necessarily involved in the industries to which these topics referred. Furthermore, certain aspects of impairment of assets, related party disclosures, intangible assets, government grants, non-current assets held for sale and discontinued operations, foreign exchange rates and employee benefits are not applicable to SMEs (Van Wyk & Rossouw, 2009). Similarly, Aboagye-Otchere and Agbeibor (2012) establish that more than two-thirds of the accounting issues addressed in the *IFRS for SMEs* are of little or no relevance to SMEs in Ghana.

Consistent with studies conducted in developing countries (Aboagye-Otchere & Agbeibor, 2012; Van Wyk & Rossouw, 2009), findings of this thesis also reveal that most of the topics addressed in the accounting standard *SLFRS for SMEs* were not relevant to Sri Lankan SMEs. For the majority of the survey respondents, the topics on investment in non-listed companies, investment in listed companies and joint ventures have never occurred in their businesses. The typical SMEs in Sri Lanka do not operate in a group structure, nor do they invest directly in other businesses. Generally they are not diverse, but limited to a single product line or business purpose. Furthermore, topics related to foreign currency transactions such as foreign exchange risk resulting from a customer order or a supplier, and foreign exchange rate loans and borrowings, appear as less relevant to Sri Lankan SMEs. This is probably because Sri Lankan SMEs have few, if any, cross-border activities such as foreign ownership and borrowings. These topics should be considered for omission from the *SLFRS for SMEs*.

The IASB's efforts to omit topics that were irrelevant, or of little relevance, to SMEs are not fully reflective of the financial reporting needs of Sri Lankan SMEs. This is because IASB failed to address the needs and positions of developing countries when developing the *IFRS for SMEs* (Singh & Newberry, 2009). The findings of this thesis agree with the opponents to the *IFRS for SMEs* who questioned whether the IASB had given sufficient attention to the position of SMEs in developing countries (Chand et al., 2015; Devi & Samujh, 2014, 2015; Ram & Newberry, 2013; Singh & Newberry, 2009). While the IASB considers the needs of developed countries, developing countries have specific needs, which may not have been considered by the IASB. Results of this research agree with Di Pietra et al. (2008) who comments that standards for SMEs should not be based on the concepts and principles in the IASB framework and existing standards. Therefore, the IASB needs to consider the relevance of these topics to SMEs in developing countries and provide further simplification to the *IFRS for SMEs*.

10.5.3 Costs and benefits of adopting *SLFRS for SMEs* in Sri Lankan context

This section discusses the perceptions of the owner-managers and accountants of Sri Lankan SMEs regarding the costs and benefits of *SLFRS for SMEs*. Evidence from the questionnaire survey and the interviews helped to identify costs and benefits of adopting *SLFRS for SMEs* in Sri Lanka.

10.5.3.1 Costs of adopting SLFRS for SMEs

In their efforts to address the need for international comparability in the financial reporting of SMEs and to ease the financial reporting burden on SMEs, the IASB issued the *IFRS for SMEs* in 2009. The promotion of *IFRS for SMEs* by the IASB claims that it is equally applicable to all countries. However, *IFRS* adoption is costly to firms since greater effort, knowledge and often new information systems are needed to implement the standard, and the additional efforts are needed to manage the risk of material misstatements appearing in *IFRS* compliant financial statements (George et al., 2013). Hail et al. (2010) argued that *IFRS* reporting costs are particularly burdensome for SMEs. The main costs of the application of *IFRS for SMEs* are related to training accountants and the possible emergence of separate reporting systems for financial accounting and taxation (Albu et al., 2013). The

Institute of Chartered Accountants in England and Wales (2007) suggests that the costs associated with the *IFRS* implementation process comprise: establishing an *IFRS* project team, training other staff such as IT staff, internal audit and management, obtaining external technical advice, taking tax advice, changing software and systems, communicating with third parties, incurring additional external audit costs, renegotiating debt covenants, and obtaining other necessary external data.

Costs of obtaining external technical advice and making payments to accounting and audit firms

The introduction of *SLFRS for SMEs* led to an increase in costs for Sri Lankan SMEs as in other national contexts (Albu et al., 2013; Chand et al., 2015; Laing, 2012; Neag, 2010). However, contrary to the findings of Eierle and Haller (2009), Chand et al. (2015) and, Albu et al. (2013), results from both the questionnaire survey and interviews indicate that the costs of obtaining external technical advice and making payments to accounting and audit firms were the main costs incurred by Sri Lankan SMEs when preparing financial statements in accordance with the *SLFRS for SMEs* (see also, Cameran and Perotti (2014) who found that higher audit fees were paid after moving to *IFRS* by Italian Banks). In the case of the *IFRS* adoption, auditors exert additional efforts to become knowledgeable about the new standards and they assess whether these standards have been appropriately implemented (George et al., 2013). As a result, auditors are likely to recover the cost of this increased effort through an increase in audit fees (Cameran & Perotti, 2014; Charles et al., 2010; George et al., 2013; Ghosh & Pawlewicz, 2009).

One of the main problems faced by developing countries during the adoption of the *IFRS* is accountants' limited knowledge of these standards (Halbouni, 2005). Similarly, there is a lack of knowledge, and expertise on *SLFRS for SMEs* among owner-managers and accountants of Sri Lankan SMEs. Even though CASL claims they had conducted various seminars and workshops on *SLFRS for SMEs* to owner-managers and accountants of SMEs, it appears from the interview results that the majority of SME owner-managers and accountants were not aware of these workshops and thus, did not attend them. Similar points were raised by the income tax officers and bank lending officers. Even accountants who did participate in the workshops have a limited knowledge of the *SLFRS for SMEs*. This raises questions regarding the content, quality, and quantity of seminars and workshops conducted by the CASL for the intended user groups of the *SLFRS for SMEs*. It is doubtful that effective education and implementation of the *SLFRS for SMEs* was achieved in Sri Lanka.

The findings discover differences between adopting and non-adopting entities of *SLFRS for SMEs* according to the size of the entity. Large SMEs are more likely to adopt *SLFRS for SMEs* than small SMEs. A small entity might not have the in-house accounting expertise and therefore needs to rely more heavily on outside accounting expertise resulting in higher fees (Eierle & Haller, 2009). The possible reason for non-adoption of the small SMEs is the scarcity of qualified staff and resources, as well as the higher costs of complying with the standard (Eierle & Haller, 2009; Evans et al., 2005; Institute of Chartered Accountants in England and Wales, 2007; Yang, 2014). Large SMEs are more likely to be able to access qualified staff and resources to implement new accounting standards. Thus, results from this thesis confirm that it is difficult to design one-size-fits-all standards for SMEs (Di Pietra et al., 2008; Eierle & Haller, 2009; Evans et al., 2005).

The findings confirm that there is a lack of qualified accountants in Sri Lanka generally and in SMEs in particular, and that this could lead SMEs to seek advice and assistance from external professional accountants and auditors when preparing financial statements in compliance with *SLFRS for SMEs*. The need to employ professionals is a direct result of the lack of knowledge of *SLFRS for SMEs*, by employees within SMEs. The number of professionally qualified accountants currently working in Sri Lanka are 3461 (Institute of Chartered Accountants of Sri Lanka, 2014a). However, for a country with about 20.4 million people, 3461 accountants is inadequate. Consequently, qualified accountants are in a privilege position to demand higher salaries for their services. As a result, SMEs are unable to hire a qualified accountant as they are unable to offer high salaries for them. The shortage of qualified accountants in Sri Lanka means that the implementation of *SLFRS for SMEs* is problematic.

Audit firms greatly support and provide services for those entities adopting *SLFRS for SMEs.* It appears from the interview results that most of the SMEs' decisions to adopt *SLFRS for SMEs* are influenced by their audit firms (Owner manager 19; Accountant 02). Since, the small and mid-tier audit firms can boost their income by offering services such as training and consultancies on *SLFRS for SMEs,* this could be their primary motivation for supporting *SLFRS for SMEs*. However, Yapa et al. (2017) observed a knowledge gap between the employees of local audit firms such as small and mid-tier audit firms and the Big Four audit firms in Sri Lanka with respect to information technology and international standards. This is because the Big Four audit firms poach qualified and experienced staff from locally established firms (Yapa et al., 2017). As a result, local audit firms face difficulties maintaining their market share and survival in the profession (Yapa et al., 2017). Given that small and mid-tier audit firms are likely to play a key role in shaping financial reporting practices of SMEs, the results signal the need to increase the number and quality of training, workshops and seminars on *SLFRS for SMEs* for local audit firms in Sri Lanka.

Costs of information acquisition and complex calculations

Most respondents to the questionnaire survey indicate that costs of information acquisition such as fair value calculations is another significant cost they have to incur when preparing financial statements in compliance with *SLFRS for SMEs*. This is also supported by the findings from interviews. Interview respondents raised their concern over the complex calculations such as gratuity calculations and use of fair value (Accountant 5, Accountant 6, and owner manager 20).

In most developing countries, fair value is difficult to obtain, due to the absence of an active market for most assets (International Network of Accountants and Auditors, 2007). Other researchers argue that some developing countries do not have the specialists needed to assist in fair value determination, thus potentially undermining the credibility and reliability of information through lack of precision and excessive subjectivity (International Federation of Accountants, 2007; Singh & Newberry, 2009; South African Institute of Chartered Accountants, 2007). Pacter (2007) also outlined concerns associated with the application of fair value accounting in developing countries. These concerns include: inactive market in developing countries; cost of applying recognition and measurement principles; shortage of skilled valuers; government controlled markets; weak regulatory environment; and lack of valuation standards and guidance. Similarly, Kumarasiri and Fisher (2011) claim that Sri Lankan auditors face similar challenges regarding the fair value calculations. Consistent with the above arguments, it appears that fair value determination is difficult in the Sri Lankan context. Also, the need for training or hiring knowledgeable and qualified professionals would increase costs (Taylor, 2009). There is no reliable measurement of fair value available in Sri Lanka because of lack of guidance on measuring methods, non-existence of an active market and lack of skilled and qualified valuers.

Income tax officers also have concerns over the fair value calculations. They raise issues about the subjective elements of fair value calculations. Fair value allows preparers to use their judgment in determining the factors or elements being used in the valuation models. The officers have problems verifying the accuracy and credibility of the figures reported in the financial statements as Sri Lanka does not have an active market or a qualified data base of valuers (Income tax officer 02). The issues raised by the income tax officers in Sri Lanka pose a potential threat to the credibility of financial statements prepared on the basis of fair value. It is clear that fair value is difficult to apply in Sri Lanka.

Due to the complexity and costs of implementing the *SLFRS for SMEs*, most interviewees emphasised the need for a simplified financial reporting framework for SMEs. The need for further simplification to *SLFRS for SMEs* was also indicated by the questionnaire respondents. When they were asked about their perception on the need to provide additional exemptions to the accounting standard *SLFRS for SMEs*, 49 per cent of respondents were unable to comment on it. This was due to their lack of knowledge of *SLFRS for SMEs*. However, nearly 46 per cent of respondents agreed with the need for additional exemptions to *SLFRS for SMEs*. This finding emphasises the lack of understanding and complexity of the *SLFRS for SMEs* for Sri Lankan SMEs.

Both bank lending officers and income tax officers prefer a simple reporting format so they could get accurate financial information. They think that due to the complexity of existing financial reporting frameworks, SMEs are inclined to hide true financial information and depend on external accountants to prepare their financial statements. Many SMEs in Australia and New Zealand do not need to prepare general purpose financial statements. Rather, they prepare special purpose financial reports that comply with taxation regulations developed locally to meet the reporting needs of SMEs in those countries (Devi & Samujh, 2014). Similarly, further simplification is given for South African SMEs that have a public interest score under 100 points (see section 3.6) and whose financial statements are internally compiled. SMEs falling under this category can use their own accounting policies (International Financial Reporting Standards Foundation, 2016). The formulation of such a financial reporting framework, as adopted in these countries, could meet the reporting needs of Sri Lankan SMEs and could benefit the SMEs and the Sri Lankan economy.

10.5.3.2. Benefits of SLFRS for SMEs

The IASB's objectives in issuing *IFRS for SMEs* were to address the need for international comparability in the financial reporting of SMEs, and ease the financial reporting burden on SMEs (International Accounting Standards Board, 2009a). One of the most mentioned merits of the use of *IFRS for SMEs* is the improved comparability of financial statements for SMEs globally (Institute of Chartered Accountants of Sri Lanka, 2012; International Accounting Standards Board, 2009a). There was some disagreement among the questionnaire respondents and interviewees regarding this matter. The questionnaire respondents believe that the adoption of *SLFRS for SMEs* in Sri Lanka would increase the comparability of SME financial statements globally. Yet, those same respondents placed the benefit of comparability of financial statements fourth in importance. Conversely, interviewees did not identify 'comparability' as a benefit of adopting *SLFRS for SMEs*, which is surprising since it was one of the main reasons given by the IASB for the development of *IFRS for SMEs*. Limited international activities amongst Sri Lankan SMEs is the probable reason for not recognising comparability as a benefit of *SLFRS for SMEs*. This finding is consistent with Sy and Tinker (2013) who claim that improvement in global comparability may benefit multinational corporations, and their Big Four accounting firms, but companies with primarily domestic operations will not receive the same benefit.

Prior research finds that developing countries are more likely to mimic their trade partners when adopting *IFRS* (see for example: Al-Omari, 2010; Hassan et al., 2014; Irvine, 2008). However, it is interesting to note that top 12 trading partners of Sri Lanka with the exception of Singapore, United Arab Emirates and United Kingdom, have not yet adopted the *IFRS for SMEs* (countries such as United States of America, China, India, Japan, Germany, Italy, Belgium, Netherland and France). As a result, the global comparability of financial information is not likely to be a benefit for Sri Lankan SMEs. Sy and Tinker (2013) question whether *IFRS* would permit comparisons of financial statements due to variations between the different *IFRS* 'clusters'. They argue "the Asia Pacific group has carved out its own version, Japan, has bailed out of *IFRS* altogether, and several large European countries have also customised the standards to suit their own convenience" (Sy & Tinker, 2013, p. 4).

In addition to the benefit of comparable financial statements, questionnaire respondents identified 'easy access to finance' as a benefit of adoption of *SLFRS for SMEs*. It would appear that accountants tend to place more importance on these benefits than do the owner-managers. 'Easy access to finance' came first in importance as perceived by respondents to the questionnaire survey. Respondents from large SMEs, were more likely to perceive these benefits than the respondents from medium and small SMEs. This is consistent with the IASB's and CASL's view as *IFRS for SMEs/SLFRS for SMEs* have been issued in the anticipation that they would assist SMEs to gain access to finance. However, owner-managers and accountants of SMEs who participated in the interviews disagreed with the idea that *SLFRS for SMEs* adoption would improve the ease of access to finance. According to their views, collateral is the main barrier they experienced when attempting to gain access to finance. This idea is supported by bank lending officers. Bank lending officers also disagreed with the idea that adoption of *SLFRS for SMEs* in Sri Lanka would contribute to improving access to finance. There appears to be no relationship between the adoption of *SLFRS for SMEs* and an improvement in reliability of SME financial information. However, research conducted with listed companies (Abu-Nassar & Rutherford, 1996) and SMEs (Baker & Cunningham, 1993) demonstrates that the accounting information in financial statements is more reliable when it is prepared in compliance with accounting standards or IFRS.

A possible explanation for this different finding from the Sri Lankan context is that bank lending officers believe that SMEs alter their financial statements in order to minimise the tax liabilities. Against this background, Sri Lankan banks largely adopt collateral-based lending to SMEs (see also Gamage, 2015). The issue of collateral-based lending to the SME sector is also evident from a representative of a government institution. It is clear that the adoption of *SLFRS for SMEs* in Sri Lanka would not contribute by itself, to improving the quality and credibility of SME financial reporting as it would also be necessary to have a proper mechanism to enhance the reliability of SME financial information and to protect user interests. Apart from the identification of costs and benefits, most of the respondents to the questionnaire survey (52.20%) perceive that the costs exceed the benefits. Similar results were obtained in the study conducted by Chand et al. (2015). Most respondents in their survey strongly agreed with the statement that the costs of complying with *IFRS for SMEs* were far greater than the corresponding benefits.

10.6 Summary

This chapter integrated and discussed the results of the questionnaires and interviews in order to answer the research questions. The discussion was largely focused on exploring Sri Lankan SME users and their financial information needs and the perception of respondents regarding the adoption and relevance of *SLFRS for SMEs* in Sri Lanka.

This thesis finds support for the institutional isomorphic pressures to adopt the *IFRS for SMEs* at both country and firm level. Although research suggests that all three isomorphic pressures explain *IFRS* adoption, this thesis does not find empirical evidence to support the claim of mimetic pressures in the decision to adopt the *IFRS for SMEs*. Coercive pressures from the World Bank were the strongest at the country level adoption of *IFRS for SMEs*. CASL was the influential player at the firm level who exerted coercive pressure on SMEs to adopt *IFRS for SME*. Small and mid-tier audit firms in Sri Lanka also influenced SMEs' decision to adopt *IFRS* *for SMEs*. However, actual implementation is found be low due to the lack of regulatory pressure from the government of Sri Lanka.

The results from both the questionnaire survey and interviews indicated that users of SME financial information are limited to owner-managers, banks and the Inland Revenue Department of Sri Lanka. Government institutions are also considered as users of SME financial information under certain circumstances, such as when trading with government institutions as a supplier or a buyer. The perceived main users of SME financial information varies according to entity size as measured by number of employees. Other users such as creditors, suppliers, customers and non-manager owners were not identified as main users of SME financial information. Findings regarding the users of SME financial information contradict with the IASB's list of users of SME financial information as given in the *IFRS for SMEs*.

Interview results revealed that for most SMEs, financial statements were prepared by their external accountants as a 'legal' document to be submitted for certain purposes, especially for taxation. Given this purpose, SMEs try to manipulate their financial information to understate their turnover and profits to minimise their tax liability. Both income tax officers and bank lending officers are aware of this and therefore, have a serious issues with the reliability of financial information contained in the SME financial statements. Quality and credibility of external professional accountants who provide accounting and auditing services to SMEs also appear to be troublesome for bank lending officers and income tax officers. The weak legal and regulatory mechanism in Sri Lanka aggravates this situation. Further, it appears from interview results that bank lending officers and income tax officers access internal financial information such as management accounting information from the SMEs.

Owner-managers do not depend on SME financial statements to make their business decisions. Lack of detail, out-of-date and complex information in the financial statements are the reasons for limited usefulness of SME financial statements for their decision making. The profit and loss statement is the only useful report because owner-managers could estimate their tax liability from it. Results from both the questionnaire survey and interviews reveal the usefulness of management information for decision making. Managing the cash flow of the business appears to be one of the major concerns of owner-managers. Given the limited usefulness of SME financial statements for owner-managers, bank lending officers and income tax officers, the result suggests that current SME financial reporting in Sri Lanka is in conflict with the decision-usefulness objective of financial reporting.

There is a general consensus among owner-managers and accountants of SMEs about the need for internationally comparable accounting information for SMEs. Owner-managers and accountants did not see the benefit of having internationally comparable accounting information for SMEs. For most Sri Lankan SMEs, international activities such as exports, foreign borrowings and ownerships are irrelevant business activities. Moreover, they do not receive requests to provide internationally comparable financial statement from their trade partners. Interview data with owner-managers reveal barriers for cross-border operations and further, identify that their primary concern is the survival of the business and not the expansion of business operations. Questionnaire respondents state that not all *SLFRS for SMEs* topics were suitable for Sri Lanka and hence needed to be modified to reflect the needs of the country. Respondents indicate that topics related to investment in non-listed companies, investment in listed companies, joint ventures, foreign exchange risk resulting from a customer order or a supplier, and foreign exchange rate loans and borrowings are largely irrelevant to Sri Lankan SMEs.

It can be seen that the adoption of *IFRS for SMEs* (as known as *SLFRS for SMEs*) in Sri Lanka creates some problems and is not cost effective for Sri Lankan SMEs. Costs include accounting and auditing services, lack of qualified accountants, lack of knowledge on *SLFRS for SMEs* among SME accountants and local audit firms, issues regarding fair value calculations and measurements. However, divergent findings were obtained from the questionnaire survey and interviews regarding the benefits of *SLFRS for SMEs*. Respondents to the questionnaire survey indicated that the adoption of *SLFRS for SMEs* improved access to finance and comparability of SME financial statements. SME accountants tend to identify with these benefits more than SME owner-managers. In contrast to the findings from the questionnaire survey, owner-managers and accountants who participated in interviews do not identify ‘easy access to finance’ and ‘comparability’ as benefits of *SLFRS for SMEs*. Overall, they are not certain about the benefits of adopting *SLFRS for SMEs*. However, there is an overall agreement among the respondents to the questionnaire survey that the costs of *SLFRS for SMEs* in Sri Lanka outweigh the benefits.

CHAPTER ELEVEN

DEVELOPMENT OF A FINANCIAL REPORTING FRAMEWORK FOR SRI LANKAN SMEs

11.1 Introduction

This chapter presents the proposed financial reporting framework for Sri Lankan SMEs. In order to develop the proposed financial reporting framework, a three-stage process was followed. First, a draft framework was developed based on the findings obtained through a questionnaire survey and first round of interviews. Second, follow-up interviews were conducted with users and preparers of SME financial information to obtain their feedback on the draft financial reporting framework. Third, the draft financial reporting framework was refined according to the feedback given by the interviewees and a modified framework is proposed.

The need for an effective financial reporting framework for SMEs stems from the importance of SMEs in the country's economy. Findings relating to the two research questions driving this thesis reveal that the users of SME financial information and their needs are different to those of large entities with public accountability. Additionally, the findings indicate that users and their financial information needs vary according to the size of SMEs. Costs of adopting the accounting standard *SLFRS for SMEs* are seen as a burden for Sri Lankan SMEs, and exceed the benefits. Evidence supports a more simplified format for SMEs to reduce the reporting burden and to satisfy the decision-making needs of users. A financial reporting framework for SMEs therefore, needs to strike an appropriate balance between satisfying information needs of SME users and reducing the reporting burden on SMEs.

The remainder of the chapter is organised as follows. Section 11.2 reviews the financial reporting framework before *IFRS* adoption in 2012. Section 11.3 discusses the current financial reporting frameworks for Sri Lanka (post 2012). Section 11.4 presents a draft framework to be evaluated by the users and preparers of SME financial information. Section 11.5 considers the findings from the follow-up interviews. Section 11.6 proposes a modified financial reporting framework incorporating the feedback obtained through follow-up interviews. Section 11.7 concludes the chapter.

11.2 Financial reporting framework of Sri Lanka pre-2012

Since 2003, Sri Lanka has recognised that SMEs need a reporting framework (Confederation of Asian and Pacific Accountants, 2003). Many countries recognise the inappropriateness of general purpose financial reporting requirements for SMEs, and have introduced differential financial reporting frameworks (Confederation of Asian and Pacific Accountants, 2003). Differentiating financial reporting rests mainly on two foundations: the differences between users and their information needs; and cost-benefit considerations of SME financial reporting (Eierle, 2005). The IASB was not the first to develop a differential financial reporting framework for SMEs. Differential reporting for SMEs has been practised since 1992 in Australia, followed by New Zealand in 1994. Other developed countries followed (for example, US in 1996, UK in 1997, and Canada in 2002) as well as some developing countries (for example, South Africa and Malaysia in 2000, and Sri Lanka in 2003.) (Confederation of Asian and Pacific Accountants, 2003). Differential reporting is built on:

> … the notion that some entities should be allowed to depart from some particular requirements of accounting standards or the entire accounting standards in preparing their financial statements (Confederation of Asian and Pacific Accountants, 2003, p. 7).

In 2003, the CASL issued *Sri Lanka Accounting Standards for Smaller Enterprises* (*SLASSE*) (Institute of Chartered Accountants of Sri Lanka, 2003). CASL used listing status and size measures to classify companies into three Tiers (Table 40).

Table 40: Financial reporting framework of Sri Lanka pre-2012

Tier 1	**Tier 2**	**Tier 3**
Sri Lanka Accounting Standards (SLAS)	*Sri Lanka Accounting Standards for Smaller Enterprises (SLASSE)*	*Framework for Preparation and Presentation of Financial Statements*
SBEs and other large companies with more than: Annual turnover Rs500 million Shareholders equity Rs100 million Gross assets Rs300 million Liabilities Rs100 million Staff 1000 [Any one of the size criteria to apply]	Annual turnover Rs50 - 750 million Shareholders equity Rs10 -150 million Gross assets Rs30 - 450 million Liabilities Rs10-150 milliom Staff 100 - 1000 [All of the upper threshold size criteria to apply but only one of the lower threshold size criteria need to apply]	Annual turnover below Rs 50 million Shareholders equity below Rs10 million Gross assets less than Rs30 million Liabilities less than Rs10 million Staff below 100 [All of the size criteria to apply]

Source: Confederation of Asian and Pacific Accountants (2003) and Institute of Chartered Accountants of Sri Lanka (2003)

All Specified Business Enterprises (SBEs),[35] such as Listed Companies, Banks, Insurance companies, Factoring companies, Finance companies, Stockbrokers and others nominated in the *Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995*, were required to apply Tier 1 accounting standards in the preparation of their financial statements, and large companies meeting any one of the size criteria.

Tier 2 accounting standards were applied to Smaller Enterprises (SE) that were companies, not listed in a stock exchange but licensed under the *Securities and Exchange Commission Act No. 36 of 1987* and were below all the upper size criteria and yet above any one of the lower size criteria (Institute of Chartered Accountants

[35] The *Sri Lanka Accounting and Auditing Standards Act No. 15 of* 1995 defines a class of companies as Specified Business Enterprises (SBEs). SBEs include: 1. Companies listed on a stock exchange. 2. Banks. 3. Insurance companies. 4. Factoring companies. 5. Finance companies. 6. Leasing companies. 7. Unit trusts. 8. Fund management companies. 9. Stockbrokers and stock dealers. 10. Stock exchanges. 11. Public corporations engaged in the sale of goods or the provision of services. 12. Non-listed companies that have; ─ annual turnover in excess of Rs500 million; ─ shareholders' equity in excess of Rs100 million; ─ gross assets in excess of Rs300 million; ─ liabilities to banks and other financial institutions in excess of Rs100 million; ─ staff in excess of 1,000 persons.

of Sri Lanka, 2003). The *SLASSE* was intended to give a true and fair view of the financial position and profit or loss (or income and expenditure) of all entities that were covered under the definition of SEs, whilst lessening the financial reporting requirements burden (Institute of Chartered Accountants of Sri Lanka, 2003).

Tier 3 provided for financial statements of enterprises falling below all the lower size-based thresholds to be prepared in accordance with the accounting concepts as described in the Sri Lankan *Framework for the Preparation and Presentation of Financial Statements*. (Institute of Chartered Accountants of Sri Lanka, 2003). This 3-tier framework remained in place until Sri Lanka decided to converge with *IFRS*.

11.3 Current financial reporting framework of Sri Lanka (post 2012)

The CASL decided to converge fully with all standards issued by the IASB in 2012. The CASL introduced the Sri Lanka Accounting Standard for Small and Medium-Sized Entities (*SLFRS for SMEs*) as a word-for-word Sri Lankan language translation of the IASB's *IFRS for SMEs,* effective for financial periods beginning on or after 1 January 2012. However, the CASL later introduced a third Tier for 'smaller entities' to take effect on 1 January 2016. Table 41 shows current financial reporting framework for Sri Lankan SMEs.

Table 41: Current financial reporting framework of Sri Lanka

Tier 1	Tier 2	Tier 3
Sri Lanka Accounting Standards (SLFRS)	*Sri Lanka Accounting Standards for Small and Medium Sized Entities (SLFRS for SMEs)*	*Sri Lanka Accounting Standards for Smaller Entities (SLFRS for Smaller Entities)* (Introduced effective from 1 January 2016)
SBEs and companies with public accountability	Without public accountability	(a) revenue less than Rs. 100 million in the reporting period; (b) equity less than Rs. 50 million at the end of the previous reporting period; (c) is not required by company law to prepare group financial statements or (d) does not hold assets in a fiduciary capacity as one of its primary business

SBEs who had previously adopted Tier 1 reporting standards are now required to prepare their financial statements in accordance with *SLFRS*. Those reporting standards are identical to the *IFRS*. However, other larger companies in the SBEs' definition are permitted to adopt either *SLFRS* or *SLFRS for SMEs*. The IASB, permits local authorities at the individual jurisdiction level to decide what constitutes an eligible entity to which the *IFRS for SMEs* should be applied (International Accounting Standards Board, 2009a). When the CASL adopted the *IFRS for SMEs* as the *SLFRS for SMEs* in 2012, they specified that its application was for non-publicly accountable entities (Institute of Chartered Accountants of Sri Lanka, 2012). No size criteria are contained in the specification used to classify an entity as belonging to Tier 2. For the four years (2012 to 2015) following adoption of the IASB standards, only two tiers existed and SMEs had no option but to follow the *SLFRS for SMEs*.

The CASL reintroduced a third Tier of accounting standards known as Sri Lanka Accounting Standards for Smaller Entities (*SLFRS for Smaller Entities*) which came into effect from 1 January 2016. The Tier 3 accounting standards could be applied by a smaller entity, i.e. an entity that does have any of the criteria listed in

Table 41 based on size and fiduciary relationships. Although the CASL introduced the third Tier in 2016 to simplify the financial reporting requirements of small SMEs, it is considered inadequate. Because some irrelevant accounting topics for small SMEs such as government grants, and foreign exchange rates were still retained in the *SLFRS for Smaller Entities*. Further, according to the *SLFRS for Smaller Entities*, financial statements of an entity shall include a statement of cash flows for the reporting period. Interviews with income tax officers indicate that cash flow statement is not necessary for or required from small SMEs. Figure 11 presents the evolution of the financial reporting framework for SMEs in Sri Lanka.

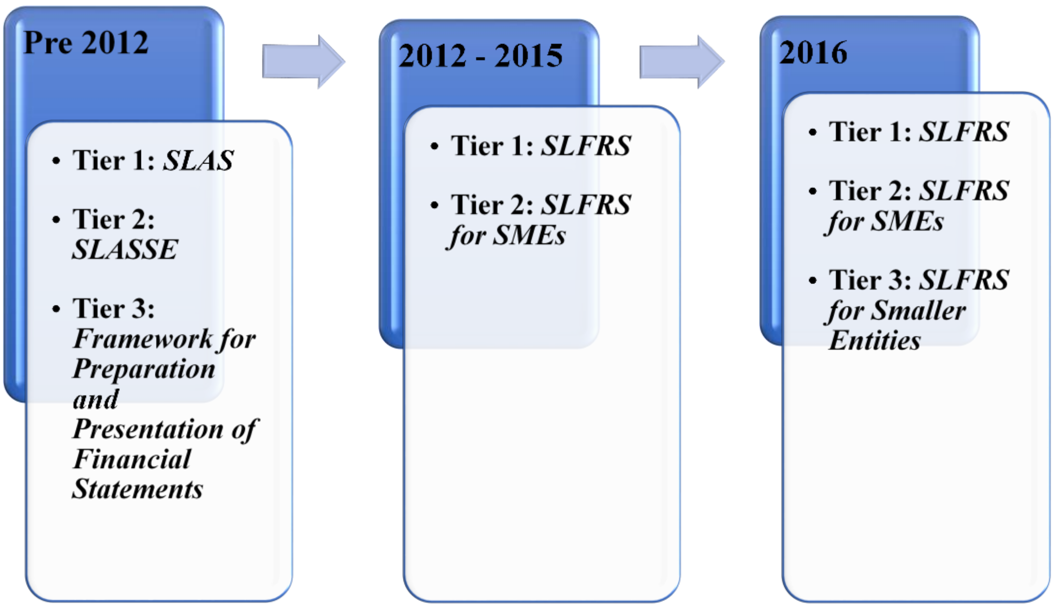

Figure 11: Evolution of financial reporting framework for SMEs in Sri Lanka

Source: Author

11.4 Stage 1: Draft framework for financial reporting by Sri Lankan SMEs

A draft framework was developed utilising the findings obtained from the questionnaire survey and the interviews, relating to users and their financial information needs and the costs and benefits of *SLFRS for SMEs*. Building upon the current Sri Lankan financial reporting framework and incorporating the special circumstances of the Sri Lankan business environment and economic climate, a draft framework is proposed, which includes four tiers for four different classes of entities. Three proxies are used to determine whether dependent users exist for such entities: (1) public accountability; (2) separation of ownership and management; and (3) entity size. This financial reporting framework follows the 'user needs' approach as used in New Zealand and Australia (Australian Accounting Research Foundation, 2001; External Reporting Board, 2012).

This thesis finds that the needs of users of SMEs financial reporting vary according to the size of the entity. Large SMEs work with a greater variety and number of transactions and their reporting needs appear distinctively different to those of the medium and small sized SMEs. Consequently, a draft framework for financial reporting by Sri Lankan SMEs is developed. Table 42 presents the draft framework for financial reporting by Sri Lankan SMEs.

Table 42: Draft financial reporting framework for SMEs

Tier	Accounting Standard	Revised Criteria	Notes
Tier 1	SLFRS	Entities with public accountability	Under this modified financial reporting framework, entities which have "public accountability" are required to report in accordance with SLFRS regardless of their size. An entity has public accountability if: (a) Its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or (b) It holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance providers, securities brokers/dealers, mutual funds and investment banks. (International Accounting Standards Board, 2009, p. 10)
Tier 2 (Revised)	Revised SLFRS for SMEs	1.No public accountability 2.Ownership & management separated; and 3.Large	Ownership and management separated means, owners/shareholders are not managers/directors of the entity. entity is large if it meets any two of the following: (a) revenue in excess of Rs100 million at the end of the previous reporting period; (b) had equity in excess of Rs50 million at the end of the previous reporting period; (c) has more than 39 employees
Tier 3	SLFRS for Smaller Entites	1.No public accountability 2.Ownership & management separated;and 3.Not large.	Other entities that do not have owners who are not managers, also have the option to prepare their financial statements in accordance with Tier 3 reporting standards if they have wider users.
Tier 4 (New)	Special purpose financial reporting	1.No public accountability 2.Ownership & management not separated; 3.Submits financial information to the IRD	A simple financial reporting format (see appendix P) **Minimum requirements for preparing financial statements:** A statement of profit or loss A statement of Assets and Liabilities **Principles with which statements must comply:** The double entry methods of recording of finanical transactions; and The principles of accrual accounitng **Valuations** – historical cost method

Tier 1 – *SLFRS*

Under the draft financial reporting framework, entities which have "public accountability" are required to report in accordance with SLFRS regardless of their size. An entity has public accountability if:

> a) Its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or
> b) It holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance providers, securities brokers/dealers, mutual funds and investment banks.
>
> (International Accounting Standards Board, 2009, p. 10)

Therefore, there are no recommended changes to the present Tier 1 requirements.

Tier 2 Standards – Revised *SLFRS for SMEs* (proposed a cut down version of *IFRS for SMEs*)

The Tier 2 financial reporting requirements (*SLFRS for SMEs*) of the current framework for Sri Lankan SMEs are solely based on the non-public accountability criterion. The IASB's SME definition is criticised for its broad description (Di Pietra et al., 2008; Evans et al., 2005; Holgate, 2007). It is a definition that would apply to a large range of entities, with differing information uses and users, especially between the small and large SMEs (Evans et al., 2005). The Sri Lankan SME definition adopted for *SLFRS for SMEs* is therefore, different to that of most other countries and is not based on size-threshold. Users vary with to the size of the SMEs and most of them in Sri Lanka are owner managed. As a result, the existing standards might not be able to meet the needs of different financial statement user groups (Evans et al., 2005). For these reasons, SME definition for Tier 2 is modified to read:

'An entity may elect to be in Tier 2 when the entity does not have public accountability, and:

a) has owners who are not managers of the entity, and;
b) the entity is large if it meets any two of the following:

(a) revenue in excess of Rs100 million at the end of the previous reporting period;
(b) had equity in excess of Rs50 million at the end of the previous reporting period;
(c) has more than 39 employees'

If the entity has owners who are not participating in the management of the entity, there is stewardship requirement between the management and the owners. In response to the findings of this research, large SMEs with more than 39 employees would be required to apply *SLFRS for SMEs*. Further, it is observed that the current *SLFRS for SMEs,* adopted by the CASL without any modifications, is not cost effective for Sri Lankan SMEs. Findings of this thesis indicate that the adoption of *SLFRS for SMEs* is a financial burden for SMEs, mainly due to increase costs of employing external auditors and accountants and making fair value calculations. Therefore, it is advocated that the *SLFRS for SMEs* be revised to reduce the cost burdens on the reporting entities.

Large SMEs, (employing 40-99 people) are more likely than the small and medium sized SMEs to adopt *SLFRS for SMEs.* Owners and accountants who participated to interviews do not believe that the *SLFRS for SMEs* increases the comparability of financial statements nor do they perceive it eases access to finance. Overall, the majority of the respondents (52.20%) perceive that the costs exceed the benefits. Therefore, *SLFRS for SMEs* needs to be revised to reflect the local reporting environment. The CASL should omit irrelevant topics such as: investment in non-listed companies; investment in listed companies; joint ventures; government grants; foreign exchange rate loans and borrowings; and foreign exchange risk resulting from a customer order or a supplier. Complexities of the *SLFRS for SMEs* such as fair value calculation could also be removed to provide further simplification to the standard. Based on the above findings of this thesis, a 'cut down version' of *SLFRS for SMEs* is therefore, recommended for entities which are falling under Tier 2.

Tier 3 Standards – *SLFRS for Smaller Entities*

At the time of conducting first round of interviews, users of SME financial information such as owner managers, bank lending officers, and income tax officers were not aware about this new accounting standard and unable to comment on it. For this reason, no amendments were made to the existing Tier 3 reporting standards except for a slight change of the definition.

An entity may elect to be in Tier 3 when the entity:

a) does not have public accountability, and
b) has owners who are not managers of the entity and;
c) is not large, as defined for Tier 2

As shown in the draft framework in Table 42, other entities that do not have owners who are not managers, also have the option to prepare their financial statements in accordance with Tier 3 reporting standards if they have wider users such as banks, and government institutions. Any entity eligible to follow the requirements of a lower tier may elect to report at higher tier.

Tier 4: Special purpose reporting

The draft framework introduces a fourth tier, being special purpose financial reporting for owner managed SMEs that produce financial information for tax purposes. An entity may elect to be in Tier 4 when the entity:

a) Does not have public accountability, and
b) Is owner managed, and
c) Needs to submit the financial information to the Inland Revenue Department of Sri Lanka as per the Inland Revenue Act

All entities categorised under the special purpose reporting are not required to prepare general purpose financial statements. They are however, required to prepare special purpose financial information as specified by the Inland Revenue Department of Sri Lanka. For this purpose, the Inland Revenue Department of Sri Lanka can introduce minimum requirements including a reporting format as recommended in Table 42. Results of this thesis reveal that most SMEs are owner managed and thus, non-manager owners are not identified as users of SME financial information. This raises an important question relating to the relevance of stewardship as one of the objectives of SME financial reporting. Apart from non-manager owners, other users such as creditors, customers, and employees are not identified as users of small SMEs. In Tier 4, the main purpose of financial reporting is for taxation. General purpose financial reporting is not therefore required for SMEs that do not have other external users of their financial information. Those SMEs can prepare special purpose financial statements to meet the financial information needs of the Inland Revenue Department of Sri Lanka.

11.5 Stage 2: User evaluation of the draft financial reporting framework and their comments on the *SLFRS for Smaller Entities*

Follow-up interviews were used to obtain interviewees' perception on the *SLFRS for Smaller Entities* (Tier 3) as part of the second stage of the financial reporting framework development. A user evaluation of the draft financial reporting framework was conducted with limited number of interviewees that had participated for the first round of interviews of this thesis. This opportunity was also used to obtain interviewees' perception on the Tier 3 accounting standards as they were not aware and were unable to comment on this accounting standard at the time of conducting the first round of interviews. Concerns raised by interviewees about the Tier 3 reporting standards and the draft framework were subsequently used to fine tune the draft financial reporting framework for Sri Lankan SMEs. This section discusses the findings from follow-up interviews.

11.5.1 Follow-up Interviews: perception on the *SLFRS for Smaller Entities*

In the follow-up interviews, one of the representatives from the standard setting authority of Sri Lanka outlined the reason for introducing the Tier 3 accounting standards for SMEs. The main intention of introducing this accounting standard was to reduce the burden of small SMEs by simplifying the financial reporting requirements. The standard setter explains:

> We identify that the *SLFRS for SME* is too complex for the smaller SMEs. We ran a series of seminars on *SLFRS for SMEs* covering almost all the regions so the feedback was that *IFRS for SMEs* is complex for many of the SMEs because that is in line with the *IFRS* standard. If you take all the complex transactions like financial instruments, borrowing costs, fair value measurement, and employee benefits, I don't think by doing that for a small SME would really get a benefit out of that. The cost benefit analysis is much more needed in financial reporting. Now

> once we do such a kind of arrangement to measure a particular value we spend X amount of money. In return we should get X + 1 but for an SME we have to ask the question are we getting that X + 1? It's really not. Then they being rational business people they will not go for financial reporting. That was basically the main reason for introducing *SLFRS for Smaller Entities*. This is more simplified version. Fair valuation option is not there but we have issued a separate amendment, it is like an amendment to the standard allowing them the revaluation option. It is not a must but it is an option. If they want they can apply it. They can select the revaluation model or they can simply go by the cost model (Standard setter-representative 02).

The standard setter believes the new accounting standard is a simplified version and cost beneficial to small SMEs as it does not include complex transactions such as financial instruments, and borrowing costs and fair value measurements. However, the standard setter implies that CASL does not encourage SMEs to follow Tier 3 reporting standards if they have already adopted the *SLFRS for SMEs*. The standard setter representative express this sentiment:

> … but actually, from the institute's side we are not expecting SMEs to downgrade their financial reporting quality. For example, if they are following the full *SLFRS*, so we don't recommend for them to go for either *SLFRS for SMEs* or *SLFRS for Smaller Entities* standard. We advise them to be in the same tier because as a responsible authority we are not recommending downgrading. Likewise, if they are following the *SLFRS for SMEs* standard why do they want to downgrade the quality of their reporting and go for Tier 3 -? We are not respecting it. The Tier 3 reporting framework is specially designed for very small SMEs. I think it can be even applied by a small SME like a small retail shop (Standard setter-representative 02).

The standard setter representative claims that CASL obtain comments from all stakeholder groups before finalising the *SLFRS for Smaller Entities* and believes it reflects users' requirements. The standard setter body received a donation from a German based institution for this project and utilised the part of the World Bank grant's to conduct awareness programmes on the draft version of the standard. The Standard setter describes the development process as follows:

> We got a direct donation from the GIZ, a German donor agency to this project. When developing this standard, we had a sub-committee. It represented very senior members of the institute including members from Big Four audit firms. Then the sub-

> committee for this purpose drafted this standard with the technical division of the institution. We exposed this for public comment including members, Chambers, Department of Inland Revenue, Banks' SME units, Chambers and we got comments from them. We had typically as I can recall my memory we had two awareness workshops from the draft standard. Actually, I doubt whether we got any written comments but we got verbal comments from these workshops itself.
>
> I think we got less than 50 comments. I am not too sure whether I can have the numbers for you because I might not have the records with me. That's the reason because we have completed this project somewhere in 2015? Under the World Bank grant extended for the Institute there was a budget allocation for SME capacity building so under that we have conducted around five to seven workshops on the audit manual that was typically a case study type workshop so we had around seven sessions. Of course, under the GIZ programme we could conduct regional seminars for two days, two-day regional workshops so we had almost seven to ten seminars covering both awareness level training as well as application level training programme covering how to prepare financial statements based on a set of transactions (Standard setter-representative 02).

The above explanation reveals that the standard setter received a grant from a German based donor institution to develop the Tier 3 accounting standard. This is consistent with the institutional account of coercive isomorphic pressure (DiMaggio & Powell, 1983; DiMaggio & Powell, 1991). The rationale underlying this institutional coercion is primarily financial dependence of the influenced organisation (Lawrence et al., 2009; Mir & Rahaman, 2005; Sharma et al., 2010, 2014; Tsamenyi et al., 2006). It further appears that they did not receive any written comments to the Exposure draft of this standard. Instead they obtained verbal comments when they conducted the awareness programme based on the draft version of the standard. However, they do not want to reveal specific number of comments and particular organisations who commented on it. These workshops and awareness programmes were funded jointly by the German donor agency and World Bank. Even though the standard setter claims that they obtain comments and feedback from the users of SME financial information, SME owners, bank lending officers and the income tax officer who participated to the follow-up interviews expressed that they were not reached by the standard setter for any comments. Interviewees expressed disappointment regarding this process:

> … since about ten years' time I have never been in touch with this what do you call that Chartered Institute so even I don't know what are their standards. I have never got a chance to attend their seminars or awareness programmes. My tax firm, they just asked me to submit, check and do the signatures for their documents. That only I do know so it's just like we are trying to search something under a blank water so it is very critical. I don't know how and what they do but I know one thing – I have to pay so that's it. I don't know for what I am paying but I have to pay (Owner-manager 02).

> As to my knowledge they do not get any views from financial institutions. I think they have a responsibility to get some feedback from us (Bank lending officer 05).

> I am not aware of the fact whether they have actually gone into getting ground level information from SMEs. I have not been contacted by any of those officials with regard to getting information from our end. I feel if they can actually put some more concern regarding SMEs as to how the operations function they might find some existing barriers in the industry where it could be difficult for an SME to adhere to all I mean to all the implications that have been imposed by them. It would always be an additional cost to the chartered accountants. On the other hand, to be honest when we get stuck with day to day business operations so the accounting information that we are supposed to gather for these regulations would at some point be seen as some extra burden that might hinder our day to day operations (Owner-manager 05).

It appears from above statements that the standard setter did not adequately consult with the users of SME financial information in developing the Tier 3 accounting standards for SMEs. Concern about the lack of user involvement in the development of accounting standards has been raised in the literature by Jonas and Young (1998) and Young (2006). With regard to the IASB's public due process for its *IFRS for SME* standard, Ram and Newberry (2013) conclude that the process was closer to a public relations exercise than one designed to capture the will of the people. Users of SME financial information who participated to the follow-up interviews did not comment positively about the *SLFRS for Smaller Entities*. For this reason, it is uncertain whether the new accounting standard address the concerns of the target group. Following quotes provide some examples:

> I think the new accounting standard is not the right solution for small entities. It is still too technical for them. So, that is why

> most of the small businesses do not wish to follow it. I have not clearly identified the financial statement that have been prepared under the new system. I can say 90% of documents are not in accordance with the new accounting standard. Actually, when we assess a loan application, we need the actual turnover and their gross profit, the net profit, what is the actual position of their assets, how much they have invested. These are simple things so these simple things should have been included in the Profit and Loss Account and the Balance Sheet. We just request only the Profit and Loss account and the Balance Sheet but it should reflect the actual position of the business. I think simple guidelines can be given to this group otherwise they would not prepare financial reports in future also (Bank lending officer 05).

> Anyone as an owner of small SME can't follow …. standards of this institute because we do not have that knowledge to do that. We have plenty of things to concern, so preparing a document by taking three to four hours, it's a very difficult task for us. Even we can't afford it. However, we normally manage our day to day transactions and keep records of our incomes and expenditure. That is most simple and most available things we do have by the way. I use this information to make my day to day business decisions. Even I used these documents to get bank loans. They did not ask for accounting standards. So far I do not feel the need to follow accounting standards. I think those are for big companies like … (Owner-manager 02).

> I think most of these people belongs to the small category, run the business on their own and do not have a formal way of recording business transactions but I know they keep some records on their income and expenses in an informal way. However, normally owner knows how much they earn. When they want to get a bank loan, they just submit their internal records for an example, their income/receipts and expenditure/payments sheets/books. I do not think this category need accounting standards but when they have grown the business to a certain level that is ok (Income tax officer 02).

A different view on preparing financial statements according to the accounting standards is held by a SME accountant, including the need for being prepared to pay a bribe. He describes:

> In my point of view SME accounting standards are good for the examination of Chartered Institute. When it comes to the practical situation, owners or directors they won't care …. Ok we prepare the financial statements as per the accounting standards and we provide those statements to the Department of Inland Revenue. That's the people who are basically looking at our accounts.

> When we go for a refund or something, they will interview us, and then the questions they ask from us is completely out of the accounting standards. Then if we tell these are prepared according to the accounting standards and they will listen and tell ok you go to the Chartered Institute and take the refund. My experience is when you go for a refund or something related to taxes, we have to have some cash for them. I have experienced it many times. We can't do anything unless we change this culture. We can follow the accounting standards in our organisations but it does not work for the government environment (Accountant 05).

The most of above, further reinforce that financial reporting requirements should reflect the nature, and size of SMEs but should also reflect the costs and benefits to SMEs and users. Moreover, when financial reporting requirements for SMEs are viewed to be too complicated, SMEs will tend to avoid them. Apart from the lack of user involvement of setting accounting standard, interviewees express concern about the SME definition of the new accounting standard. According to the *SLFRS for Smaller Entities,* an SME with annual revenue in excess of Rs.100 million is not eligible to apply this accounting standard and they are required to follow *SLFRS for SMEs*. About this definition, interviewees say:

> My company formed as a single director private limited company. Our usual turnover per year is somewhere around Rs150 million and we have only 7 employees. So, in such case I feel that I should be eligible to use the new accounting standard but because of the slight increase of my turnover, I think my company does not fall under this category. They should have some other way of categorisation. Not all companies are capable enough to follow whatever the regulations imposed by the government. What I feel is we should be allowed some exceptions. For an example, when we really calculate the profitability we feel that a large portion of the hard-earned money is at the moment is exposed to Government taxes, maybe the same rules that are applied to large scale organisations are like in a more or less similar manner to small companies as well. That is not fair. (Owner-manager 05).

One bank lending officer highly criticises the use of turnover as a criteria for categorisation of SMEs. His words:

> … we can take turnover into account for any categorisation only if SMEs reveal what the exact turnover is. If you can't get the actual turnover of a particular business then all the categorisations and the tools what we use to categorise them will

> not be useful because without knowing the actual turnover I mean how can you, maybe we will depend on the information what we have got, we might categorise that particular SME under the small category or medium category to see maybe in real terms we may be representing the corporate level. Likewise, if you can't get the real turnover you can't categorise them into the real category that they belong to. In certain other countries they use, now in India they define SMEs according to the investment. They don't go by the turnover or number of employees, they go by the investment so the investment you can find out because actually investment very rarely they can manipulate because at least by going through their business or by doing a visit you can find out what and what they have invested that is physically can be seen. … or we should have some other proper mechanism to categorise them (Bank lending officer 04).

Contrast to the opinion of bank lending officer 04, another bank lending officer believes that turnover can be used to categorise SMEs into different size classes. She highlights that bank lending officers use the Central Bank definition when they make lending decision to SME sector. She explains the Central Bank definition and proposes three SME clusters based on the turnover:

> As per the Central Bank of Sri Lanka, turnover is one of the criteria to categorise SMEs for bank loan purposes. SMEs coming under this categorisation can enjoy a special benefit at the time of calculating the capital adequacy ratio. Normally, the risk rate for SMEs coming under this category (other two criteria should also be satisfied) is reduced from100% to 75%. If we take the annual turnover criteria, it has to be less than Rs750 million or less if it is to be considered as an SME. I think they can use this. I feel the current threshold for Tier 3 reporting can be increased up to Rs.250 million. Because there is a special loan scheme which has been introduced by the Government. So they have classified small entities like that. If the turnover is between Rs15 million to Rs250 million it is considered as a smaller one but turnover should not be the only criterion. (Bank lending officer 05).

SME users are not satisfied with the SME definition adopted for the *SLFRS for Smaller Entities*. The different approaches adopted by different countries indicates that size should not be the ultimate criterion for a financial reporting framework but it can be used as one of the criterion. Because size criteria do not adequately represent the circumstances unique to different types of SMEs. For example, countries including Australia, and New Zealand adopt 'user needs' as the guiding principle to design the financial reporting framework for SMEs.

Even though the CASL claims that *SLFRS for Smaller Entities* is a simplified accounting standard for smaller entities, it appears that it does not provide sufficient relief for those very many small entities who may perceive no need to provide general purpose financial reports. The current *SLFRS for Smaller Entities* therefore, should be revised by CASL to make it more in tune with the needs of the small and medium sized SMEs. The following section describes the interviewees' feedback on the draft financial reporting framework, which is used to refine a proposed new framework.

11.5.2 Interviewees' feedback on the draft financial reporting framework for Sri Lankan SMEs

In the follow-up interviews, the draft financial reporting framework was evaluated. Overall, there is a general consensus among interviewees that there should be a simpler financial reporting format for the small SMEs and they are positive about introducing special purpose financial reporting.

> I think in Sri Lanka most of the businesses, the owners do not know about the business. The chartered accountants prepare all the figures so most of the owners or do not know about their figures. So if we ask some questions regarding their financials they co-ordinate with chartered accountants. So I think your framework is ideal because it is not complex, even it can be prepared internally. I think every owner should have an idea regarding the financial highlights of the business In some instances the owners do not know what is the gross profit of their business so what is the net profit of their business so they depend on the chartered accountants or one of the accountants so I think your framework, a simple framework is needed for owners to prepare actual position of the business at least revealing in the Profit and Loss account or Balance Sheet. In that sense, your suggestion for small SMEs is good. We are in a position to demand whatever the additional information we require for making lending decisions, so that I think they could easily prepare these documents internally (Bank lending officer 01).

> As you must be aware that most SMEs do not have the knowledge and resources to adopt accounting rules such as standards. Actually, there is a role to play by the Government because they will have to give some incentives or encouragement to these people. Now if we take the lower category, that is the starting point there has to be a very simple package for them, then maybe a medium one with something higher than that or maybe the top

layer or the upper category, they are just about to move into the corporate category, a different call reporting mechanism so that is ok because you can't give a single package or reporting system for all. Yes there has to be some mechanism adopted, there has to be some encouragement given to SMEs to bring them to a formal sector otherwise as a country we will not be able to prosper and also even when it comes to SME their sustainability I mean there will be a very big question mark in front of their sustainability unless they adopt the proper financial reporting system. Your simple format might be work well for the small SMEs. Through that I think we can bring them to a formal sector from this informal way of doing this financial reporting (Bank lending officer 04)

As a director of a small-scale entity, I feel that your framework would be in favour of the business entities. I think my company fall under the last category (Owner-manager 05).

In a country like Sri Lanka where most small SMEs are not aware about these accounting standards and do not have the capacity to apply these standards, we should have a simpler way to get the information from them. Even a survey questionnaire sort of thing would be good because we can use it in the way we want. We should not burden them. I believe your guidelines stated in the Tier 4 of the framework that you sent would be suitable for small SMEs. From our side, we are satisfied with a simple format which could be used to reveal their (small SMEs) turnover, profit, expenses, and assets. We can ask for any detailed information for further clarifications (Income tax officer 02).

Interviewees are very positive about the Tier 4 financial reporting requirements for SMEs. These discussions, further reinforce the need for financial reporting simplification for small SMEs. However, the representative from the standard setter is not certain about further relaxation of financial reporting requirements for SMEs. However, she is positive about the draft framework:

I think it is a very good document for use and for SMEs to understand which framework that they can follow when selecting the standard they might have more clarity when we have such a kind of demarcation. Owner-managers concept is good but it will be more relevant to the smaller entities right. I know for sure Tier 3 standard is also targeted to owner-managed SMEs. I think most of small SMEs belongs to that size category. So actually, we had a very good crowd at our training programmes and workshops conducted on the Tier 3 standard. There were small entities who even don't have any system for recording other than the transactions even so we trained them how to apply double entry

> system to prepare basic set of financial statements so I doubt whether we need further simplification but please do share with us your findings that would be really great. However, we thought to keep these standards for a while and say by next year we would think of and go for a revision then we can see how best we could address your suggestions as well. (Standard setter-representative 02).

It appears that the standard setter believes that the Tier 3 reporting standard of the current financial reporting framework could be applied by an owner-managed small SMEs that fall below the size criteria given in the current framework. However, the other interviewees (including bank lending officers, income tax officer, and owner managers) suggest an increase of the turnover threshold of the Tier 3 reporting standard and they also suggest including a size criteria for Tier 4 reporting requirements of the proposed framework using both turnover and number of employees. The interviewees believe that current number employees' threshold also need to be increased in the draft framework. They suggest:

> … as per our law the persons who maintain more than Rs 250 million annual turnover have to submit the audited financial statements. The other persons need not do that. Financial statements should be submitted to review their performance but should not audited. Other entities having an annual turnover below Rs250 million can provide their P & L, and the balance sheet because we need to know their performance for the last year. In this situation, I think you could consider increasing the turnover threshold of the Tier 3 and accordingly set a size criteria for Tier 4 companies (Income tax officer 02).

> According to your framework, if the organisation is owner-managed, then automatically it goes to the fourth category. Let's take a company like Y (name of a well-known private company), all three owners are directors of the company but we know that it's a big business. However, they can use the Tier 4 reporting standards of your framework. So, in such a case if you can introduce criteria such as turnover and number of employees it will give some further validity to your proposed system - that is my personal opinion. I also feel that the current threshold for number of employees could be increased (owner-manager 05).

> I personally believe that criteria based on number of employees in your proposed framework can be increased. For example, for large SMEs it should be more than 100 so on. For the turnover, as I said you before, you can have three categorisations like small, medium and large (Bank lending officer 05).

Discussions with a bank lending officer reveals that the government has an initiative to formulate a national definition for SMEs in Sri Lanka. Accordingly, he suggests to consider using the government definition, about to be finalised, for categorisation purposes:

> … the Government is to introduce a national definition for SMEs in Sri Lanka. I think it has already been approved by the cabinet. Under that Government suggests turnover and the number of employees as criteria for defining SMEs. So that is yet to come into operation. So do not get confused with all those definitions because for the moment the banks use the definition given by the Central Bank of Sri Lanka. However, if you could consider the Government SME definition, I think it would be ideal as Government is going to implement this definition for any policy related measures (Bank lending officer 04).

SME accountant commented on the revisions proposed for the Tier 2 accounting standards in the draft framework:

> I can agree with you regarding your suggestion to the Tier 2 reporting framework. To be very frank with you, I know they just adopt what you call *SLFRS for SMEs* as it is. They could have undertaken a wide consultation before adopting those standards developed by the International organisations. That is the mentality they have. Whatever you bring from overseas are considered as ideal solutions. That's why we are still a developing country. However, I would like to add few more suggestions to this standard. You may consider removing some topics that are still found to be complex and irrelevant such as borrowing cost, intangibles, Share based payments, and financial instruments (Accountant 05).

As can be seen from the above quotes, some important suggestions were obtained on the draft framework for financial reporting framework for SMEs, are able to be applied to formulate a proposed financial reporting framework.

11.6 Stage 3: Proposed financial reporting framework for Sri Lankan SMEs

As the final stage of the financial reporting framework development process, the draft framework was revised according to the feedback obtained from the follow-up interviews conducted with users and preparers of SME financial information. Accordingly, the following amendments were made to the draft framework. Except for Tier 1, SME definitions for the other three tiers are amended. However, the size criteria are suggestions, as a proposal that can be refined on the basis of further analysis of statistical data of entities and other policy considerations.

Tier 2 Standards – Revised *SLFRS for SMEs*

It is proposed that an entity may elect to use Tier 2 when the entity does not have public accountability, and has owners who are not managers of the entity. However, if an owner-managed SME is large, it is required to adopt Tier 2 financial reporting requirements. The entity is large if it meets any two of the following: (1) revenue in excess of Rs450 million at the end of the previous reporting period; (2) had equity in excess of Rs.100 million at the end of the previous reporting period; (3) has more than 100 employees.

Tier 3 Standards – *SLFRS for Smaller Entities*

The definition of smaller entities in Tier 3 is also modified from the draft financial reporting framework. An entity may elect to be in Tier 3 when the entity: (1) does not have public accountability, and (2) is owner-managed; and (3) is a 'medium sized' entity. The entity is medium-sized if it meets any two of the following: (1) revenue is between Rs250-450 million at the end of the previous reporting period; (2) had equity between Rs50-100 million at the end of the previous reporting period; (3) has between 50-100 employees.

Tier 4: Special purpose financial reporting

An entity may elect to be in this category when the entity: (1) Does not have public accountability, and; (2) is owner managed, and (3) is 'small'. The entity is small if it meets any two of the following criteria: (1) revenue is less than Rs250 million at the end of the previous reporting period; (2) had equity less than Rs50 million at the end of the previous reporting period; (3) has less than 49 employees.

The proposed framework for Sri Lankan SMEs presents an opportunity for non-publicly accountable entities to determine the objective of its financial reporting and tailor it to the user's needs. By doing so, it would help to resolve issues, such as cost and relevance, in the current financial reporting framework applying to Sri Lankan SMEs. Figure 12 presents a decision chart for the proposed financial reporting framework for Sri Lankan SMEs. This chart guides entities in deciding the category to which they belong to fulfil their financial reporting requirements.

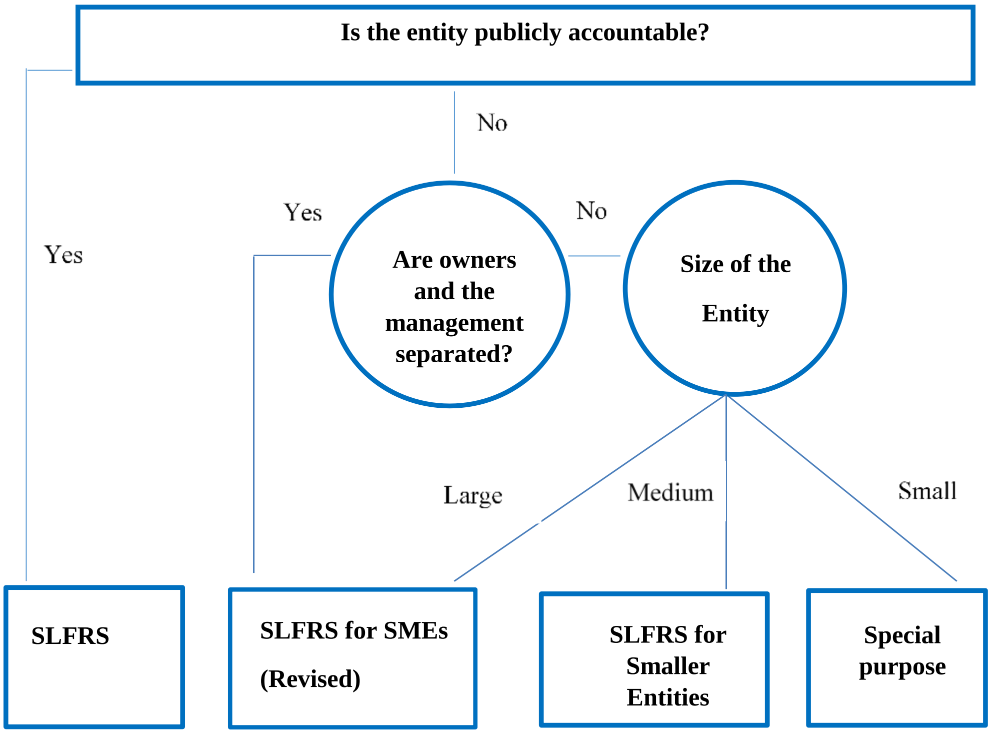

Figure 12: Proposed financial reporting framework for Sri Lankan SMEs

Source: Author

11.7 Summary

Based on the findings from both the questionnaire survey and interviews, the thesis developed a draft financial reporting framework for Sri Lankan SMEs. Having developed the draft version, user consultation was conducted in way of follow-up interviews in order to obtain perceptions on the draft financial reporting framework and the Tier 3 reporting standards of the current framework (*SLFRS for Smaller Entities*). Accordingly, the draft framework was refined and a modified financial reporting framework was proposed for SME financial reporting in Sri Lanka. The proposed framework comprises of four tiers to be applied to four different categories of entities. The guiding principle to determine the reporting requirement is based on the 'user need' approach as adopted by countries such as Australia, and New Zealand. A revised version of *IFRS for SMEs* (issued as *SLFRS for SMEs)* is recommended for non-public accountable SMEs that are not owner managed. However, if an owner-managed entity is large, it is also required to follow *SLFRS for SMEs*. If a medium entity that is owner-managed could apply *SLFRS for Smaller Entities*. A special purpose financial reporting category is suggested to small SMEs that are owner-managed. A simple reporting format needs to be developed for this category of SMEs as recommended in this thesis. As a consequence, the majority of Sri Lankan SMEs would not be required to prepare general purpose financial statements.

CHAPTER TWELVE

RESEARCH SUMMARY, IMPLICATIONS, AND CONCLUSION

12.1 Introduction

This chapter is the final chapter of this thesis. Section 12.2 outlines the research questions, summarises the research approach and methods used. Section 12.3 presents the key findings and section 12.4 provides an overview of the proposed financial reporting framework. Section 12.5 discusses the contribution of this thesis. Section 12.6 identifies the implications of this thesis to policy and practice. Section 12.7 considers the limitations of this thesis. Section 12.8 recommends future research directions. Finally, section 12.9 concludes the thesis.

12.2 Research background, questions and approach

The thesis proposes a financial reporting framework for Sri Lankan SMEs by first identifying users of Sri Lankan SME financial information to ascertain their needs, and second examining the desirability of internationally comparable financial information. SMEs play an important role in any economy (Isaga et al., 2015) and Sri Lanka is of no exception. In Sri Lanka, SMEs account for more than 90 per cent of total number of industrial establishments (Department of Census and Statistics, 2013). It is surprising that while SMEs are considered as important players in any economy, they have to adopt financial reporting requirements such as *IFRS for SMEs,* which is not primarily designed for them but for large and listed companies (Devi & Samujh, 2014; Di Pietra et al., 2008; Evans et al., 2005). Financial reporting requirements based on the full application of generally accepted accounting principles are suitable for the users of large companies whose shares are publicly traded and they are not appropriate for financial statement users of SMEs (Di Pietra et al., 2008; Eierle & Haller, 2009; Evans et al., 2005; Rennie & Senkow, 2009). (Rennie & Senkow, 2009). Thus, the identification of SME users and their financial information needs is highly relevant to the development of a financial reporting framework for SMEs.

A search of literature indicates only a few studies that exclusively examine the users and uses of SME financial information. Evans et al. (2005) assert that differences in users and their needs exist within SMEs, especially when it comes to very small entities and larger SMEs. However, most of the extant literature focuses on SMEs in general and does not distinguish between large SMEs, which may have external shareholders, and the small, and medium-sized owner-managed SMEs (Sian & Roberts, 2009). Many studies only survey the views of a single user group (see for example: Collis, 2008; Collis & Jarvis, 2000, 2002; Dang-Duc et al., 2008; Deakins & Hussain, 1994; Maingot & Zeghal, 2006; Page, 1984; Rennie & Senkow, 2009; Sian & Roberts, 2009), other users of SME financial information such as lenders, tax authorities, regulators, and other government institutions are ignored . Empirical research on users and their financial information needs, especially in the context of developing countries is limited (Di Pietra et al., 2008; Evans et al., 2005). Additionally, research that examines the effect of the adoption of international financial reporting standards on SMEs is sparse. There have been calls by academics like Chand et al. (2015), Uyar and Güngörmüş (2013), and Devi and Samujh (2015) for more research in the developing country context.

This thesis, therefore, contributes to this important but relatively neglected area. This research is a first to study the users and their financial information needs of Sri Lankan SME financial information and to examine the effect of *IFRS for SMEs* adoption on Sri Lankan SMEs. This thesis provides direction and insights for policy makers within the accounting profession and government institutions to assist their knowledge and appreciation of the issues and reality Sri Lankan SMEs face regarding the standardisation of financial reporting. Based on the findings, this thesis proposes a financial reporting framework for Sri Lankan SMEs. In order to obtain useful insights to develop a financial reporting framework for Sri Lankan SMEs, and to contribute to understanding and knowledge of the context of Sri Lanka, two research questions were posed:

1. How do Sri Lankan users and their financial information needs differ with regard to size of SMEs?
2. Do Sri Lankan SMEs need internationally comparable financial information?

A mixed-method approach to research combining quantitative and qualitative methods was adopted to answer the research questions. The use of a mixed method approach comes from the recognition that each method has its own strengths and weaknesses and a combination of the two methods is likely to increase the reliability and validity of the research findings. A quantitative approach using a questionnaire survey was used to collect data from accountants and owners of Sri Lankan SMEs. Usable responses were received from 323 SMEs giving an overall response rate of 13 per cent. Responses from the SME owners and accountants were further reclassified into a three group of entities based on the number of employees. Responses were analysed separately for small SMEs (5 to 15 employees), medium SMEs (16 to 39 employees) and large SMEs (40 to 99 employees). Qualitative semi-structured interviews were conducted with 41 individuals including bank lending officers, income tax officers, representatives of government institutions, and the standards setting authority of Sri Lanka, and owners and accountants of SMEs. Eight follow-up interviews were conducted with the interviewees who had participated to the first round of interviews to obtain their feedback on the draft financial reporting framework for Sri Lankan SMEs. The quantitative data obtained through the questionnaire survey were analysed using SPSS software. Qualitative data obtained through interviews were analysed thematically. NVivo software was used to organise and manage the qualitative data.

The thesis adopts an institutional theory perspective, particularly institutional isomorphism to understand, and interpret the empirical data. Institutional theory is a dominant organisational theory and is increasingly being applied to study the practice of accounting in organisations (Dillard et al., 2004; Sharma & Lawrence, 2008; Sharma et al., 2010, 2014; Tsamenyi et al., 2006; Tuttle & Dillard, 2007). Scholars have supported the use of institutional theory, in particular institutional isomorphism, in explaining the *IFRS* adoption (Al-Omari, 2010; Hassan et al., 2014; Heidhues & Patel, 2012; Irvine, 2008; Kholeif, 2010; Lasmin, 2011). However, research (see, for example, Al-Omari, 2010; Hassan et al., 2014; Heidhues & Patel, 2012; Irvine, 2008; Kholeif, 2010; Lasmin, 2011) is restricted to either country or firm level analysis of the *IFRS* adoption.

To fully understand institutional change we must consider the influence of higher social, political, and economic levels on the organisational context (Dillard et al., 2004). Therefore, as suggested by Dillard et al. (2004) and Irvine (2008), this thesis focuses upon how various institutional pressures drove the decision to adopt *IFRS for SMEs* in Sri Lanka at both country and SME levels.

12.3 Key findings

The main findings derived from data gathered by the quantitative and qualitative surveys are summarised as follows.

RQ1: How do Sri Lankan users and their financial information needs differ with regard to size of SMEs?

The IASB's rationale for the identification of users and uses of SME financial information is based on decision-usefulness objective of financial reporting. Accordingly, various user groups such as shareholders, creditors, employees, and the public were identified as main users of SME financial information (International Accounting Standards Board, 2009b, p. 7). The IASB claimed that the financial statements produce for the use of owner-managers or tax authorities are not necessarily general purpose financial statements (International Accounting Standards Board, 2009b) and excluded the specific needs of these two key users. The main users of Sri Lankan SME financial information and owner-managers' needs are discussed under three separate headings based on the size of SMEs as follows. None of the previous researchers has investigated users and their information needs of SME financial information in relation to entity size.

Small SMEs (5-15 employees)

The majority of the responding entities from the 5-15 employee category identify owner-managers and banks as main users of financial information. The majority of small SMEs indicate that they use SME financial information to take marketing and pricing decisions, capital investment decisions, and, planning decisions. Calculating income tax liabilities was not identified as a purpose of using financial information. This finding was in line with the responses given to the question which asked about the main financial information users, because they did not identify the Inland Revenue Department as one of the main users of SME financial information. The findings from interviews indicate that financial statements of small SMEs are prepared by external accountants to meet legal requirements such as taxation, and the preparers send them directly to the Inland Revenue Department. This is the probable reason for not identifying Inland Revenue Department as a user of SME financial information by the small SMEs. Findings from interviews further indicate that the Inland Revenue Department is a user of SME financial information regardless of SME size. Every SME is required to provide their financial statements to the Inland Revenue Department when they submit their annual tax return. Other users such as government institutions, non-manager owners, and suppliers are not identified by owner-managers of small SMEs as users of their financial information. The profit and loss statement is the most useful financial report for decision making of owner-managers followed by the balance sheet, and the cash flow statement. However, notes to the financial statements, and the statement of changes of equity are not useful for making business decisions of owner-managers of small SMEs. The owner-managers of small and medium sized entities perceive budgets as the most useful management information for their decision making.

Medium SMEs (16-39 employees)

The majority of respondents from the 16-39 employee category identified owner-managers, banks, and the Department of Inland Revenue as main users of their financial information. Owner-managers from medium SMEs use financial information for the purposes of: estimating income tax liabilities; taking marketing and pricing decisions; deciding employees' pay and bonuses; comparing performances with previous periods; Deciding managers'/directors' pay/bonuses/dividends; and, when taking short-/long-term planning decisions. Owner-managers of medium SMEs also perceive that the profit and loss statements as the most useful financial report for making business decisions followed by the balance sheet, and the cash flow statement. Similar to the findings for small SMEs, owner-managers in this category do not perceive notes to the financial statements, nor the statement of changes of equity as useful for making business decisions. In line with the perception of owner-managers' in small SMEs, budgets are identified as most useful management information to owner-managers of medium SMEs for their decision making.

Large SMEs (40 – 99 employees)

Large SMEs from the 40-99 employee category, identify owner-managers, banks, Inland Revenue Department, and government institutions as main user of their financial information. A higher proportion of non-manager owners was to be found in large SMEs than the below 40 employee categories. This finding is consistent with the finding by Eierle and Haller (2009) when studying German SMEs. They suggest that larger entities are more likely than small entities to have non-participating owners. These findings suggest that principal-agent conflicts are more likely to be seen in large rather than in small SMEs.

It is reasonable to argue that the main users of SME financial information vary according to entity size. The majority of owner-managers from large SMEs indicate that they used financial information for estimating income tax liabilities; comparing performances with previous periods; comparing performances with targets; making short or long-term planning decisions; and, when deciding directors' pay/bonuses/dividends. In contrast to the findings for small and medium SMEs, owner-managers from large SMEs perceive the cash flow statement to be the most useful financial report, followed by the profit and loss statement, and the balance sheet. Notes to the financial statements are more useful to the owner-managers of large SMEs than to the respondents from the other two categories. The majority of the owner-managers from both small and medium entities identify budgets as useful management information whereas the majority of owner-managers from large SMEs identify management accounting information as the most useful management information for making business decisions. These findings are in agreement with Evans et al. (2005) who asserts that differences in users and their needs exist within SMEs, especially when very small entities are compared with larger SMEs.

Overall, the perceived main users of Sri Lankan SME financial information are owner-managers, bank and financial institutions, and tax authorities. This finding is supported by the literature on users of SME financial information (see for example: Barker & Noonan, 1996; Carsberg et al., 1985; Collis & Jarvis, 2000;

Maingot & Zeghal, 2006; Page, 1984). However, the needs of owner-managers and tax authorities are ignored by the current conceptual framework adopted for SME financial reporting - their opinions were never obtained.

Government institutions are also considered as a user of SME financial information under certain circumstances. This finding is consistent with the developing country study (Dan-Duc et al., 2006). However, findings of this thesis, with regard to the government institutions, contradict earlier findings from studies in developed countries (Collis & Jarvis, 2000; Sian & Roberts, 2009). For example, Sian and Roberts (2009) find that government institutions are not important users of UK SME financial information as only 2.8 per cent of respondents indicate them as users. Government institutions of Sri Lanka governs and implements the SME loan schemes that received from the donor agencies such as the Asian Development Bank (ADB), and the World Bank (Ministry of Enterprise Development, 2012). As a result, donor agencies require certain standards of financial accountability from their aid recipients (Mir & Rahaman, 2005; Singh & Newberry, 2009). The findings from the Sri Lankan interviews further reveal that SMEs are required to provide their financial information when they obtain permits and/or contracts from government institutions. These are the reasons why government institutions can be considered a user of SME financial information in Sri Lanka. Apparently, government institutions as a user of SME financial information confirms that context is an important dimension that has an impact on users of SME financial information. Non-manager owners, customers, and suppliers are not identified as users of Sri Lankan SME financial information. Overall, these findings do not accord with the list of users identified by the IASB in the *IFRS for SMEs* (International Accounting Standards Board, 2009b).

The function of financial statements as perceived by respondents in this research, is not to serve users' information needs, rather for taxation purposes. As a result, Sri Lankan SME users perceive financial statements are of limited value in making their financial decisions. Unreliable financial information due to tax oriented financial reporting, lack of detail and lack of up-to-date financial information are the main weaknesses in the SME financial statements as perceived by bank lending and income tax officers. Most SMEs obtain services from external accountants to prepare financial statements. However, the quality and credibility of those external accountants, who provide accounting and auditing services to SMEs, are concerns expressed by both bank lending and income tax officers in Sri Lanka. Therefore, immediate attention should be given to address these concerns relating to the professional standards of those providing accounting services.

Bank lending officers use financial information relating to profitability, cash flows, and gearing when they make lending decisions to SMEs. Rather than relying on the information contained in the financial statements, bank lending officers verify the accuracy of the financial statements and prepare their own reports, such as projected cash flow, profit and loss and balance sheet, by interviewing the owners and/or visiting the business premises. Management accounting information, rather than financial information produced in annual financial statements, plays an important role in this regard.

Income tax officers obtain additional detailed financial information (such as turnover, expenses, creditors and debtors), from SMEs at the time when SMEs submit their annual tax returns. It is not compulsory for SMEs to produce cash flow statements. Income tax officers compare one SMEs financial information, such as industry trends and mark ups, with other SMEs in the same industry to reveal any abnormalities in performance. Further, they gather information from other government agencies (such as the Registrar of Motor Vehicles, and the Land Registration Department), and make site visits to cross-check the data provided in the annual returns to the Inland Revenue Department.

Owner-managers use their entity's financial statements primarily for calculating income tax liabilities rather than for management purposes. The profit and loss statement is regarded as the most useful source of data for management decisions. However, the interviewees share that separate sets of accounts are prepared internally for the owner's decision making purposes. The majority of owner-managers used budgets, management accounts, and bank reconciliation to support their business decisions. Management information is perceived by owner-managers to be more useful than annual financial statements, since they provide accurate, detailed, and up-to-date information about the entity's business operations.

RQ2: Do Sri Lankan SMEs need internationally comparable financial information?

The IASB argues that the need for global SME financial reporting standards arises out of the international structures and activities of SMEs and their financial statement users (International Accounting Standards Board, 2009a). However, findings from the interviews reveal the decision to adopt *IFRS for SMEs* in Sri Lanka is significantly related to institutional pressures rather than any benefits of internationally comparable financial information, as envisaged by the IASB. Based on the findings, this thesis concludes that coercive and normative institutional isomorphism are intertwined in shaping *IFRS* adoption in Sri Lanka.

Coercive isomorphism causes the most profound impact on the country's decision to adopt *IFRS for SMEs*. Accounting literature supports the claim that coercive institutions have an impact leading to the adoption of international standards. For example, Al-Omari (2010), Hassan (2005), Irvine (2008) and Mir and Rahaman (2005) indicate that international funding bodies such as the World Bank exert coercive pressures to developing countries to implement the *IFRS*. Similarly, the World Bank exerts coercive pressure on CASL to adopt *IFRS* as promulgated by the IASB. Further, the World Bank provides financial support for implementing the *IFRS for SMEs*. The rationale underlying these institutional influences is primarily financial dependence (DiMaggio & Powell, 1991; Oliver, 1991). Resource dominant actors such as the World Bank, Asian Development Bank and International Monetary Fund force the adoption of *IFRS* by recipients of their finance. Thus, the *IFRS for SMEs* adoption decision determined at the country level is then transmitted to more specific SME level (Irvine, 2008) by the CASL which has the sole authority for setting accounting standards in Sri Lanka. The CASL did not obtain comments and consultancies from government institutions during the review of *IFRS for SMEs*. It appears from the interview results that the influence of local users' needs and the government interference on the development of accounting standards does not exist in Sri Lanka.

Consistent with previous research (see, Albu et al., 2011; Jones & Higgins, 2006; Joshi & Ramadhan, 2002) the findings of this thesis reveal that external audit firms exert normative pressure on Sri Lankan SMEs to adopt *IFRS for SMEs*. Sri Lankan small and mid-tier audit firms, who provide accounting and auditing services to SMEs, encourage the adoption of *IFRS for SMEs*. According to interviewees, auditors provide advice on how to interpret and apply accounting standards. It further appears SMEs who have owners and use accountants who are members of CASL, are likely to adopt *IFRS for SMEs*. This means that they are able to exert normative pressure on the organisation to adopt the *IFRS for SMEs*.

The majority of Sri Lankan SMEs are domestically based and financed locally. Hence, international activities such as foreign exports, borrowings, and ownership are relevant to them. Limited resources, limited capabilities and a lack of government incentives were identified as barriers for Sri Lankan SMES to engage in cross border activities. It seems that expanding business operations globally is not a primary concern of Sri Lankan SME owner-managers. Their focus is on survival. Accordingly, Sri Lankan SMEs do not perceive the need to provide internationally comparable accounting information. Large SMEs have more cross-border activities than the small and medium SMEs. Entity size and the level of international activities have an impact on an entity's need to provide internationally comparable accounting information. This finding is consistent with the study conducted by Eierle and Haller (2009) in Germany. However, German SMEs have considerably more cross-border activities (foreign exports and foreign imports) than SMEs in Sri Lanka.

The questionnaire survey of owner mangers and accountants of SMEs show that the majority of the entities surveyed did not have transactions with most of the accounting-related topics included in the accounting standard *SLFRS for SMEs*. The majority of the respondents indicate that investment in non-listed companies, investment listed companies, joint ventures, government grants, purchase/sale of goods and services in foreign currencies, foreign exchange rate loans and borrowings, foreign exchange risk resulting from a customer order or a supplier, had never occurred in their business. A range of possible reasons is that the majority of Sri Lankan SMEs do not operate in a group structure and their activities are commonly limited to a single product line. Another reason is that majority of Sri Lankan SMEs are based domestically and use local sources of finance. Similarly, Aboagye-Otchere and Agbeibor (2012) establish that more than two-thirds of the accounting issues addressed in the *IFRS for SMEs* are of little or no relevance to SMEs in Ghana. In their study carried out with German SMEs, Eierle and Haller (2009) found that three-quarters of the responding SMEs encounter the following accounting issues only seldom or not at all, or are of little or no relevance: the sale of business/discontinued operations, leases in which the company acts as lessor, share-based payments, transactions to hedge price or exchange risks (except foreign exchange risk in a foreign currency position), investment in listed associates and listed subsidiaries (Eierle & Haller, 2009).

Despite the fact that the goal of the IASB in issuing the *IFRS for SMEs* was to reduce the burden of preparing SMEs' financial statements, the participants to the questionnaire survey and interviews were not convinced that this would be achieved in the Sri Lankan context. The adoption of *IFRS* is a financial burden for SMEs mainly due to increase costs of auditors and accountants and fair value calculations. Auditors charge higher fees to compensate their additional effort (Charles et al., 2010; George et al., 2013; Ghosh & Pawlewicz, 2009). In line with previous research (Carsberg et al., 1985; Kitching et al., 2011; Marriott & Marriott, 2000; Professional Oversight Board for Accountancy, 2006), it was found that the majority of Sri Lankan SMEs are heavily depend on external accountants. The use of external accountants for the bookkeeping and preparation of financial statements tasks was more often the practise of the small and medium SMEs than in the large SMEs. External accountants are used to prepare the financial statements due to a lack of qualified staff and knowledge of the *SLFRS for SMEs* within SMEs.

The application of fair value measurements in Sri Lanka also appears to be costly and challenging. A lack of qualified valuers, an absence of guidance on fair value calculations and an inactive market in Sri Lanka were the major problems of applying fair value in Sri Lanka. Income tax officers have issues with the reliability and accuracy of fair value figures presented in the SME financial statements. Interviewees spoke of how SMEs consult their audit firms regarding the fair value calculations. Employing consultants adds an additional financial burden on SMEs. Even though the majority of respondents to the questionnaire survey identified 'comparability' and 'easy access to finance' as benefits of adopting *SLFRS for*

SMEs, owner-managers and accountants who participated to interviews do not believe that *SLFRS for SMEs* increase the comparability of financial statements nor do they ease access to finance. This is surprising, since the *IFRS for SMEs* was promoted by the standard setters on that basis. Interviewees further identify that collateral based lending is dominant in SME lending decisions by Sri Lankan banks. This means owner-managers have problems of gaining access to finance due to collateral issues. The *SLFRS for SMEs* does not solve issues arising from a lack of collateral. These are the reasons for not identifying ‘easy access to finance’ as a benefit of *SLFRS for SMEs* by the interview participants. The majority of respondents indicate that the costs of preparing financial statements in compliance with *SLFRS for SMEs* exceeded the benefits.

12.4 Proposed financial reporting framework for Sri Lankan SMEs

A draft financial reporting framework was developed based on the findings obtained through both the questionnaire survey and interviews. This draft framework was then evaluated with the feedback given by the interviewees who participated to the follow-up interviews. The draft framework was refined accordingly and a modified framework was proposed. Figure 13 present an overview of the proposed framework. This four-tier reporting framework is designed to be applied to four categories of SMEs.

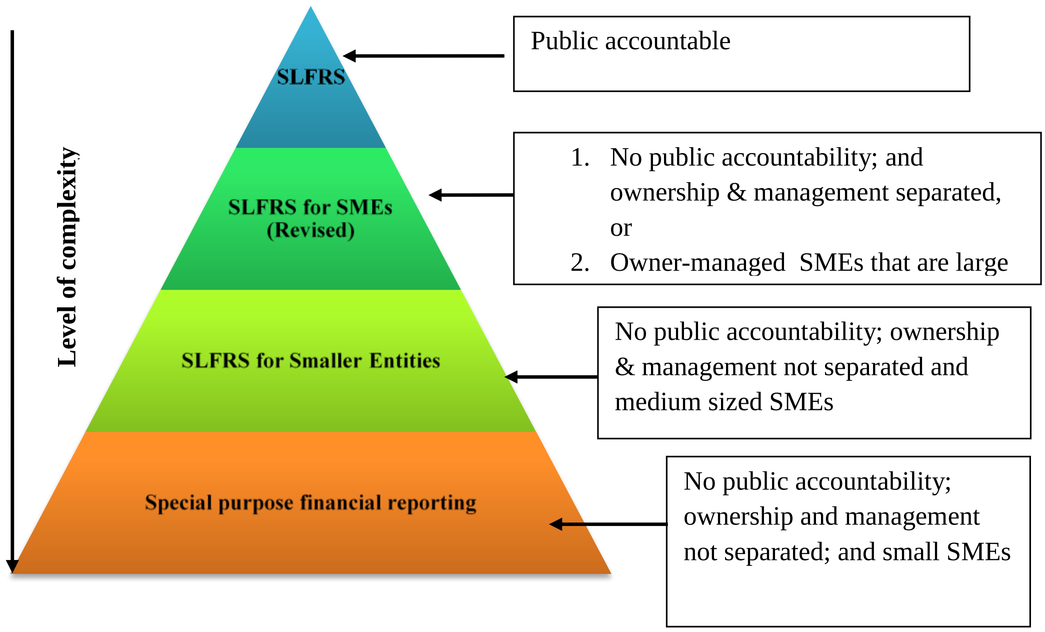

Figure 13 : An overview of the proposed financial reporting framework for SMEs
Source: Author

The proposed framework is based on the needs of the financial information users and with cost-benefit considerations for Sri Lankan SMEs. The proposed framework differs from the current financial reporting framework for Sri Lankan SMEs in three aspects. First, it proposes 'users' needs' as the guiding principle to determine the financial reporting requirements of SMEs. Three proxies are used to determine whether dependent users exist for such entities: (1) public accountability; (2) separation of ownership and management; and (3) entity size. According to these three criteria, the SME definition contained in the current financial reporting framework for Tier 2 and Tier 3 are revised. Second, the proposed framework suggests revising the accounting standard *SLFRS for SMEs* to reflect the financial reporting needs of Sri Lankan SMEs, since (as findings reveal) most SMEs do not engage in complicated transactions such as investment in listed companies, non-listed companies and joint ventures, and do not have many (if any) cross-border activities. Third, the proposed framework introduces special purpose financial reporting for owner-managed small SMEs. The finding indicate that most Sri Lankan SMEs are owner-managed and prepare financial information only for taxation purposes. Therefore, according to the proposed framework, the majority of owner managed Sri Lankan SMEs are not required to prepare general purpose financial information, instead they will prepare special purpose financial information.

The special purpose financial reporting format would also support applications for bank financing when the bank lending decisions are not solely based on the financial statements but also on available collateral or other evaluation mechanisms not directly related to the financial statements. Under the special purpose financial reporting format, SMEs should prepare their financial information based on double entry methods of recording financial transactions; and the principles of accrual accounting. It utilises historical cost as the valuation basis. It is argued that a significant number of Sri Lankan SMEs would benefit from the proposed framework utilising the 4-tier classification.

12.5 Contribution of this thesis

This thesis makes several contributions both to knowledge, and to practitioners. Because there is a considerable gap in the literature relating to developing countries and Sri Lanka in particular, this research provides rich data on SME financial reporting. The research findings and the development of the financial reporting framework provide useful insights for the CASL to attend to problems with, and issues raised following adoption of the current financial reporting framework for Sri Lankan SMEs. The proposed SME financial reporting framework makes an important contribution because findings of the thesis reveal that users of SME financial information demand reliable and relevant information. This thesis extends existing knowledge on how SMEs in developing countries meet information needs of the users of financial information. The proposed framework responds to those information needs while reducing the financial reporting burden on SMEs. Consequently, the findings of this thesis make a valuable contribution to the work of practitioners such as local and international standards-setters and regulators who may be considering developing/revising financial reporting framework for SMEs either worldwide or in developing countries.

The thesis makes important contributions to the existing literature. This thesis addresses a gap in the literature relating to the SME users and their financial information needs, especially in developing countries. Perceptions of various user groups of SME financial information including bank lending and income tax officers, government institutions were obtained in order to answer research questions of this thesis. This provides an opportunity to obtain a comprehensive and holistic understanding of different SME user groups, unlike other studies in developed countries that survey only a few users of SME financial information.

The adoption of the *IFRS by SMEs* has not been adequately explored in the context of developing countries. Therefore, findings of the thesis make a contribution to the existing literature by providing an empirical study from a developing country, Sri Lanka. Additionally, the findings about the need of internationally comparable financial information for SMEs, and the costs and benefits of *IFRS* adoption, provide useful insights to the IASB and other standard setters for planning a review of the *IFRS for SMEs.* Also, developing countries, particularly the Asian countries such as Nepal and Thailand where adoption of *IFRS for SMEs* is underway (International Financial Reporting Standards Foundation, 2016), could benefit from the experiences and wisdom gained from the Sri Lankan adoption of the *IFRS for SMEs*.

This thesis makes another contribution through its methodology. The mixed method approach employed, assists in gathering rich data on SME financial reporting. While the interviews provide in-depth understanding of research issues associated with financial reporting by SMEs, the questionnaire survey helps to verify and extend the findings through the wider distribution. By doing so, reliability and validity of the research findings are enhanced.

The thesis contributes to the literature by adopting institutional theory to interpret the empirical findings and to understand *IFRS for SMEs* adoption by Sri Lankan SMEs. The thesis also contributes to understanding the decision to adopt *IFRS for SMEs* both at country and SME level - an extension of prior research that generally concentrates on the *IFRS* adoption decision at either country or firm level. Prior research focused on the full *IFRS* adoption by large and/or listed companies. SMEs' decision to adopt the accounting standard *IFRS for SMEs* has not been explored using New Institutional Sociology theory. This thesis fills a gap by examining the adoption of the *IFRS for SMEs* (not the full *IFRS)* and extends the applicability of NIS theory.

12.6 Implications for policy and practice

The findings of this research have several implications for policy makers, and standard setters positioned to develop the financial reporting framework for SMEs in Sri Lanka, and for consideration by other developing countries.

12.6.1 Implications for policy making

Government intervention in the accounting standards setting process is low in Sri Lanka. For example, the Ministry of Finance, and the Ministry of Industry and Commerce do not actively participate and are not consulted in the process. Results indicate adoption and implementation of the *IFRs for SMEs* are dominated by international organisations and CASL. Government should participate in the standard setting process to protect users' interests and prevent domination by organisations that are external to the country and may have allegiances with non-Sri Lankan interests. It appears that poor governance and low enforcement of rules and regulations in Sri Lanka impact on the quality and credibility of SME financial reporting. For example, SMEs tend to alter their financial information for tax purposes. Policy makers should adopt effective mechanisms to minimise non-compliance with rules and regulations of the country.

12.6.2 Implications for Sri Lankan standard setter

The findings of this thesis indicate that the current financial reporting framework based on the general purpose financial reporting is not suitable for Sri Lankan SMEs as it ignores the financial information needs of key users such as owner mangers and Inland Revenue Department of Sri Lanka. The results further reveal that the adoption of *IFRS for SMEs* is a burden more than a benefit to Sri Lankan SMEs. Therefore, the CASL should re-examine the current financial reporting framework for Sri Lankan SMEs and consider the proposed framework as developed in this thesis.

The preparation and provision of financial information by SMEs under the current framework, do not meet the needs of users. Users have major concerns over the reliability of financial information due to tax oriented financial reporting of Sri Lankan SMEs. The research results suggest that CASL should pay a greater attention to SME financial reporting and take steps to make it credible, relevant, and appropriate to the financial reporting needs of users of SME financial information.

Even though CASL conducted various training programmes on *SLFRS for SMEs*, findings indicate most of the owner-managers, accountants, and users of SME financial information are not familiar with the standard. This raises questions regarding the benefit of the content of current training programmes of CASL. CASL should conduct customised training on *SLFRS for SMEs* for the Inland Revenue Department, bank lending officers, small and mid-tier audit firms, and SMEs. Findings also suggest that small and mid-tier audit firms need to enhance their competencies on the application of *SLFRS for SMEs*.

At present, setting accounting standards in Sri Lanka is the responsibility of the CASL. The findings from interviews reveal that standards setting process is dominated by the chartered accountants. It is recommended that the CASL should revise the composition of the bodies involved in the standard setting process in Sri Lanka to ensure that users of accounting information such as owners of SMEs, bank lending officers, income tax officers, and government institutions also contribute to the accounting standards prepared for Sri Lankan SMEs in the future.

Sri Lankan SMEs depend upon and obtain support from external professional accountants for preparing financial statements in compliance with *SLFRS for SMEs*. This implies that SMEs lack of internal accounting expertise and the complexity of *SLFRS for SMEs*. Therefore, they have to incur additional costs for this reporting task. Given the significant cost burden to SMEs, the majority of participants are in favour of a simplified financial reporting standards for Sri Lankan SMEs. The results provide a signal that greater effort is required to revise and simplify the *SLFRS for SMEs* to ease the financial reporting burden of SMEs. Results reveal that most of the accounting topics of the *SLFRS for SMEs* are not relevant to Sri Lankan

SMEs, especially to small SMEs. Accordingly, CASL should consider omitting from the *SLFRS for SMEs* topics such as: Investment in non-listed companies, Investment listed companies, Joint venture, Government grants, Foreign exchange rate loans and borrowings, and Foreign exchange risk resulting from a customer order or a supplier.

Interview respondents express their concern about the use of fair value measurements in Sri Lanka, as currently there is a lack of qualified individuals, lack of guidelines for fair value calculations, and inactive market in Sri Lanka. If Sri Lanka adopts fair value accounting, these concerns should be addressed and resolved jointly by the CASL and the government.

12.6.3 Implications for the IASB and other countries

The results presented in this thesis have several implications for the IASB and countries that are currently undertaking convergence projects throughout the world. The findings provide useful insights to the IASB for planning the next review of *IFRS for SMEs*. Since the IASB did not pay sufficient attention to SMEs in developing countries, findings of the thesis could assist them in determining the need for a global accounting standard for these entities. Findings on types of SMEs that would benefit from an international financial reporting standards could offer fruitful insights for both local and international standard setters in deciding the most appropriate financial reporting frameworks for the SME sector.

Moreover, the findings of this research regarding the complexity of the standards as the most undesirable feature of *IFRS for SMEs* highlight the need for the IASB to reduce complexity of the *IFRS for SMEs*. Overall, these findings suggest the IASB places a strong focus on the developing countries as they seek global convergence with *IFRS for SMEs*.

12.7 Limitations of this thesis

The outcomes of this research are subject to several limitations and the findings should be interpreted in the light of these limitations. First, the research is set in the context of a developing country. There are limitations relating to the adequacy of the sample frame as there is no comprehensive database of SMEs in Sri Lanka. The smallest of SMEs (0-4 employees) are omitted from this research because the database used by this research does not include SMEs that have 0 to 4 employees. The lack of comprehensive databases of business entities is common in developing countries and may be this is why research into SMEs in Sri Lanka is scarce.

Second, the World Bank definition from the *Enterprise Survey of Sri Lanka* was used to define SMEs in this thesis as no standard definition of SMEs in Sri Lanka existed at the time of data collection. Whilst interpretation of the findings may be enhanced for making comparisons with other studies using the World Bank definitions, interpretation within Sri Lanka may be hindered through the use of an external definition of SME.

Third, this thesis covers some topics within the IFRS for SMEs that might be subject to change in the foreseeable future, thus limiting the results to the time prior to any update of these topics. Fourth, the criteria such as the number of employees and turnover are not necessarily good indicators of the size of SMEs in Sri Lanka. The reason for this is that Sri Lanka operates largely as a cash-based economy. As such records of turnover and the number of employees may be understated and therefore not accurate. Finally, the research is limited to a single country. The data were collected from SMEs in Sri Lanka, as intended by the research boundary. However, different jurisdictions have different institutional settings, different accounting regimes, and may define SMEs according to different criteria, so that generalisation of the results to other jurisdictions may have limited application and relevance. However, inter-country comparisons are enhanced through such 'one country' boundaries during research.

12.8 Recommendations for future research

The thesis provides the foundation for future studies. It is recommended future research be undertaken

- To compare findings of this research with those that use another sampling frame and a different SME definition particularly in light of the new SME definition to be introduced by the government in Sri Lanka.

- To explore how the *IFRS for SMEs* is perceived and used by respondent groups such as external professional accountants, officers of chamber of commerce, and regulators.

- To investigate users' perspectives of whether the *IFRS for SMEs* fulfils user needs for financial information based on disclosure requirements.

- To examine Sri Lanka's decision to adopt the accounting standard *IFRS for SMEs* using institutional entrepreneurship approach of institutional theory.

- To undertake studies in other developing countries to gain comparative insights regarding the relevance and impact of the *IFRS for SMEs*.

- To examine the application of the proposed financial reporting framework developed for Sri Lankan SMEs in this thesis with a large sample of SMEs.

12.9 Conclusion

This thesis was conducted with the overarching aim of improving the financial reporting framework for Sri Lankan SMEs. SMEs make up the majority of business entities in the country and as such are important economic contributors. The findings reported in this thesis reveal several important features of SME financial reporting. Inland Revenue Department, owner-managers, and banks are identified as the most important users of SME financial information. Government institutions are also identified as users. Large SMEs are likely to identify government institutions as a user of financial information. An important finding of the study is that the perceived main users and owner-managers' needs of SME financial information varied according to entity size. Based on this finding, it is argued that, there is a need to distinguish between small, medium, and large SMEs for financial reporting purposes.

It becomes clear that the stewardship is not one of the main objectives of SME financial reporting in Sri Lanka since most of the SMEs are owner managed and non-manager owners are not identified as an important user of SME financial information. Users of SME financial information perceive little decision usefulness of SME financial statements due to tax oriented financial reporting and lack of detail and lack of up-to-date information. Overall, the finding with regard to users of SME financial information supports the critique of the adoption of a conceptual framework for financial reporting designed for large and listed companies for SME reporting (Di Pietra et al., 2008; Evans et al., 2005). Therefore, general purpose financial reporting model is not relevant or applicable to owner managed SMEs that do not have users who depend on their financial statements for making decisions.

The decision to adopt *IFRS for SMEs* in Sri Lanka was not driven by the needs of SMEs and their users of financial information, but was rather imposed on them by organisations such as the World Bank, IASB and the CASL. While the political, cultural, economic, and social situation in Sri Lanka may not be identical to that in other nations, much of the experience in Sri Lanka is anticipated to be useful to other developing countries in the region. Countries seeking financial assistance from international donor institutions are also likely to be affected by pressures from these institutions to improve their accounting regimes. However, findings confirm that reforms to legal, regulatory and governance systems within the jurisdiction are required to successfully adopt a financial reporting regime (Hassan et al., 2014). Otherwise, the adoption may be seen as simply symbolic (DiMaggio & Powell, 1983).

Though the accounting standard *IFRS for SMEs* is a simplified version of the full *IFRS*, the implementation of this set of standards seems to be more of a burden than a benefit to Sri Lankan SMEs, especially small and medium-sized SMEs. From the empirical results it is indicated that the *SLFRS for SMEs* is not deemed to be relevant to small and medium-sized SMEs in Sri Lanka as most of them domestically based and financed locally. As indicated by Sy and Tinker (2013) international financial reporting standards may benefit multinational corporations, and their Big Four accounting firms, but companies with primarily domestic operations will not receive the same benefit. The desirability of international financial reporting standards for SMEs therefore, still remains uncertain and further simplification to the *SLFRS for SMEs* is suggested if this is to be maintained as a financial reporting standards for Sri Lankan SMEs. Individual countries have unique circumstances which may make standards more difficult to understand or to apply to than in other countries. Findings of this thesis positively contribute to the development of an up-to-date, relevant financial reporting framework for Sri Lankan SMEs.

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APPENDICES

Appendix A: Content of the *SLFRS for Smaller Entities*

Chapter	**Description**
1	Scope of this SLFRS
2	Concepts and Pervasive principles
3	Presentation of financial statements
4	Accounting policies, estimates and errors
5	Inventories
6	Property, plant and equipment
7	Leases
8	Employee benefits
9	Revenue
10	Provisions and contingencies
11	Borrowing cost
12	Foreign currency translation
13	Related party disclosures
14	Government grants
15	Other assets and liabilities
16	Events after the end of the reporting period
17	Transition to SLFRS for SMEs

Source: Institute of Chartered Accountants of Sri Lanka (2015)

According to *SLFRS for Smaller Entities*, a complete set of financial statements of an entity shall include all of the following: a statement of assets and liabilities; a statement of profit or loss and retained earnings for the reporting period; a statement of cash flows for the reporting period; and notes, comprising a summary of significant accounting policies and other explanatory information.

Comparison of *SLFRS for Smaller Entities* with *SLFRS*

SLFRS Reference	Description of SLFRS	Requirements in SLFRS for Smaller Entities
SLFRS 1	First-time adoption of Sri Lanka Accounting Standards (SLFRSs)	Simplified
SLFRS 2	Share-based payment	Not included
SLFRS 3	Business combinations	Not included
SLFRS 4	Insurance contracts	Not included
SLFRS 5	Non-current assets held for sale and discontinued operations	Not included
SLFRS 6	Exploration for and evaluation of mineral resources	Not included
SLFRS 7	Financial instruments: Disclosure	Modified
SLFRS 8	Operating segments	Not included
SLFRS 9	Financial instruments	Not included
SLFRS 10	Consolidated financial statements	Not included
SLFRS 11	Joint arrangements	Not included
SLFRS 12	Disclosure of interests in other entities	Not included
SLFRS 13	Fair value measurement	Not included
SLFRS 14	Regulatory deferral accounts	Not included
SLFRS 15	Revenue from contracts with customers	Modified
LKAS 1	Presentation of financial statements	Simplified
LKAS 2	Inventories	Simplified
LKAS 7	Statement of cash flows	Not included
LKAS 8	Accounting policies, changes in accounting estimates and errors	Simplified
LKAS 10	Events after the reporting period	Simplified
LKAS 11	Construction contracts	Simplified
LKAS 12	Income taxes	Modified
LKAS 16	Property, plant and equipment	Simplified
LKAS 17	Leases	Modified
LKAS 18	Revenue	Simplified
LKAS 19	Employee benefits	Modified
LKAS 20	Accounting for government grants and disclosure of government assistance	Simplified
LKAS 21	The effects of changes to foreign exchange rates	Simplified
LKAS 23	Borrowing costs	Modified
LKAS 24	Related party disclosures	Simplified
LKAS 26	Accounting and reporting by retirement benefit plans	Not included
LKAS 27	Consolidated and separate financial statements	Not included
LKAS 28	Investment in associates	Not included
LKAS 29	Financial reporting in hyperinflationary economies	Not included
LKAS 31	Interests in joint ventures	Not included
LKAS 32	Financial instruments: Presentation	Modified
LKAS 33	Earnings per share	Not included
LKAS 34	Interim financial reporting	Not included
LKAS 36	Impairment of assets	Modified

Source: Institute of Chartered Accountants of Sri Lanka (2015)

Comparison of *SLFRS for Smaller Entities* with *SLFRS for SMEs*

SLFRS for SMEs chapter	**Description of chapter in *SLFRS for SMEs***	**Requirements in SLFRS for Smaller Entities**
1	Small and medium sized entities	Not applicable
2	Concepts and pervasive principles	Simplified
3	Financial statement presentation	Simplified
4	Statement of financial position	Simplified
5	Statement of comprehensive income and income statement	Simplified
6	Statement of changes in equity and statement of income and retained earnings	Simplified
7	Statement of Cash flows	Not included
8	Notes to the financial statements	Simplified
9	Consolidated and spate financial statements	Not included
10	Accounting policies, estimates and errors	Simplified
11	Basic financial instruments	Modified
12	Other financial instruments issues	Modified
13	Inventories	Simplified
14	Investments in associates	Not included
15	Investment in joint ventures	Not included
16	Investment property	Modified
17	Property, plant and equipment	Simplified
18	Intangible assets other than goodwill	Not included
19	Business combinations and goodwill	Not included
20	Leases	Modified
21	Provisions and contingencies	Simplified
22	Liabilities and equity	Modified
23	Revenue	Simplified
24	Government grants	Clarified
25	Borrowing costs	Modified
26	Share-based payment	Not included
27	Impairment of assets	Modified
28	Employee benefits	Modified
29	Income tax	Modified
30	Foreign exchange translation	Simplified
31	Hyperinflation	Not included
32	Events after the end of the reporting period	Simplified
33	Related party disclosures	Simplified
34	Specialised activities	Not included
35	Transition to SLFRS for SMEs	Modified

Simplified means the requirements have been simplified without significant modification to the principles on which the chapter was based.

Modified means the requirements have been significantly modified to reduce complexity and improve cost effectiveness for a smaller entity.

Not included means the requirements of the chapter have not been included.

Appendix B: Interview Guide – English version

Interview Guide

Research Title: Towards the development of a financial reporting framework for Sri Lankan SMEs

1. **The participants will be provided the following information through participant information sheet before the interview starts.**

   Title of the research

   Researcher's name and contact information

   Purpose of the research study

   Type of data/information expected to be collected through interviews

   Expected duration of the interview

   Confidentiality

   Rights of interviewees

   What will happen to the information collected from participants

Group 1: Owners and accountants of SMEs			
Introduction	The participants will be provided with a participant information sheet before the interview starts. Introduce myself and say thank you to owner/accountant for agreeing to meet with me Explain briefly about the research project (with an informed consent form) If needed, provide a brief overview of the financial reporting by SMEs Ask for permission to tape record and obtain the participant's signature on a consent form.		
Part	**Main question**	**Sub questions**	
I. General information	Could you tell me about your business?	What is the business type of your entity?	
		How many owners does your entity have?	
		How many of them are held managerial positions of the entity?	
		What is your main type of business?	
		How many years has the entity been trading?	
		How many employees currently work in your entity?	
		What was the entity's turnover for the last financial year? (2014)	
II. Preparation of financial statements	Which types of financial statements do you prepare?		
	How does your entity keep records of business transactions?		
	Who normally prepares your entity's financial information?		
	Do you use the services of external professional accountants?	**If YES,** What are they?	

III. Users and uses of financial information	Who do you view as the main users of your entity's financial information?	Who normally receives a copy of the annual financial statements?	
	Apart from financial statements, is there any other financial information you prepare for these users?	**If YES,** What are they?	
		For what purpose?	
		How often?	
	For what purposes do you use your entity's financial information?		
	Which specific information or parts of financial statements are useful to you, personally, as sources of financial information for business decisions e.g. balance sheet, profit and loss account or notes?	How important/useful is it?	
	In addition to these statements, what additional information do you find useful for business decisions e.g. management accounts, budgets or bank reconciliation?	How important/useful is it?	
	What information would you find useful that is not currently shown		

	in the entity's financial statements for decision making?		
	What information do you consider should not be disclosed in the entity's financial statements?		
IV. Accounting standards for SMEs	What is your view on the role of accounting standards for SMEs?		
	Is it necessary to create criteria to classify SMEs that should apply the accounting standards?	**If YES**, What would you suggest as the criterion/criteria	
	Does your entity have any foreign activity?	**If YES,** What are they? (Foreign exports? Foreign imports? Foreign ownership? Borrowing from abroad?)	
	Does your entity need to provide internationally comparable accounting information?	**If YES,** Why?	
	In the course of your business, have you dealt with: Investment in non-listed companies? Investment in listed companies? Joint venture? Investment property? Construction contracts? Research and development projects within the company?	**If YES,** How often?	

	Government grants? Share based payments? Purchase/sale of goods and services in foreign currencies? Foreign exchange rate loans and borrowings?		
	Did your entity adopt the accounting standard *SLFRS for SMEs?*	**If YES,** ▪ How would you describe your own knowledge about *SLFRS for SMEs*? ▪ What are the costs of preparation of financial statements in accordance with *SLFRS for SMEs*? ▪ What are the benefits of preparation of financial statements in accordance with *SLFRS for SMEs*? ▪ What do you think about the relationship between the costs and the benefits an SME may receive from the preparation of financial statements in accordance with *SLFRS for SMEs*?	

		IF NO, ▪ What accounting standard/principles do you use when preparing financial statements? ▪ Are you aware of the new accounting standards entitled “Sri Lanka Accounting Standards for Smaller entities”? ▪ Will your entity be preparing financial statements in accordance with new accounting standards? (Sri Lanka Accounting Standards for Smaller entities)	Why/Why not?
Closing	Is there anything else you want to add? Thank you for your time		

Group 2: Banks, Taxation authority and Government institutions (External users)			
Introduction	The participants will be provided with a participant information sheet before the interview starts. Introduce myself and say thank you to officers representing Banks/Taxation authority/Government institutions Explain briefly about the research project (with an informed consent form) If needed, provide a brief overview of the financial reporting by SMEs Ask for permission to tape record and obtain the participant's signature on a consent form.		
Part	**Main question**	**Sub questions**	
I. General information	Could you please describe your main job functions?	Your position?	
		How long have you been working in this position?	
	To classify a company as an SME, which criteria would you use?	Please indicate the specific threshold(s) you use to classify an entity as an SME?	
II. Users and uses of financial information	What information sources about SMEs do you normally use for your job?		
	How do you access such information?		
	Do you use SME financial statements in your job?	**If NO,** Why do you not use them?	
		If YES, For what purposes do you use SMEs' financial statements?	

		Which specific information or parts of financial statements are used for your decision making?	
		How important/useful is it?	
		Does information provided in financial statements meet your information needs?	How or how do they not?
		Do you require additional information/any other sources of information not provided by financial statements? if yes please indicate the type of information you need	
		What information would you find useful but it is not currently shown SME financial statements?	
III. Accounting standards for SMEs	What is your view on the role of accounting standards for SMEs?		
	Is it necessary to create criteria to classify SMEs that should apply the accounting standards?	**If YES**, What would you suggest as the criterion/criteria	
	Do you consider that the adoption of the accounting standard *IFRS for SMEs* by SMEs will assist you to obtain additional relevant information for making decisions on SMEs?	**If YES,** How?	

	Did you see any improvement of financial reporting by SMEs after the adoption of the accounting standard *IFRS for SMEs*?		
	Do you believe if SME adopt the accounting standard *IFRS for SMEs*, your information needs will be met?	To what extent do you agree that information disclosed in SMEs financial statement under IFRS for SMEs meet your needs?	
	What do you think about using a one set of accounting standard for all SMEs?		
	What do you think about using simpler accounting standards for SMEs?	Do you foresee any impact on your decisions or the usefulness of information resulting from using financial statements prepared by simpler standards?	
	Which entities should use the simpler accounting standards?		
Closing	Is there anything else you want to add? Thank you for your time		

Group 3: Standards setter			
Introduction	The participants will be provided with a participant information sheet before the interview starts. Introduce myself and say thank you to officers representing the Institute of Chartered Accountants of Sri Lanka Explain briefly about the research project (with an informed consent form) Ask for permission to tape record and obtain the participant's signature on a consent form.		
Part	**Main question**	**Sub questions**	
I. General information	Could you please describe your main job functions?	Your position?	
		How long have you been working in this position?	
II. Users and uses of financial information	Who do you view as the main users of SME financial statements?		
	What are the financial information needs of these users?		
	Did your institution conduct any empirical studies on users and their information needs on SME financial reporting in Sri Lanka?	**If NO,** How did you assess users and their information needs of SME financial reporting?	
III. Accounting standards for SMEs	What is your view on the role of accounting standards for SMEs?		
	Did the institution receive any assistance from multinational lending agencies and donors (such as the World Bank, ADB, IMF) for the adoption of *SLFRS for SMEs?*	**If YES,** How?	

	Did the institution receive any assistance from the International Accounting Standards Board (IASB) for the adoption of *SLFRS for SMEs?*	**If YES,** How?	
	Do you consider that the adoption of the accounting standard *SLFRS for SMEs* will provide additional relevant information to users for making decisions on SMEs?	**If YES,** How?	
	Do you see any improvement of financial reporting by SMEs after adoption of the accounting standard SL*FRS for SMEs*?		
	What are the implications of *SLFRS for SMEs* on your institution? E.g. training etc.		
	What are the implications of *SLFRS for SMEs* on SMEs? e.g. costs etc.		
	Has the adoption of *SLFRS for SMEs* required any changes in legislation?		
	To what extent does the *SLFRS for SMEs* comply with taxation rules?		
	What is the level of compliance with *SLFRS for SMEs* by Sri Lankan SMEs?	Why does non-compliance with accounting standards exist?	

	Which entities should use *Sri Lanka Accounting standards for Smaller Entities*?		
	Are these entities' users and their information needs different from entities that adopt *SLFRS for SMEs*?	**If YES,** Please explain	
	Did the institution obtain comments from SMEs and their users of financial statements in formulating *Sri Lanka Accounting standards for Smaller Entities*?	**How?**	
Closing	Is there anything else you want to add? Thank you for your time		

Interview Guide – Sinhala version

සමීක්ෂක මඟපෙන්වීම

පර්යේෂණ මාතෘකාව : ශ්‍රී ලංකික සුළු හා මධ්‍ය පරිමාණ කර්මාන්තයන් සඳහා මූල්‍ය වාර්තා රාමුව සංවර්ධනය

සමීක්ෂණය පටන් ගැනීමට ප්‍රථමව සහභාගීවෙන්නන්හට සහභාගී තොරතුරු පත්‍රය හරහා පහත තොරතුරු ලබාදෙනු ලැබේ.

- පර්යේෂණ මාතෘකාව
- පර්යේෂක නම සහ සම්බන්ධතා තොරතුරු
- පර්යේෂණයේ අධ්‍යයන අරමුණ
- සම්මුඛ සාකච්ඡා මගින් රැස් කිරීමට අපේක්ෂිත තොරතුරු / දත්ත වර්ගය
- සම්මුඛ සාකච්ඡා සඳහා අපේක්ෂිත කාලය
- රහස්‍යභාවය
- සම්මුඛ පරීක්ෂකයන්ට ඇති හිමිකම්
- සහභාගීවන අයගෙන් රැස් කරගන්නා ලද තොරතුරු වලට කුමක් සිදුවන්නේද

1 කාණ්ඩය : සුළු හා මධ්‍ය පරිමාණ ව්‍යවසාය හිමිකරුවන් හා ගණකාධිකාරිවරුන්		
හැදින්වීම	• සමීක්ෂණය ආරම්භ කිරීමට පෙර සහභාගී තොරතුරු පත්‍රය ලබා දීමට කටයුතු කරනු ලැබේ. • තමන් පිළිබඳ හදුන්වා දීම සහ සාකච්ඡාවට එක්වීම සම්බන්ධයෙන් අයිතිකරු / ගණකාධිවරයාට ස්තුතිය ප්‍රකාශ කරන්න • පර්යේෂණ ව්‍යාපෘතිය ගැන කෙටියෙන් පැහැදිලි කරන්න (තොරතුරු ලබාදීමට කැමැත්ත ලබාදුන් ෆෝර්මය සමග) • අවශ්‍ය නම්, සුළු හා මධ්‍ය පරිමාණ කර්මාන්තයන්හී මූල්‍ය වාර්තා පිළිබදව දළ විශ්ලේෂණය සැපයීම • පටිගත කිරීමට අවසර ඉල්ලීම සහ තොරතුරු ලබාදීමට කැමැත්ත ලබාදුන් ෆෝර්මයේ අත්සන ලබා ගැනීම	
කොටස	**ප්‍රධාන ප්‍රශ්නය**	
I. **සාමාන්‍ය තොරතුරු**	ඔබේ ව්‍යාපාරය ගැන මට තොරතුරු කියන්න පුළුවන්ද?	ඔබේ ආයතනයක් ව්‍යාපාර වර්ගය කුමක්ද?
		ඔබේ ආයතනයට හිමිකරුවන් කොපමණ සංඛ්‍යාවක් සිටින්නේද?
		ඔවුන්ගෙන් කොපමණ සංඛ්‍යාවක් ආයතනයේ කළමණාකරණ තනතුරු දරන්නේද?
		ඔබගේ ව්‍යාපාරයේ ප්‍රධාන වර්ගය කුමක්ද?
		මෙම ව්‍යාපාරය කොපමණ කලක සිට වෙළදාම් කටයුතු වල නිතර වන්නේද?
		ඔබ ආයතනය තුළ කොපමණ සේවක සංඛ්‍යාවක් රැකියාවේ නිතර වෙන්නේද?
		ආයතනයේ පසුගිය මූල්‍ය වර්ෂය සඳහා වූ පිරිවැටුම කුමක්ද? (2014)
II. **මූල්‍ය ප්‍රකාශ පිළියෙල කිරීම**	ඔබ සකසනු ලබන්නේ කුමන මූල්‍ය ප්‍රකාශ වර්ගයන්ද?	
	ඔබේ ආයතනයේ ව්‍යාපාර ගනුදෙනු වාර්තා තබා ගන්නේ කෙසේද?	
	ඔබේ ආයතනයේ මූල්‍ය තොරතුරු සකසනුලබන්නේ කවුරුන් විසින්ද?	
	ඔබ බාහිර වෘත්තීය ගණකාධිකාරිවරුන්ගේ සේවාවන් භාවිතා කරන්නේද?	**ඔව් නම්,** ඔවුන් කවුරුන්ද?
III. **මූල්‍ය තොරතුරු භාවිතා කරන පරිශීලකයන් හා එහි භාවිතයන්**	ඔබ දකින ආකාරයට ඔබේ ආයතනයේ මූල්‍ය තොරතුරුවල ප්‍රධාන පරිශීලකයන් කවුරුන්ද?	වාර්ෂික මූල්‍ය ප්‍රකාශනයේ පිටපතක් සාමාන්‍යයෙන් ලබා ගන්නේ කවුරුන් විසින්ද?
	මූල්‍ය ප්‍රකාශව වලට අමතරව, එම පරිශිලකයන් සදහා වෙනත් මූල්‍ය තොරතුරු සකසනු ලබන්නේද?	**ඔව් නම්,** ඔවුන් කවුරුන්ද?
		කුමක් සදහාද?
		කොපමන කලකට වරක්ද?

	කුමන අරමුණු සඳහා ඔබ ඔබේ ආයතනයේ මූල්‍ය තොරතුරු භාවිතා කරන්නේද?	
	ව්‍යාපාර තීරණ සඳහා, මූල්‍ය තොරතුරු මූලාශ ලෙස කුමන විශේෂිත තොරතුරු හෝ මූල්‍ය ප්‍රකාශක කොටස්ද ඔබට පෞද්ගලිකව වැදගත්වෙන්නේ? උදා ශේෂ පත්‍ර, ලාභ සහ අලාභ ගිණුම හෝ සටහන්?	එය කොතරම් වැදගත්ද/ ප්‍රයෝජනවත්ද?
	මෙම ප්‍රකාශවලට අමතරව, ඔබගේ ව්‍යාපාර තීරණ සඳහා ප්‍රයෝජනවත්වන වෙනත් අමතර තොරතුරු මොනවාද? උදා කළමනාකරණ ගිණුම්, අයවැය හෝ බැංකු සැසඳුම්?	එය කොතරම් වැදගත්ද/ ප්‍රයෝජනවත්ද?
	ඔබගේ ව්‍යාපාර තීරණ සඳහා ප්‍රයෝජනවත් වන නමුත් දැනට ආයතනයේ මූල්‍ය ප්‍රකාශන තුළ නොදක්වන වෙනත් අමතර තොරතුරු මොනාද?	
	ආයතනයේ මූල්‍ය ප්‍රකාශන තුළ ආවරණය නොකළ යුතු යැයි ඔබ සලකන තොරතුරු මොනවාද?	
IV. සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා ගිණුම්කරණ ප්‍රමිතීන්	සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා වන ගිණුම්කරණ ප්‍රමිතීන්ගේ කාර්යභාරය පිළිබඳව ඔබේ අදහස කුමක්ද?	
	සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත වර්ගීකරණය කිරීම සඳහා නිර්ණායක නිර්මාණය කිරීමට ගිණුම්කරණ ප්‍රමිතීන් භාවිතා කිරීමට අවශ්‍යයද?	**ඔව් නම්,** ඔබ නිර්ණායකය / **නිර්ණායක** වශයෙන් යෝජනා කරන්නේ කුමක්ද?
	ඔබේ ආයතනය හා සම්බන්ධ කිසියම් විදේශ කටයුතු තිබේද?	**ඔව් නම්,** ඒවා මොනවාද? (විදේශ අපනයන? ආනයන? විදේශ අයිතිය? පිටරටින් ණය ගැනීම?)
	අන්තර්ජාතිකව සංසන්දනාත්මක ගිණුම්කරණ තොරතුරු ඔබේ ආයතනයට අවශ්‍යද?	**ඔව් නම්,** ඇයි?
	ඔබේ ව්‍යාපාරය තුළදී ඔබ ගනුදෙනුකර තිබෙන්නේද: ලැයිස්තුගත නොවන සමාගම්වල ආයෝජන? ලැයිස්තුගත සමාගම් ආයෝජන? ඒකාබද්ධ ව්‍යාපාර?	**ඔව් නම්,** කොපමණ වාරයක්ද?

	දේපළ ආයෝජන? ඉදිකිරීම් කොන්ත්‍රාත්? ආයතනය තුළ පර්යේෂණ හා සංවර්ධන ව්‍යාපෘති? රජයේ ප්‍රතිපාදන? කොටස් පදනම් කරගත් ගෙවීම් විදේශ මුදල් තුළින් භාණ්ඩ හා සේවා මිලදී ගැනීම / විකිණීම? විදේශ විනිමය අනුපාත ණය සහ ණය ගැනීම්?	
	ඔබේ ආයතනය සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා වන ගණකාධිකරණ ප්‍රමිති සම්මතයන් අනුගමනය කිරීම ආරම්භ කළේද?	**ඔව් නම්,** ▪ ඔබ සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා වන සම්මතයන් ගැන ඔබේ දැනුම විස්තර කරන්නේ කෙසේද? ▪ සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා වන සම්මතයන්ට අනුකූලව මූල්‍ය ප්‍රකාශ පිළියෙල කිරීම සඳහා දැරිය යුතු පිරිවැය කුමක්ද? ▪ සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා වන සම්මතයන්ට අනුකූලව මූල්‍ය ප්‍රකාශ පිළියෙල කිරීමේ ප්‍රතිලාභ මොනවාද? ▪ සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා සම්මතයන්ට අනුකූලව මූල්‍ය ප්‍රකාශ පිළියෙල කිරීම නිසා ඔබේ වියදම්වල හා සුළු හා මධ්‍ය පරිමාණ ව්‍යවසායකයින්ට ලැබෙන වියදම් හා ප්‍රතිලාභ හි සම්බන්ධතාවය ගැන ඔබ සිතන්නේ කුමක්ද?

		නැත නම්, ▪ මූල්‍ය ප්‍රකාශ සකස් කරන විට ඔබ ගණකාධිකරණ ප්‍රමිතීන්/ප්‍රතිපත්ති ලෙස භාවිතා කරන්නේ මොනවාද? ▪ ඔබ "කුඩා ආයතන සඳහා වන ශ්‍රී ලංකා ගිණුම්කරණ ප්‍රමිතින්" යන නව ගිණුම්කරණ ප්‍රමිතීන් ගැන දැනුවත් ද? ▪ ඔබේ ආයතනයේ මූල්‍ය ප්‍රකාශ නව ගිණුම්කරණ ප්රමිතීන්ට අනුකූලව සූදානම් කරන්නේද? (කුඩා ආයතන සඳහා ශ්‍රී ලංකා ගිණුම්කරණ ප්‍රමිති)
අවසානය	මෙම සාකච්ඡාවට ඔබට එකතු කිරීමට අවශ්‍ය වෙනත් යමක් තිබේද? ඔබ ලබාදුන් කාලයට බෙහෙවින් ස්තුතියි	

Appendix C: Covering Letter: Interviews

Nisansala Wijekoon

Department of Accounting

Waikato Management School

University of Waikato

Private Bag 3105, Hamilton, New Zealand

Email Address: hnww1@students.waikato.ac.nz

Mobile: +64 221 955394; Office: +64 7838 4466 (Ext: 6419)

Dear Madam/Sir,

Request to participate in a survey questionnaire on "Towards the development of a financial reporting framework for Sri Lankan SMEs"

I am lecturer at the Department of Accountancy, University of Kelaniya and presently pursuing doctoral studies at the department of Accounting, Waikato Management School, University of Waikato, New Zealand. I am inviting your participation in the research study designed to identify small and medium enterprise users and their information needs as well as gather perceptions from preparers and users of SME financial statements on the SME financial reporting in general and the accounting standard International Financial Reporting Standards for Small and Medium- sized Entities (IFRS for SMEs) in particular.

Your participation is highly valued and will make a valuable contribution to study on an important issue for small businesses in Sri Lanka. I assure you that all information collected will be strictly confidential and used solely for my PhD studies. Real names of the company and /or participants will not be used in any subsequent reports or publications and all data will be analysed in a collective manner and any quotes will be anonymous. Please see the attached participant information sheet and consent form for more details.

If you are happy to participate, please send me an email so that I can contact you to set up a mutually convenient time for the interview.

I hope to receive a positive response.

Thanking you.

Yours Sincerely

Nisansala Wijekoon

Appendix D: Participant information sheet - Interviews

Waikato Management School
Te Raupapa

THE UNIVERSITY OF
WAIKATO
Te Whare Wānanga o Waikato

Project Title

Towards the development of a financial reporting framework for Sri Lankan SMEs

This study is a part of my PhD research programme, undertaken at the Department of Accounting, Waikato Management School, University of Waikato. The objective of this research is to develop a financial reporting framework for Sri Lankan SMEs. This study seeks to identify small and medium enterprise users and their information needs as well as gather perceptions from preparers and users of SME financial statements on the SME financial reporting in general and the accounting standard *International Financial Reporting Standards for Small and Medium- sized Entities (IFRS for SMEs)* in particular.

The face to face interview will be conducted by the researcher. The approximate time duration of the interview will be 30-45 minutes and a semi structured questionnaire will be used to ensure the proper direction of the interview. It is expected to note down the outcomes while the interview is going on and the whole discussion will be tape recorded.

The both forms of data (voice and written) will be available only for the researcher and the supervisors. The copies of written data and voice records will be kept under the responsibility of the researcher until the data are feed into the computer system. Data will be coded and aggregated in analysis. Therefore, the anonymity and the confidentiality of data are highly maintained. Real names of participants/organisations will not be used in research reports or publications. The researcher will use some interview transcribed data as quotations in the thesis. All notes and other transcribed data will be destroyed and all voice recorded will be deleted once the research is completed. The outcome of the research may be presented in academic conferences and published in academic publications.

When you participate in the interview, you will have the right to refuse to answer any particular question and to ask for further explanations on any matter arisen in the interview. Further, you will have the right to access the summary of the findings of the research when it is completed. Finally, you have the right to withdraw the data provided by you within 3 weeks of the interview.

Thank you.

If you have any questions or concerns about the project, either now or in the future, please feel free to contact either:

Researcher:
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Or

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Appendix E: Consent form for participants

Waikato Management School
Te Raupapa

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Te Whare Wānanga o Waikato

Research Title Towards the development of a financial reporting framework for Sri Lankan SMEs

I have read the **Participant Information Sheet** for this study and have had the details of the study explained to me. My questions about the study have been answered to my satisfaction, and I understand that I may ask further questions at any time. I also understand that I am free to withdraw from the study within three weeks of participation, or to decline to answer any particular questions in the study. I agree to provide information to the researchers under the conditions of confidentiality set out on the **Participant Information Sheet**.

I agree to participate in this study under the conditions set out in the **Participant Information Sheet**.

I agree that while participating in the study my responses and comments may be voice recorded for the purposes of the research analysis.

Signed: ____

Name: ____

Date: ____

Researcher:

Nisansala Wijekoon, Department of Accounting, Waikato Management School

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Appendix F: Demographic data of interviewees

Interviewee group	Interviewee	Gender	Position	Experience
Bank lending officers	01	Male	Head of Credit Division	12 years
	02	Male	Head of Micro Finance and SMEs	11 years
	03	Male	Credit Officer	6 years
	04	Male	Head of Credit Division	25 years
	05	Female	Manager - SME Loans	7 years
Income tax officers	01	Female	Assistant Commissioner	11 years
	02	Female	Assistant Commissioner	9 years
	03	Male	Assistant Commissioner	9 years
Representatives from government institutions	01	Male	Director, Development Finance	18 years
	02	Male	Additional Secretary	15 years
Representatives from the standard setting authority	01	Male	Head of Technical Division	8 years
	02	Female	Manager, Technical Division	5 years
SME accountants	01	Male	Chief Accountant	7 years
	02	Female	Senior Accountant	6 years
	03	Male	Accountant	8 years
	04	Female	Accountant	5 years
	05	male	Senior Accountant	23 years
	06	Male	Financial Accountant	11 years

Profile of owner managers

Owner manager	Gender	Number of years in the business	Number of employees	Type of business	Form of business
1	Male	13 years	28	Manufacturing	Private limited
2	Male	27 years	22	Manufacturing	Partnership
3	Male	7 years	15	Service	Sole proprietor
4	Male	8 years	22	Service	Private limited
5	Male	11 years	7	Manufacturing	Private limited
6	Female	27 years	35	Manufacturing	Private limited
7	Male	14 years	97	Manufacturing	Private limited
8	Male	30 years	14	Trading	Sole proprietorship
9	Male	23 years	42	Manufacturing	Private limited
10	Male	23 years	20	Service	Private limited
11	Male	20 years	16	Manufacturing	Private limited
12	Male	12 years	10	Manufacturing	Private limited
13	Male	22 years	45	Manufacturing	Private limited
14	Male	25 years	95	Service	Private limited
15	Male	23 years	31	Manufacturing	Private limited
16	Male	28 years	12	Manufacturing	Private limited
17	Male	38 years	98	Service	Private limited
18	Male	3 years	95	Service	Private limited
19	Male	21 years	52	Manufacturing	Private limited
20	Female	24 years	98	Service	Private limited
21	Male	26 years	94	Service	Private limited
22	Male	15 years	95	Manufacturing	Private limited
23	Male	10 years	55	Service	Private limited

Appendix G: Follow up interview questions for Users, and preparers of SME financial information

<u>New Accounting standard (*SLFRS for Smaller Entities*)</u>

1. Can you describe the financial reporting framework in your own words? Are there any problems or issues with the existing framework (see page 1 of financial reporting frameworks)?
2. Do you believe that the Institute of Chartered Accountants of Sri Lanka (CASL) adequately consulted with all stakeholders before issuing this standard?
3. Can you describe your experiences of working with the new accounting standard for smaller entities (*SLFRS for Smaller Entities*) issued in 2015 (see tier 3 of current financial reporting framework on page 1) by CASL?
4. What are your views on the new accounting standard for smaller entities (*SLFRS for Smaller Entities*)?
5. What do you see are the benefits of the *SLFRS for Smaller Entities* issued in 2015, for SMEs?
6. What potential problems do you envisage as a result of adopting the accounting standard *SLFRS for Smaller Entities* which was issued in 2015?
7. Will the current financial reporting framework address the problems associated with financial reporting for SMEs in Sri Lanka?

<u>Proposed financial reporting framework for SMEs (see page 2of financial reporting frameworks)</u>

1. Bearing in mind the recent changes to the Sri Lankan financial reporting framework, can you provide me with your view the proposed financial reporting framework (see page 2 of financial reporting frameworks) sent to you for comment?
2. Do you think that the new framework adequately address financial reporting problems of SMEs in Sri Lanka?
3. Any suggestions or recommendations on this proposed framework?

Follow up interview questions for the standard setter

New Accounting standard (*SLFRS for Smaller Entities*)

1. Why was a further tier introduced for smaller entities in Sri Lanka?
2. Did your institution conduct any empirical studies on users and their information needs before introducing this standard?
3. Did the institution receive any assistance from multinational lending agencies and donors for formulating/implementing this accounting standard? (such as the World Bank, IMF, and ADB)?
4. Did the institution obtain comments from SMEs and their users such as income tax officers, and bank lending officers in formulating *SLFRS for Smaller Entities?*
    a) If yes, who did comment on the standard?

Proposed financial reporting framework for SMEs (see page 2 of the financial reporting frameworks)

4. Bearing in mind the recent changes to the Sri Lankan financial reporting framework, can you provide me with your view the proposed financial reporting framework sent to you for comment?
5. Do you think that the new framework adequately address financial reporting problems of SMEs in Sri Lanka?
6. Any suggestions or recommendations on this proposed framework?

Appendix H: Themes, sub-themes, categories and sub-categories from qualitative data analysis

Theme 1 - Users of SME financial information		
Sub-theme	**Categories**	**Sub-categories**
Purpose of reporting	Financial accounting versus tax reporting	Legal requirement Filing income tax return
Perceived main users of SME financial information	External versus internal users	Banks Owner managers Inland Revenue Department Government institutions e.g ministries, BOI, Customs Suppliers and customers
Theme 2 - Use of financial information by owner managers		
Sub-theme	**Categories**	**Sub-categories**
Usefulness of SME financial statements for making business decisions Usefulness of profit and Loss statement	Not useful versus useful	Prepared for tax purpose Lack of accounting knowledge Lack of up to date financial information Lack of detailed financial information Check the income tax liability
Usefulness of management information	Not useful versus useful	Not technical and Easy to understand Up to date and accurate financial information about the entity Provide detail information
Types of management reports or information	Management accounts versus other management reports	Budgets Ratio analysis Cost analysis Production and Productivity plans Separate set of accounting records for owner managers Bank statements and cash flow reports Income and expenditure reports Creditors and debtors report Sales and purchases report
Purpose of using entity's financial information	Types of business decisions	Compare performances with previous periods Compare with targets Deciding on employees' salaries and bonuses Take investment decisions Take marketing decisions
Theme 3 - Use of financial information by bank lending officers		

Sub-theme	Categories	Sub-categories
Usefulness of SME financial statements for making lending decisions	**Limited use**	Not reliable due to tax oriented financial reporting No proper financial reporting due to Lack of knowledge among owner managers Financial statements are prepared for loan purposes
Usefulness of audit report	Limited use	Credibility of auditors and quality of the audit Big auditing firms versus Small and Medium Practitioners (SMPs)
Use of other financial information for lending decisions		Projected financial statements prepared by bank lending officers Ratio analysis Management accounting information and internal documents obtained through site visits and interviews with owners Cash flow position through bank statements Report from Credit Information Bureau of Sri Lanka (CRIB)
Use of other financial information for lending decisions		Collateral Nature of the business Business registration Character of the owner Production volumes through electricity, water, and telephone bills information from SMEs' suppliers and customers
Usefulness of financial statements for loan monitoring purposes	useful Not useful	Review annual financial statements Not reliable accounting information
Use of other information for loan monitoring purposes		monthly/quarterly inspections Check internal records for identifying any arrears with the bank or other banks
Theme 4 - Use of financial information by income tax officers		
Sub-theme	**Categories**	**Sub-categories**
Usefulness of SME financial statements for tax assessment		Understated figures in the financial statements Lack of detail information Qualifications of external accountants
Use of other financial information for tax assessment		Detail financial information including break ups of turnover, expenses, creditors and debtors paying site visits to obtain internal records of financial information Compare SME financial information with other SMEs in the same industry

		VAT returns to reconcile turnover
Use of non-financial information for tax assessment		Internal records and data base Information from customers, suppliers, and distributors Information from government agencies such as registrar of motor vehicles, and land registration department
Theme 5 - Internationally comparable accounting information		
Sub-theme	**Categories**	**Sub-categories/concept**
Perception on the usefulness of international accounting standards for SMEs	Positive, neutral and negative	Only for the compliance purpose Add no value to the business Limited use in taxation and management purposes Provide financial discipline
Relevance of international activities such as foreign exports, imports, borrowings and ownership	Not relevant versus relevant	Business operations limited to domestic markets Focus on survival than the internationalisation of the business Barriers for internationalisation such as limited resources, lack of government supports and incentives
Need for internationally comparable accounting information	Need versus no need	No request from foreign suppliers, customers and owners for financial information Check through other sources such as web sites, industry information, local agents, ISO certifications, and bank guarantees
Theme 6 – Adoption process, awareness and knowledge of IFRS for SMEs		
Sub-theme	**Categories**	**Sub-categories/concept**
Process of adoption of IFRS for SMEs	User involvement	Low government involvement Comment letters from other users
Pressures on adoption	Coercive	The World bank pressure The IASB's involvement CASL engagements and activities
	Normative	Audit firms provide consultancies, and recommendations for adoption SME accountants and owners' decision and recommendations for adoption
Knowledge and awareness of IFRS for SMEs	Low versus high	Owner managers were not aware about the IFRS for SMEs Owner managers were made aware by their external accountants Limited knowledge on IFRS for SMEs among income tax officers and bank loan officers
Theme 7 - Costs and benefits of preparing financial statements in accordance with IFRS for SMEs		
Sub-theme	**Categories**	**Sub-categories/concept**

Costs of IFRS for SMEs	Accounting and auditing fees for professional accountants	Depend on external accountants to prepare financial statements Complexity of international accounting standards Lack of qualified accountants in the organisation Costs of hiring and retaining qualified accountants
	Use of fair value accounting and gratuity calculation	Complex Time consuming costly No active market in Sri Lanka Reliability of valuations No qualified valuers and valuers data base in Sri Lanka
	Preference for Simplified financial reporting framework for SMEs	Capabilities of SMEs Cost of reporting
Benefits of *IFRS for SMEs*	General perception	Owners are not certain on benefits to entity clear presentation few more notes acceptance internationally
	Using for loan application	Not useful as banks largely use collateral based lending to SMEs compliance with accounting standards is not a necessary requirement for making lending decisions to SMEs.

Appendix I: Development of questionnaire instrument

Research questions	Investigative questions in the questionnaire	Link to question no:	Sources
RQ1: Who are the users of Sri Lankan SME financial statements?	Q: who do you view as the main users of your entity's/company's financial information? A:List of users	Q14	Dang-Duc, Marriott, and Marriott (2008) and the SLFRS for SMEs
	Q: Who normally receives a copy of the financial information? A: list of users	Q15	Collis and Jarvis (2000)
RQ2: What are the financial information needs of Sri Lankan SME users?	Q: Have you ever used the financial information of your entity/company for the following purposes? A: List of purposes: 5 rating with never, seldom to always	Q16	Collis and Jarvis (2000)
	Q: For what purposes do you use your entity's/company's financial information? A:List of (internal) uses	Q17	Page (1984) and Collis and Jarvis (2000)
	Q: How useful are the following financial information of your entity/company to you, personally, as sources for business decisions? A:List of reports: 5 rating with not useful, less useful to very useful	Q18	
	Q: In addition to the statements in Q18, what additional financial information do you find useful for business decisions? A:List of (internal) reports : 5 rating with not useful, less useful to very useful	Q19	
	Q: What information would you find useful for decision making that is not currently shown in the entity's/company's financial information? (opened question)	Q20	Collis and Jarvis (2000)

	Q: What information do you consider should not be disclosed in the entity's/company's financial information?	Q21	Collis and Jarvis (2000)
RQ4: Do Sri Lankan SMEs need internationally comparable financial statements?	Q: How relevant are the following foreign activities for your entity/company? A: List of foreign activities: 5 rating with no relevance, low relevance to very high relevance	Q24	Conseil National de la Comptabilité (2008) and Eierle and Haller (2009)
	Q: Is there any need for your entity/company to provide internationally comparable accounting information? A: 5 rating with no need, little need to very high need	Q25	Eierle and Haller (2009)
RQ5: Are the specific topics covered by the *IFRS for SMEs* relevant to Sri Lanka?	Q: How often do the following transactions/investments occur in your entity/company? A: list of specific accounting topics : 5 rating with never, seldom to very often	Q26	Conseil National de la Comptabilité (2008) and Eierle and Haller (2009)
RQ6: What are the costs and benefits of adopting the *IFRS for SMEs* in Sri Lanka?	Q: What is your view on the role of accounting standards for SMEs? A: 3 choices with different perceptions	Q28	
	Q: How significant is each of the following items in terms of costs for preparing financial statements in accordance with *SLFRS for SMEs* A:type of costs: 5 rating with not significant, less significant to very significant	Q29	Dang-Duc, Marriott, and Marriott (2008) and Albu et al. (2013)
	Q: What benefits do you think an SME will obtain from preparing financial statements in accordance with *SLFRS for SMEs*? A: list of benefits 5 rating with not beneficial, less beneficial to very beneficial	Q30	Dang-Duc, Marriott, and Marriott (2008) and International Accounting Standards Board (2009)
	Q: What do you think about the relationship between the costs and the benefits an SME may receive from the preparation of financial statements in accordance with *SLFRS for SMEs*?	Q31	Dang-Duc, Marriott, and Marriott (2008)

	A: 4 choices with different perceptions		
	Q: Do you believe that the additional exemptions need to be given in SLFRS for SMEs to make it more cost effective for SMEs in Sri Lanka?	Q32	Chand, Patel, and White (2015)
RQ3: How do users and their information needs differ with regard to size and ownership structure of Sri Lankan SMEs? **(data for cross analysis)**	Q: How many owners/shareholders does your entity/company have? (open question)	Q2	
	Q: How many non-manager owners/non-director shareholders (owners/shareholders who are NOT involved in the management of the entity/company) does the entity/company have?	Q3	
	Q:Number of employees (current year) A: 4 choices given	Q6	
	Q: What was the entity's/company's turnover for the last financial year (2014)? A: 5 choices given	Q7	
Data for cross analysis	Questions regarding characteristics of entity/company: business type; industry; age of business.	Q1, Q4,Q5	
	Q: How would you describe your position in the entity/company?	Q8	
	Q: Which types of financial information do you prepare?	Q9	
	Q: How often are the above financial information prepared?	Q10	
	Q: How does your entity/company keep records of business transactions? A: Different types of accounting systems e.g. manual, computerised system, combination	Q11	
	Q: Who normally prepares your entity's/company's financial information? A: 5 choices given	Q12	
	Q: Which of the following services are supplied by external professional accountants to your entity/company? A: different types of services	Q13	
	Q: Did your entity adopt the accounting standard *SLFRS for SMEs?* A: Yes/No	Q27	

	Q: is it necessary to create criteria to classify the SMEs that should apply the accounting standards? A: Yes/No	Q22	
	Q: If Yes; What would you suggest as the criterion/criteria? A: 3 specific criterion given. Respondent can select all that apply or suggest any other	Q23	
	Q: What accounting standard/principles do you use when preparing financial statements? (opened question)	Q34	
	Q: Are you aware of this new accounting standards (*Sri Lanka Accounting Standards for Smaller entities*) for SMEs? A: Yes/No	Q35	
	Q: Will your entity be preparing financial statements in accordance with new financial reporting standard for smaller entities? A: Yes/No/ Undecided/ Will take professional advice	Q36	
Note: Question 33 is opened question Question 37 is opened question asking for comments regarding accounting standards for SMEs			

Appendix J: English version of the questionnaire

Waikato Management School

Te Raupapa

THE UNIVERSITY OF WAIKATO

Te Whare Wānanga o Waikato

Questionnaire

Research Title: Towards the development of a financial reporting framework for Sri Lankan SMEs.

Your participation in this research is greatly appreciated. Your responses are anonymous and no attempt is made to identify you.

Part I: General information about the organisation (please tick where relevant)

This section asks for some general information about you and your organisation. Any information given will be only used for the purposes of this research. Anonymity will be preserved at all times. The information about you and your organisation will not be published under any circumstances.

1. **How would you describe your business?**

○ Sole proprietor
○ Registered partnership
○ Non registered partnership
○ Limited company
○ Other (please specify) ………………………..

2. **How many owners/shareholders does your organisation have?**

……………………….

3. **How many of above owners/shareholders are managers/directors of the organisation?**

………………………

4. **What is the main activity of your organisation?**

○ Manufacturing
○ Agriculture
○ Service
○ Retail
○ Wholesale/distribution
○ Other (please state) ……………………………………

5. How many years has the organisation been trading?

- ○ Less than 1 year
- ○ 1-3 years
- ○ 4-6 years
- ○ 7-10 years
- ○ More than 10 years

6. Number of employees (current year)

- ○ 5-15
- ○ 16-39
- ○ 40-99

7. What was the organisation's turnover for the last financial year (2014)?

- ○ Less than Rs.1,000,000
- ○ Rs.1,000,000 to Rs.10,000,000
- ○ Rs. 10,000,001 to Rs. 25,000,000
- ○ Rs. 25,000,001 to Rs. 50,000,000
- ○ Rs. 50,000,001 to Rs. 100,000,000
- ○ More than Rs. 100,000,000

8. How would you describe your position in the organisation?

○ Owner	GOTO Q8A
○ Shareholder	GOTO Q8A
○ Accountant	GOTO Q9
○ Other (please state) ……………………….	

8A. What is your involvement with the company?

- ○ Director
- ○ Manager
- ○ No position but involved in day to day operations

Part II: Preparation of financial information (please tick where relevant)

Good financial management requires business to keep records of their transactions and use this financial information for making business decisions.

9. Which types of financial information do you prepare? (tick all that apply)

- ○ Balance sheet
- ○ Profit and loss account/income statement
- ○ Cash flow statement
- ○ Changes in equity statement
- ○ Notes to the financial statements
- ○ Other (please specify)

…………………………………………………

10. How often are the above financial information prepared?

	Monthly	Quarterly	Annually
Balance sheet			
Profit and loss account/ income statement			
Cash flow statement			
Changes in equity statement			
Notes to the financial statements			
Other reports (please mark and specify below)			
Name of report ……................................			

11. How does your organisation keep records of business transactions?

- ○ Manual record keeping
- ○ Computerised accounting system
- ○ Combination of manual and computerised system
- ○ Other (please specify)

....

12. Who normally prepares your organisation's financial information?

- ○ A qualified accountant
- ○ A non-qualified accountant
- ○ An external accountant from a local accounting firm
- ○ An external accountant from an international accounting firm
- ○ Other (please specify)

………………………………

13. Which of the following services are supplied by external professional accountants to your organisation? (tick all that apply)

- ○ Bookkeeping
- ○ Preparation of financial statements
- ○ Taxation service
- ○ Audit service
- ○ Other (please specify)

Part III: Users and uses of financial information (please tick where relevant)

Financial statement information is potentially read by a wide range of people (users) to help them make decisions.

14. Who do you view as the main users of your organisation's financial information? (tick all that apply)

- ○ Owners/shareholders who are managers/directors
- ○ Owners/shareholders who are NOT managers/directors
- ○ Other managers/directors of the organisation
- ○ Employees
- ○ Bank/financial institutions
- ○ Department of Inland Revenue
- ○ Government institutions
- ○ Major suppliers/ creditors
- ○ Major customers
- ○ Anyone else? (please state)

……………………………….

15. Who normally receives a copy of the financial information? (tick all that that apply)

- ○ Owners/shareholders who are managers/directors
- ○ Owners/shareholders who are NOT managers/directors
- ○ Other managers/directors of the organisation
- ○ Employees
- ○ Bank/financial institutions
- ○ Department of Inland Revenue
- ○ Government institutions
- ○ Major suppliers/creditors
- ○ Major customers
- ○ Anyone else? (please state)

………………………………………..

16. **Have you ever used the financial information of your organisation for the following purposes?**

	Never	Seldom	Sometimes	Usually	Always
Applying for capital from banks					
Obtaining credit from suppliers or trade creditors					
Supporting bidding on contracts or obtaining a licence					
Showing compliance with loan covenants in borrowing agreement					

17. **For what purposes do you use your organisation's financial information? (tick all that apply)**

- ○ Deciding managers'/directors' pay/bonuses/dividends
- ○ Marketing and pricing decisions
- ○ Capital investment decisions
- ○ Estimating income tax liabilities
- ○ Planning (short/long-term)
- ○ Deciding employees' pay and bonuses
- ○ Comparing performance with targets
- ○ Comparing performances with previous periods
- ○ Other (please specify)

……………………………………………..

18. **How useful are the following financial information of your organisation to you, personally, as sources for business decisions?**

	Not useful	Less useful	Somewhat useful	Useful	Very useful
Balance sheet					
Profit and loss statement					
Cash flow statement					
Changes in equity statement					
Notes to the financial statements					
Other reports (please rate and specify in box)					
Name of report ……................................					

19. **In addition to the statements in Q18, what additional financial information do you find useful for business decisions?**

	Not useful	Less useful	Somewhat useful	Useful	Very useful
Management accounts (monthly or quarterly)					
Bank reconciliation statement					
Budgets					
Variance analysis					
Aging reports of debtor balance					
Financial ratio analysis					
Other reports (please specify below)					
Name of reports (indicate the usefulness) …..					

20. **What information would you find useful for decision making that is not currently shown in the organisation's financial information?**

……………………………………………………………………………………………….

21. **What information do you consider should not be disclosed in the organisation's financial information?**

……………………………………………………………………………………………….

Part IV: Accounting standards for SMEs (please tick where relevant)

Entities that do not have public accountability (such as SMEs) and publish general purpose financial statements for external users are permitted to apply the Sri Lanka Financial Reporting Standards for Small and Medium sized Entities (SLFRS for SMEs) issued by the Institute of Chartered Accountants of Sri Lanka.

22. **Is it necessary to create criteria to classify the SMEs that should apply the accounting standards?**

    - Yes
    - No
    - Do not know

23. **If yes; what would you suggest as the criteria/criterion? (please tick all that apply)**

    - Criterion based on number of employees
    - Criterion based on turnover
    - Criterion based on total assets
    - Any other (please specify)

    ………………………….

The development of the Sri Lanka Financial Reporting Standards for Small and Medium sized Entities SLFRS for SMEs is justified by the argument that SMEs increasingly engage in international business activities and therefore foreign stakeholders as well as the entity could benefit from internationally comparable financial accounting data.

24. **How relevant are the following foreign activities for your organisation?**

	No relevance	Low relevance	Moderate relevance	High relevance	Very high relevance
Foreign exports					
Foreign imports					
Foreign ownership					
Borrowing abroad					

25. **Is there any need for your organisation to provide internationally comparable accounting information?**

- ○ No need
- ○ Little need
- ○ Partial need
- ○ High need
- ○ Very high need

26. **How often do the following transactions/investments occur in your organisation?**

	Never	Seldom	Sometimes	Often	Very often
Investment in non-listed companies					
Investment in listed companies					
Joint venture					
Investment property					
Construction contracts					
Research and development projects within the company					
Government grants					
Purchase/sale of goods and services in foreign currencies					
Foreign exchange rate loans and borrowings					
Foreign exchange risk resulting from a customer order or a supplier					

27. **Did your organisation adopt the accounting standard *SLFRS for SMEs?***

- ○ Yes
- ○ No

If "YES", please continue from Q28 to Q33.

If "NO" please go to the Q34and continue up to Q38.

Entities need to incur costs to provide financial statement information. Costs include information collection and processing costs, and potential indirect costs such as competitive disadvantages. The benefit expected from the provision of such information include uses and usefulness of such information in making decisions of internal and/or external users.

28. What is your view on the role of accounting standards for SMEs?

- ○ Unnecessary intrusion into your organisation's activities
- ○ Desirable and impose no significant burden on your organisation
- ○ Desirable but do impose significant burden on your organisation
- ○ No idea

29. How significant is each of the following items in terms of costs to be incurred for preparing financial statements in accordance with *SLFRS for SMEs*

	Not significant	Less significant	Somewhat significant	Significant	Very significant
Costs of training accounting and IT staff					
Costs of hiring qualified accounting staff					
Costs of obtaining external technical advice (payments to accounting firms)					
Costs of changing accounting software and systems					
Costs of information acquisition (e.g. fair value)					
Costs of taking tax advice					
Any other costs (please specify) ……................					

30. What benefits do you think an SME will obtain from preparing financial statements in accordance with *SLFRS for SMEs*

	Not beneficial	Less beneficial	Somewhat beneficial	Beneficial	Very beneficial
To compare financial statements					
To fulfil tax declaration					
To easy access to finance					
To serve administrative/statistical purposes of the government					
To support loan applications					
To tender for business projects/contracts					
To meet your internal management needs					
Any other benefits (please specify) …….........................					

31. **What do you think about the relationship between the costs and the benefits an SME may receive from the preparation of financial statements in accordance with *SLFRS for SMEs?* (please tick only one)**

The benefits exceeds the costs	
The benefits fit with the costs	
The costs exceeds the benefits	
No idea	
Other (please specify) …………………………………………………	

32. **Do you believe that the additional exemptions need to be given in *SLFRS for SMEs* to make it more cost effective for SMEs in Sri Lanka?**
    - ○ Yes (please give reasons)
    - ○ No (please give reasons)
    - ○ No idea

33. **If you have any general comments regarding *SLFRS for SMEs*, please state below**

GOTO Q40.

34. **What accounting standard/principles do you use when preparing financial statements?**

Currently, another set of financial reporting standards have been drafted by the Institute of Chartered Accountants of Sri Lanka for SMEs called Sri Lanka Accounting Standards for Smaller entities.

35. Are you aware of this new accounting standards (*Sri Lanka Accounting Standards for Smaller entities*) for SMEs?

- ○ Yes
- ○ No

36. Will your organisation be preparing financial statements in accordance with new financial reporting standard for smaller entities?

- ○ Yes (please give reasons)

…………………………………………………………………………….

- ○ No (please give reasons)

……………………………………………………………………………

- ○ Undecided
- ○ Will take professional advice

37. If you have any general comments regarding accounting standards for SMEs, please state below

38. Would you like a summary of the findings?

- ○ Yes
- ○ No

39. If you have answered 'yes' to Q38, please provide your details below:

Name:……………………………………………………………………………………
Address: ………………………………………………………………………………………
…………………………………………………………………………………………
Tel: …………………………………**Email:**…………………………………………...

Thank you very much for taking part in this survey
Please return the questionnaire by using the enclosed stamped envelope

Appendix K: Sinhala version of the questionnaire

Waikato Management School

Te Raupapa

THE UNIVERSITY OF WAIKATO

Te Whare Wānanga o Waikato

පර්යේෂණ මාතෘකාව:
ශ්‍රී ලංකාවේ සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා මූල්‍ය වාර්තාකරණ රාමුව සංවර්ධනය කරා.

මෙම පර්යේෂණයට ඔබගේ සහභාගිත්වය අගේ කොට සලකන්නෙමු. ඔබගේ ප්‍රතිචාරය නිර්නාමිකය. ඔබ හඳුනාගැනීම සඳහා කිසිදු උත්සහයක් ගනු නොලැබේ.

I කොටස : ආයතනය පිළිබඳ සාමාන්‍ය තොරතුරු (කරුණාකර අදාළ ස්ථානයෙහි ලකුණු කරන්න)

මෙම කොටස ඔබ සහ ඔබගේ ආයතනය පිළිබඳ යම් තොරතුරු විමසයි. ලබාදෙන ලද කිසියම් තොරතුරක් මෙම පර්යේෂණයේ අරමුණු සඳහා භාවිතා කරනු ඇත. නිර්නාමිකත්වය සෑම විටම ආරක්ෂා කරනු ලැබේ. ඔබ සහ ඔබගේ ආයතනය ගැන තොරතුරු කිසිදු හේතුවක් යටතේ ප්‍රකාශය ට පත් කරනු නොලැබේ.

---

1. ඔබ ඔබගේ ව්‍යාපාරය විස්තර කරන්නේ කෙසේද?
   - ○ තනි පුද්ගල ව්‍යාපාරය............................
   - ○ ලියා පදිංචි හවුල් ව්‍යාපාරය.....................
   - ○ ලියාපදිංචි නොවන හවුල් ව්‍යාපාරය............
   - ○ සීමා සහිත සමාගම.............................
   - ○ වෙනත් **(කරුණාකර සඳහන් කරන්න)**

____

2. ඔබගේ ආයතනයේ කොපමණ හිමිකරුවන්/කොටස් හිමියන් සිටිනවාද?

3. ඉහත හිමිකරුවන්ගෙන්/කොටස් හිමියන්ගෙන් කොපමණ පිරිසක් ආයතනයේ කළමනාකරුවන්/ අධ්‍යක්ෂවරුන් ද?

4. ඔබගේ ආයතනයේ ප්‍රධාන ක්‍රියාකාරකම කුමක් ද ?
   - ○ නිෂ්පාදනය.....................
   - ○ කෘෂිකාර්මික...................
   - ○ සේවා..........................
   - ○ සිල්ලර ....
   - ○ තොග/බෙදා හැරීම............

- ◯ වෙනත් **(කරුණාකර සඳහන් කරන්න)** ________________________

5. කොපමණ කාලයක සිට ආයතනය ක්‍රියාත්මක වෙනවාද?

- ◯ වසර 1 වඩා අඩු
- ◯ වසර 1-3
- ◯ වසර 4-6
- ◯ වසර 7-10
- ◯ වසර 10 වඩා වැඩි

6. සේවකයින් ගණන (වත්මන් වසර සඳහා)

- ◯ 5-15
- ◯ 16 - 39
- ◯ 40 - 99

7. පසුගිය මූල්‍ය වර්ෂය සඳහා ආයතනයේ පිරිවැටුම කුමක් ද **(2014)**?

- ◯ රුපියල්.1,000,000 වඩා අඩු (මිලියනයට වඩා අඩු)
- ◯ රුපියල්1,000,000- . රුපියල් 10,000,000 දක්වා (මි. 01-මි.10
- ◯ රුපියල් 10,000,001 -. රුපියල්25,000,000 දක්වා (මි. 10-මි.25
- ◯ රුපියල්25,000,001- රුපියල්50,000,000 දක්වා (මි. 25-මි.50
- ◯ රුපියල්. 50,000,001- රුපියල්100,000,000 දක්වා (මි. 50 -මි.100
- ◯ රුපියල්100,000,000 වඩා වැඩි (මිලියන 100ට වඩා වැඩි)

8. ආයතනය තුළ ඔබගේ තනතුර විස්තර කරන්නේ කෙසේ ද?

- ◯ ආයතනයේ හිමිකරු .... **(Q8Aට යන්න)**
- ◯ ආයතනයේ කොටස් හිමිකරුවෙක් .... **(Q8Aට යන්න)**
- ◯ ගණකාධිකාරී .... **(Q8ට යන්න)**
- ◯ වෙනත් **(කරුණාකර සඳහන් කරන්න)**__________________________

8A. ආයතනය තුල ඔබ ඉටුකරන කාර්යභාරය විස්තර කරන්නේ කෙසේ ද?

- ◯ අධ්‍යක්ෂක...
- ◯ කළමනාකරු...
- ◯ කිසිම තනතුරක් දරන්නේ නැත, නමුත් එදිනෙදා සිදුවන ක්‍රියාකාරකම් ගැන සොයා බලයි

II කොටස : මූල්‍ය තොරතුරු සකස් කිරීම (කරුණාකර අදාළ ස්ථානය ලකුණු කරන්න)

ව්‍යාපාරයක තම ගණුදෙණු පිළිබඳ වාර්තා තබා ගැනීමට යහපත් මූල්‍ය කළමනාකරණයක් අවශ්‍ය වන අතර ව්‍යාපාර තීරණ ගැනීම සඳහා මෙම මූල්‍ය තොරතුරු භාවිතා වේ.

9. ඔබගේ ආයතනය සඳහා කුමන මූල්‍යතොරතුරු වර්ග සකස් කරන්නේ ද?

- ශේෂ පත්‍රය
- ලාභ සහ අලාභ ගිණුම/ ආදායම් ප්‍රකාශනය
- මුදල් ප්‍රවාහ ප්‍රකාශනය
- හිමිකම් වෙනස්වීමේ ප්‍රකාශනය

මූල්‍ය ප්‍රකාශන සටහන්

- වෙනත් **(කරුණාකර සඳහන් කරන්න)**

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10. ඉහත මූල්‍ය තොරතුරු සකස් කරන්නේ කොපමණ කාලයකට වරක් ද?

	මාසිකව	කාර්තුමය	වාර්ෂිකව	සකසන්නේ නැත
ශේෂ පත්‍රය				
ලාභ සහ අලාභ ගිණුම/ ආදායම් ප්‍රකාශනය				
මුදල්ප්‍රවාහ ප්‍රකාශනය				
හිමිකම් වෙනස්වීමේ ප්‍රකාශනය				
මූල්‍යප්‍රකාශන සටහන්				
වෙනත් වාර්තා **(කරුණාකර සලකුණු කොට පහත සඳහන් කරන්න)**				
වාර්තාවේ නම ______________________________				

11. ඔබගේ ආයතනය ව්‍යාපාර ගණුදෙණු වාර්තා තබා ගන්නේ කෙසේ ද ?

- අත්පොත් වාර්තා තබා ගැනීම
- පරිගණකගත ගිණුම් පද්ධතිය
- අත්පොත සහ පරිගණකගත තොරතුරු පද්ධතියේ එකතුවක්
- වෙනත් **(කරුණාකර සඳහන් කරන්න)**

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12. ඔබ ආයතනයේ මූල්‍ය තොරතුරු සකස් කරන්නේ කවුරුන් ද?

- සුදුසුකම්ලත් ගණකාධිකාරිවරයෙකු
- සුදුසුකම් නොලත් ගණකාධිකාරියෙකු
- දේශීය ගිණුම්කරණ සමාගමක් මගින්
- ජාත්‍යන්තර ගිණුම්කරණ සමාගමක් මගින්
- වෙනත් **(කරුණාකර සඳහන් කරන්න)**

13. පහත සඳහන් සේවාවන්ගෙන් කුමන සේවාවන් ඔබගේ ආයතනය සඳහා බාහිර වෘත්තිය ගණකාධිවරුන් විසින් සපයන්නේ ද? **(අදාළ සියල්ල ලකුණු කරන්න)**

- ○ පොත් තැබීම
- ○ මූල්‍ය ප්‍රකාශන සකස් කිරීම
- ○ බදුකරණ සේවා
- ○ විගණන සේවා
- ○ වෙනත් **(කරුණාකර සඳහන් කරන්න)**

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III කොටස : මූල්‍ය තොරතුරු පරිශීලකයන් හා භාවිතයන් (කරුණාකර අදාළ ස්ථානයෙහි ලකුණු කරන්න)

ජනතාවට තීරණ ගැනීමට උපකාරී වන බැවින් ඔවුන් (පරිශීලකයන්) විශාල පිරිසක් විසින් මූල්‍ය ප්‍රකාශන තොරතුරු කියවනු ලබයි.

14. ඔබගේ ආයතනයේ මූල්‍ය තොරතුරු ප්‍රධාන වශයෙන් භාවිතා කරන්නන් ලෙස ඔබ සලකන්නේ කවුද? **(අදාළ සියල්ල ලකුණු කරන්න)**

- ○ ආයතනයේ හිමිකරුවන් / කළමනාකරුවන් / කොටස් හිමිකරුවන් / අධ්‍යක්ෂකවරුන් ....
- ○ ආයතනයේ කළමනාකරුවන් නොවන හිමිකරුවන්/ අධ්‍යක්ෂවරුන් නොවන කොටස් හිමිකරුවන් ....
- ○ ආයතනයේ වෙනත් කළමනාකරුවන්/ අධ්‍යක්ෂවරු ....
- ○ සේවකයන් ....
- ○ බැංකු/ මූල්‍යආයතන ....
- ○ දේශීය ආදායම් බදු දෙපාර්තමේන්තුව ....
- ○ රජයේ වෙනත් ආයතන ....
- ○ ප්‍රධාන සැපයුම්කරුවන්/ණයහිමියන් ....
- ○ ප්‍රධානපාරිභෝගිකයින් ....
- ○ වෙනත් ඕනෑම කෙනෙක් **(කරුණාකර සඳහන් කරන්න)**

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15. ඔබගේ ව්‍යාපාරයේ මූල්‍ය තොරතුරු පිටපත් ලබා ගන්නේ කවුරුන් ද? **(අදාළ සියල්ල ලකුණු කරන්න)**

- ○ ආයතනයේ හිමිකරුවන් / කළමනාකරුවන් / කොටස් හිමිකරුවන් / අධ්‍යක්ෂකවරුන්
- ○ ආයතනයේ කළමනාකරුවන් නොවන හිමිකරුවන්/ අධ්‍යක්ෂවරුන් නොවන කොටස් හිමිකරුවන් ....
- ○ ආයතනයේ වෙනත් කළමනාකරුවන්/ අධ්‍යක්ෂවරු ....
- ○ සේවකයන් ....
- ○ බැංකු/ මූල්‍යආයතන ....
- ○ දේශීය ආදායම් බදු දෙපාර්තමේන්තුව ....
- ○ රජයේ වෙනත් ආයතන ....
- ○ ප්‍රධාන සැපයුම්කරුවන්/ණය හිමියන් ....
- ○ ප්‍රධාන පාරිභෝගිකයින් ....
- ○ වෙනත් ඕනෑම කෙනෙක් **(කරුණාකර සඳහන් කරන්න)**

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16. ඔබ කවදා හෝ පහත සඳහන් කාර්යයන් සඳහා ඔබගේ ආයතනයේ මූල්‍ය තොරතුරු භාවිතා කර තිබෙනවා ද?

	කවදාවත් නැත	කලාතුරකින්	සමහරවිට	සාමාන්‍ය පරිදි	සැමවිටම
බැංකු වලින් ප්‍රාග්ධනය සඳහා ඉල්ලුම් කිරීම					
සැපයුම්කරුවන් හෝ වෘත්තීය ණය හිමියන් වෙතින් ණය ලබා ගැනීම					
කොන්ත්‍රාත්කරුවන්මත ලංසු තැබීමට සහය දැක්වීම හෝ බලපත්‍රයක්ලබා ගැනීම.					
ණය ගිවිසුම තුළ ණය අනුකූලභාවය පෙන්වමින්					

17. ඔබ ආයතනයේ මූල්‍ය තොරතුරු කුමන අරමුණු සඳහා භාවිත කරන්නේ ද? **(අදාළ සියල්ල ලකුණු කරන්න)**

- ○ කළමනාකරුවන්ගේ අධ්‍යක්ෂවරුන්ගේ වැටුප්/ප්‍රසාද දීමනා/ලාභාංශ තීරණය කිරීම ....
- ○ අලෙවි හා මිළ නියම කිරීමේ තීරණය ගැනීමේදී ....
- ○ ප්‍රාග්ධන ආයෝජන තීරණය කිරීම ....
- ○ ආදායම් බදු වගකීම් ඇස්තමේන්තු කිරීම ....
- ○ සැළසුම් කිරීම (කෙටි/දිගු කාලීන) ....
- ○ සේවක වැටුප් හා ප්‍රසාද දීමනා තීරණය කිරීම ....
- ○ ඉලක්ක සාධන ක්‍රියාකාරීත්වය සමඟ සසඳා බැලීමට ....
- ○ වර්තමාන ක්‍රියාකාරීත්වය පෙර කාල සීමාව සමඟ සසඳා බැලීමට ....
- ○ වෙනත් **(කරුණාකර සඳහන් කරන්න)**____________________________________

18. ව්‍යාපාර තීරණ සඳහා මූලාශ්‍ර ලෙස, පෞද්ගලික ව ඔබට ඔබගේ ආයතනයේ පහත සඳහන් මූල්‍ය තොරතුරු කෙසේ ප්‍රයෝජනවත් වේද?

	ප්‍රයෝජනවත් නොවේ	ප්‍රයෝජනවත් බව අඩුය	තරමක් ප්‍රයෝජනවත්	ප්‍රයෝජනවත්	ඉතා ප්‍රයෝජනවත්
ශේෂ පත්‍රය					
ලාභ සහ අලාභ ප්‍රකාශනය					
මුදල් ප්‍රවාහ ප්‍රකාශනය					
හිමිකම් වෙනස්වීමේ ප්‍රකාශනය					
මූල්‍ය ප්‍රකාශන සටහන්					
වෙනත් වාර්තා **(කරුණාකර ශ්‍රේණිගත හා කොටුව තුළ සඳහන් කරන්න)**					
වාර්තාවේ නම____________________					

19. ඔබට ව්‍යාපාර තීරණ ගැනීම සඳහා 18 වන ප්‍රශ්නයේ සඳහන් මූල්‍ය තොරතුරු වලට අමතරව පහත සඳහන් අතිරේක මූල්‍ය තොරතුරු කෙසේ ප්‍රයෝජනවත් වේද?

	ප්‍රයෝජනවත් නොවේ	ප්‍රයෝජනවත් බව අඩුය	තරමක් ප්‍රයෝජනවත්	ප්‍රයෝජනවත් වේ	ඉතා ප්‍රයෝජනවත්
කළමනාකරණ ගිණුම් **(**මාසික හෝ කාර්තුමය **)**					
බැංකු සැසඳුම් ප්‍රකාශය					
අය-වැය					
විචලන විශ්ලේෂණ					
ණය ශේෂ පැරණි වාර්තා					
මූල්‍ය අනුපාත විශ්ලේෂණය					
වෙනත් වාර්තා **(කරුණාකර පහත සඳහන් කරන්න)**					
වාර්තා නම (ප්‍රයෝජනවත් බව අනුව සඳහන් කරන්න) ____________________ ________________________________					

20. ඔබට තීරණ ගැනීම සඳහා දැනට ආයතනයේ මූල්‍ය තොරතුරුවල පෙන්වා නැති එහෙත් ප්‍රයෝජනවත් යැයි සිතන්නේ කුමන මූල්‍ය තොරතුරු ද?

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21. ආයතනයේ මූල්‍ය තොරතුරු වල හෙළි නොකළ යුතුය යන්න ඔබ සලකා බලනු ලබන්නේ කුමන මූල්‍ය තොරතුරු ද?

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IVකොටස: **සුළු සහ මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ගිණුම්කරණ ප්‍රමිතීන් (අදාළ තැනෙහි ලකුණු කරන්න)**

බාහිර භාවිතා කරන්නන් සඳහා පොදු අරමුණ මූල්‍ය ප්‍රකාශන සකස් කරනු ලබන සහ මහජන වගකීම නැති ව්‍යාපාර වලට (සුළු හා මධ්‍යම පරිමාණ ව්‍යවසායකයින් වැනි) ශ්‍රී ලංකා වරලත් ගණකාධිකරණ ආයතනය විසින් නිකුත් කරන ලද සුළු හා සහ මධ්‍ය පරිමාණ ව්‍යාපාර උදෙසා ශ්‍රී ලංකා මූල්‍ය ගිණුම්කරණ ප්‍රමිතීන් (SLFRS for SMEs) අයදුම් කිරීමට අවසර ඇත.

22. ගිණුම්කරණ ප්‍රමිතීන් සකස් කිරීමේදී සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර වර්ගීකරණය කිරිමට නිර්ණායක තිබීම අවශ්‍ය ද?

○ ඔව්	**(22ට යන්න)**
○ නැත	**(23ට යන්න)**
○ නොදනී/කිව නොහැක	**(23ට යන්න)**

23. ඔව් නම්, ඔබ නිර්ණායක/මිණුම් දණ්ඩ ලෙස යෝජනා කරන්නේ කුමක් ද? **(අදාල සියල්ල ලකුණු කරන්න)**

- ○ සේවක සංඛ්‍යාව මත පදනම් වූ නිර්ණායක ....
- ○ පිරිවැටුම මත පදනම් වූ නිර්ණායක ....
- ○ මුළු වත්කම මත පදනම් වූ නිර්ණායක ....
- ○ වෙනත් ඕනෑම **(කරුණාකර සඳහන් කරන්න)**

සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර *වැඩි වැඩියෙන්* අන්තර්ජාතික ව්‍යාපාරික කටයුතු වල නිරත වන අතර එම නිසා විදේශ පාර්ශවයන්ට මෙන් ම ආයතනයන්ට ද අන්තර්ජාතික සංසන්දනාත්මක මූල්‍ය ගිණුම්කරණ දත්ත ප්‍රයෝජනවත් විය හැකි යන තර්කය මත සුළු හා මධ්‍යපරිමාණ ව්‍යාපාර සඳහා අන්තර්ජාතික මූල්‍ය වාර්තාකරණ ප්‍රමිතීන් හඳුන්වා දී ඇත.

24. ඔබගේ ආයතනයට පහත සඳහන් විදේශ ක්‍රියාකාරකම් කෙසේ අදාළ වේ ද?

	අදාළ නැත	අදාළත්වය අඩුය	මධ්‍යස්ථ	ඉහල අදාළත්වය	ඉතා ඉහල අදාළත්වය
විදේශ අපනයන					
විදේශ ආනයන					
විදේශ අයිතිය					
විදේශ ණය					

25. අන්තර්ජාතික සංසන්දනාත්මක ගිණුම්කරණ තොරතුරු සැපයිම සඳහා ඔබගේ ආයතනයට කිසිදු අවශ්‍යතාවක් තිබේ ද?

- ○ අවශ්‍ය නැත
- ○ සුළු අවශ්‍යතාවයක් ඇත
- ○ අර්ධ අවශ්‍යතාවක් ඇත
- ○ ඉහළ අවශ්‍යතාව ක් ඇත
- ○ ඉතා ඉහළ අවශ්‍යතාව ක් ඇත

26. ඔබගේ ආයතනය තුළ පහත සඳහන් ගණුදෙණු/ආයෝජන සිදුකරන්නේ කොපමණ කාලයකට වරක් ද?

	කිසිදාක් නැත	කලාතුරකින්	සමහර විට	නිතරම	බොහෝ විට
ලැයිස්තුගත නොවන සමාගම් වල ආයෝජන (Investment in non-listed companies)					
ලැයිස්තුගත සමාගම් වල ආයෝජන (Investment in listed companies)					
ඒකාබද්ධ ව්‍යාපාර (Joint venture)					
ආයෝජන දේපල (Investment property)					
ඉදිකිරිම් කොන්ත්‍රාත් (Construction contracts)					
සමාගම තුළ පර්යේෂණ හා සංවර්ධන ව්‍යපෘති (Research and development projects within the company)					
රාජ්‍ය ප්‍රතිපාදන (Government grants)					
විදේශ මුදල් භාණ්ඩ හා සේවා මිළ දී ගැනිම /විකිණීම (Purchase/sale of goods and services in foreign currencies)					
විදේශ විනිමය අනුපාතයට ණය සහ ණය ගැනීම් (Foreign exchange rate loans and borrowings)					
පාරිභෝගික ඇණවුම් හෝ සැපයුම් කරුගේ ප්‍රතිඵලයක් ලෙස විදේශ විනිමය අවදානම (Foreign exchange risk resulting from a customer order or a supplier)					

27. ඔබගේ ආයතනය සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා මූල්‍ය වාර්තාකරණ ප්‍රමිතීන් (***SLFRS for SMEs)*** අනුගමනය කරනවාද?

○ ඔව්

○ නැත

[“ඔව්” නම් ප්‍රශ්න අංක 27 සිට ප්‍රශ්න අංක 33 දක්වා දිගටම]

[“නැත” නම් ප්‍රශ්න අංක 36 සිට ප්‍රශ්න අංක 39 දක්වා දිගටම]

ව්‍යාපාරයන් හී මූල්‍ය ප්‍රකාශන තොරතුරු සැපයීම සඳහා පිරිවැය දැරිමට සිදු වේ. තොරතුරු එකතු කිරීම සහ සකසන වියදම මිට ඇතුලත් වන අතර තරඟකාරී අවාසි වැනි විභව වක්‍ර වියදම් මිට ඇතුළත්වේ. මෙවැනි මූල්‍ය තොරතුරු සැපයීම මගින් ව්‍යාපාරයේ අභ්‍යන්තර/බාහිර පාර්ශවයන්ට තීරණ ගැනීමට හැකිවීම අපේක්ෂිත ප්‍රතිලාභ වේ.

28. සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ගිණුම්කරණ ප්‍රමිතීන් වල භූමිකාව පිළිබඳ ඔබේ අදහස කුමක් ද?

○ ඔබගේ ආයතනයේ ක්‍රියාකාරකම් සඳහා අනවශ්‍ය ඇහිලි ගැසීමකි

○ සුදුසුය සහ අනුගමනය කිරිම සඳහා ඔබගේ ආයතනය මත අනවශ්‍ය බරක් නැත

○ සුදුසුය නමුත් අනුගමනය කිරිම සඳහා ඔබගේ ආයතනය මත බරක් ඇත

○ අදහසක් නැත

29. සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා මූල්‍ය වාර්තාකරණ ප්‍රමිතීන්ට (***SLFRSfor SMEs)*** *අනුකූලව* මූල්‍ය ප්‍රකාශන සකස් කිරිමේ දී දැරිය යුතු වියදම, පහත සඳහන් එක් එක් අයිතමයන් සඳහා කොපමණද යන්න සඳහන් කරන්න.?

	ඉතා අඩුය	අඩුය	මධ්‍යස්ථය	වැඩිය	ඉතා වැඩිය
ගිණුම්කරණ සහ තොරතුරු තාක්ෂණ කාර්ය මණ්ඩල පුහුණු කිරීමේ පිරිවැය					
සුදුසුකම් ලත් ගිණුම් කාර්ය මණ්ඩලය බඳවා ගැනීමේ පිරිවැය					
තාක්ෂණ උපදෙස් ලබා ගැනීමේ පිරිවැය (ගිණුම් ආයතන වලට ගෙවීම්)					
ගිණුම්කරණ මෘදුකාංග හා පද්ධති වෙනස්වීමේ පිරිවැය					
තොරතුරු අත්පත් කර ගැනීමේ පිරිවැය (උදාහරණ සාධාරණ වටිනාකම අගය ඇගයීම)					
බදු උපදෙස් ලබා ගැනීමේ පිරිවැය					
වෙනත් පිරිවැය **(කරුණාකර සඳහන් කරන්න)**					

30. සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා මූල්‍ය වාර්තාකරණ ප්‍රමිතීන් ට (***SLFRS for SMEs)*** *අනුකූලව* මූල්‍ය ප්‍රකාශන සකස්කිරීමේ දී සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාරයක් කුමන ප්‍රයෝජන ලබා ගනු ඇතැයි සිතන්නේ ද?

	ප්‍රයෝජනවත් නැත	ප්‍රයෝජනවත් බව අඩුය	තරමක් ප්‍රයෝජනය	ප්‍රයෝජනවත් ය	ඉතා ප්‍රයෝජනය
මූල්‍යප්‍රකාශන සංසන්දනය කිරීම සඳහා					
බදු ප්‍රකාශන ඉටුකිරීම					
මුදල් ලබා ගැනීමේ ප්‍රවේශය පහසු කිරීම සඳහා					
රජයේ පරිපාලන/ සංඛ්‍යාමය අවශ්‍යතාවය සහය වීමට					
ණය ඉල්ලුම්පත් වලට සහයවීමට					
ව්‍යාපාරික ව්‍යපෘති/ කොන්ත්‍රාත් සඳහා ඉදිරිපත් කිරීමට					
ඔබේ අභ්‍යන්තරික කළමනාකරණ අවශ්‍යතා සපුරාලීමට					
අනෙකුත් කුමන හෝ ප්‍රතිලාභ **(කරුණාකර සඳහන් කරන්න)**					

31. සුළු හා මධ්‍ය පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා මූල්‍ය වාර්තාකරණ ප්‍රමිතීන්ට (***SLFRS for SMEs)*** *අනුකූලව* මූල්‍ය ප්‍රකාශන සකස්කිරීමේ දී සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාරයක් දැරිය යුතු පිරිවැය හා ලබා ගත හැකි ප්‍රතිලාභ අතර සම්බන්ධතාවය ගැන කුමක් සිතන්නේ ද? **(කරුණාකර එකක් පමණක් ලකුණු කරන්න)**

පිරිවැයට වඩා වැඩි ප්‍රතිලාභ	
පිරිවැයේ ප්‍රමාණයට ප්‍රතිලාභ ලැබේ	
ප්‍රතිලාභ වලට වඩා වැඩි පිරිවැයක් දැරීමට සිදුවේ	
අදහසක් නැත	
වෙනත් **(කරුණාකර සඳහන් කරන්න)**	

32. ශ්‍රී ලංකාවේ සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර වලට වඩාත් ඵලදායි පිරිවැයක් ලබා ගැනීම සඳහා සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා මූල්‍ය වාර්තාකරණ ප්‍රමිතීන් (***SLFRS for SMEs)*** සඳහා අතිරේක නිදහස් කිරීම් ලබා දිම කළ යුතු බව ඔබ විශ්වාස කරනවාද?

- ○ ඔව් **(කරුණාකර හේතුව ඉදිරිපත් කරන්න)**

- ○ නැත **(කරුණාකර හේතුව ඉදිරිපත් කරන්න)**

- ○ අදහසක් නැත

33. සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා මූල්‍ය වාර්තාකරණ ප්‍රමිතීන් (***SLFRS for SMEs)*** *සම්බන්ධයෙන් කවර හෝ පොදු අදහසක් තියෙනවා නම් පහත සඳහන් කරන්න.*

[Q33ට පසු Q39 ට යන්න]

34. මූල්‍ය ප්‍රකාශන පිළියෙළ කරන විට ඔබ කුමන ප්‍රමිතීන් /මූලධර්ම භාවිතා කරන්නේ ද?

දැනට සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා ශ්‍රී ලංකා වරලත් ගණකාධිකරණ ආයතනය විසින් 'සුළු ව්‍යාපාර සඳහා ශ්‍රී ලංකා ගිණුම්කරණ ප්‍රමිතීන් '(Sri Lanka Accounting Standards for Smaller Entities) නමින්වෙනත් මූල්‍ය *වාර්තාකරණ* ප්‍රමිතීන් කට්ටලයක් කෙටුම්පත් කර ඇත.

35. ඔබ ඉහත සඳහන් කළ නව ගිණුම්කරණ ප්‍රමිතීන් (Sri Lanka Accounting Standards for Smaller Entities) ගැන දැනුවත් ද?

- ○ ඔව්
- ○ නැත

36. සුළු ව්‍යාපාර සඳහා නව මූල්‍ය *වාර්තාකරණ* ප්‍රමිතීන්ට අනුකූලව මූල්‍ය ප්‍රකාශන සකස් කිරීමට ඔබගේ ය සූදානම් වේද?

- ○ ඔව් **(කරුණාකර හේතු ඉදිරිපත් කරන්න)**

  ____

- ○ නැත **(කරුණාකර හේතු ඉදිරිපත් කරන්න)**

  ____

- ○ අවිනිශ්චිතයි
- ○ වෘත්තිමය උපදෙස් ගනු ලබයි

37. ඔබට සුළු හා මධ්‍යම පරිමාණ ව්‍යාපාර සඳහා වන ගිණුම්කරණ ප්‍රමිතීන් සම්බන්ධයෙන් කවර හෝ පොදු අදහසක් තියෙනවානම් පහත සඳහන් කරන්න .

ඔබ මෙම පර්යේෂණයේ සොයා ගැනීම් පිළිබඳ සාරාංශයක් ලබා ගැනීමට කැමති ද?

- ○ ඔව්
- ○ නැත

38. ප්‍රශ්න අංක **38** සඳහා පිළිතුර **"ඔව්"** නම්, පහත ඔබගේ විස්තර ලබා දෙන්න.

නම : ____

ලිපිනය : ____

____

____

දුර : ____________________

ඊ- මේල් **:** ____________________

මෙම සමීක්ෂණයට සහභාගී වූ ඔබට ස්තූතියි

Appendix L: Cover letter for survey questionnaire – English version

Waikato Management School
Te Raupapa

THE UNIVERSITY OF
WAIKATO
Te Whare Wānanga o Waikato

Nisansala Wijekoon

Department of Accounting
Waikato Management School
University of Waikato
Private Bag 3105, Hamilton, New Zealand
Email Address: hnww1@students.waikato.ac.nz

Mobile: 0221 955394 Office: +64 7838 4466 (Ext: 6419)

Dear Madam/Sir,

Request to participate in a survey questionnaire on "Towards the development of a financial reporting framework for Sri Lankan SMEs"

I am lecturer at the Department of Accountancy, University of Kelaniya and presently pursuing doctoral studies at the department of Accounting, Waikato Management School, University of Waikato, New Zealand. I am inviting your participation in the research study designed to identify small and medium enterprise users and their information needs as well as gather perceptions from preparers and users of SME financial statements on the SME financial reporting in general and the accounting standard *International Financial Reporting Standards for Small and Medium- sized Entities (IFRS for SMEs)* in particular.

Your participation is highly valued and will make a valuable contribution to study on an important issue for small businesses in Sri Lanka. I assure you that the information collected through this questionnaire will be strictly confidential and used solely for my PhD studies. Real names of the company and /or participants will not be used in any subsequent reports or publications and all data will be analysed in a collective manner. Please see the attached participant information sheet for more details.

Please return the completed questionnaire using the attached postage paid envelop.

Thanking you.
Yours Sincerely
Nisansala Wijekoon

Cover letter for survey questionnaire – Sinhala version

Waikato Management School
Te Raupapa

THE UNIVERSITY OF
WAIKATO
Te Whare Wānanga o Waikato

08 දෙසැම්බර් 2015

මහත්මයාණෙනි / මහත්මියනි

"ශ්‍රී ලංකික සුළු හා මධ්‍ය පරිමාණ කර්මාන්තයන් සඳහා මූල්‍ය වාර්තා රාමුව සංවර්ධනය" වෙනුවෙන් සිදුකරනු ලබන සමීක්ෂණ ප්‍රශ්නාවලිය සඳහා සහභාගී වීම සඳහා කරනු ලබන ඉල්ලීමයි.

මම කැලණිය විශ්වවිද්‍යාලයේ ගණකාධිකරණ දෙපාර්තමේන්තුවේ කථිකාචාර්යවරියක වන අතර නවසීලන්තයේ වයිකාටෝ විශ්වවිද්‍යාලයේ වයිකාටෝ කළමණාකාරණ පාසැලේ ගිණුම්කරණ දෙපාර්තමේන්තුවේ වර්තමානයේදී ආචාර්ය අධ්‍යාපන කටයුතු හදාරමි. මාගේ පර්යේෂණ අරමුණ වන්නේ ශ්‍රී ලාංකික සුළු හා මධ්‍ය පරිමාණ කර්මාන්ත සඳහා මූල්‍ය වාර්තා රාමුව සංවර්ධනය කිරීම වේ. මෙම අධ්‍යයනයේ අරමුණ වන්නේ සුළු හා මධ්‍ය පරිමාණ ව්‍යවසායක මූල්‍ය තොරතුරු පරිශීලකයන් සහ ඔවුන්ගේ මූල්‍ය තොරතුරු අවශ්‍යතාවයන් හඳුනාගැනීමයි. සුළු හා මධ්‍ය පරිමාණ ව්‍යවසාය මූල්‍ය වාර්තා පිළිබඳ පොදුවේ සුළු හා මධ්‍ය පරිමාණ ව්‍යවසායකයන්ගේ සහ ගණකාධිකාරිවරුන්ගේ අදහස් එක්රැස් කිරීමේ මෙහි බලාපොරොත්තුව වේ. ශ්‍රී ලංකාවේ කුඩා ව්‍යාපාර තුළ පවතින ගැටළු සම්බන්ධයෙන් ඔබ ලබාදෙන අදහස් අපට ඉතාමත් වැදගත් වන අතර මේ සඳහා ඔබගේ සහභාගීත්වය බෙහෙවින් අගයකරමි. මම මේ ප්‍රශ්නාවලිය මගින් රැස් කරනුලබන තොරතුරු අතිශ්‍ය රහසිගත අතර මාගේ ආචාර්ය උපාධි අධ්‍යයනය සඳහා පමණක් භාවිතාකරන බවට ඔබට සහතික වෙමි. සමාගම්හී හෝ මේ සඳහා අදහස් දක්වන අයගේ සැබෑ නම් කිසිදු වර්තාවක හෝ ප්‍රකාශනයක භාවිතා නොකරන අතර සියලු දත්ත සාමූහික ආකාරයට විශ්ලේෂණය කිරීමට නියමිතය.

ඔබට මෙම සමීක්ෂණය ප්‍රශ්නාවලියට සහභාගි විය හැකි නම්, මම එයට බෙහෙවින් ස්තුතිවන්ත වෙමි.

ස්තූතියි

මෙයට විශ්වාසී

වර්තමානයේ දී හෝ අනාගතයේ දී මෙම ව්‍යාපෘතිය ගැන යම් ගැටළුවක් හෝ ප්‍රශ්නයක් ඇතිවුවහොත් පහත ලිපිනයට/අංකයට අමතන්න.

පර්යේෂක:
නිසංසලා විජේකෝන්
ගිණුම්කරණ දෙපාර්තමේන්තුව,
වයිකාටෝ කළමණාකරණ පාසැල,
වයිකාටෝ විශ්වවිද්‍යාලය,
Private Bag 3105, හැමිල්ටන්, නවසීලන්තය
විද්‍යුත් ලිපිනය : hnww1@students.waikato.ac.nz ජංගම දුරකතන අංකයන්: +64 221 955394; Office: +64 7838 4466 (Ext: 6419) ;+ 94 773779926; +94 112969940

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ප්‍රධාන අධීක්ෂක:
මහාචාර්ය ග්‍රන්ට් සම්කින් (Professor Grant Samkin), ගිණුම්කරණ දෙපාර්තමේන්තුව,
වයිකාටෝ කළමණාකරණ පාසැල,වයිකාටෝ විශ්වවිද්‍යාලය, Private Bag 3105, හැමිල්ටන්, නවසීලන්තයවිද්‍යුත් ලිපිනය: grantsam@waikato.ac.nz දුරකතන අංකය (රැකියා): +64 7838 4466 (Ext: 8942)

Appendix M: Participant information sheet for questionnaire survey

Waikato Management School
Te Raupapa

THE UNIVERSITY OF WAIKATO
Te Whare Wānanga o Waikato

Participant Information Sheet – Questionnaire survey

Project Title

Towards the development of a financial reporting framework for Sri Lankan SMEs

This study is a part of my PhD research programme, undertaken at the Department of Accounting, Waikato Management School, University of Waikato. The objective of this research is to develop a financial reporting framework for Sri Lankan SMEs. This study seeks to identify small and medium enterprise users and their information needs as well as gather perceptions from preparers and users of SME financial statements on the SME financial reporting in general and the suitability of the accounting standard *International Financial Reporting Standards for Small and Medium- sized Entities (IFRS for SMEs)* in particular.

The approximate time taken for the questionnaire is 20-30 minutes. Please return the completed questionnaire using the attached postage paid envelop. It is considered that the completion of survey questionnaire will provide your consent for the research. Further, the researcher will assume permission has been given for the data to be used as outlined in the participant information sheet.

Any data/information you provide will be confidential to the researcher and the research supervisors and no identifying information will be used in any subsequent reports or publications. Real names of participants/organizations will not be used in research reports or publications. All questionnaires will be destroyed once the research is completed. The outcome of the research may be presented in academic conferences and published in academic publications.

If you take part in the survey, you have the right not to answer any particular question. Further, you will have the right to access the summary of the findings of the research when it is completed. Finally, you have the right to withdraw the data provided by you within 3 weeks of the data collection.

Thank you.

If you have any questions or concerns about the project, either now or in the future, please feel free to contact either:

Researcher:
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Mobile: +64 221 955394; Office: +64 7838 4466 (Ext: 6419)
Or
Chief supervisor:
Professor Grant Samkin
Department of Accounting
Waikato Management School
University of Waikato
Private Bag 3105, Hamilton, New Zealand
Email Address: grantsam@waikato.ac.nz Office: +64 7838 4466 (Ext: 8942)

Sinhala version of the participant information sheet for questionnaire survey

ව්‍යාපෘති අරමුණ

මෙම අධ්‍යනය Waikato විශ්ව විද්‍යාලයේ Waikato කළමනාකරණ පාසල , ගිණුම්කරණ දෙපාර්තමේන්තුව ආරම්භ කරන ලද මාගේ ආචාර්ය උපාධියේ පර්යේෂණ වැඩසටහනේ කොටසකි.

මෙම පර්යේෂණයේ අරමුණ වන්නේ , ශ්‍රී ලාංකික සුළු හා මධ්‍ය පරිමාණ ව්‍යාපාරිකයන් සඳහා මූල්‍ය වාර්තාකරණ රාමුව සංවර්ධනය කිරිම උදෙසා වේ. මෙම අධ්‍යනය සුළු හා මධ්‍යම ව්‍යාපාර පරිශීලකයන් හඳුනා ගැනිමත්, ඔවුන්ගේ තොරතුරු අවශ්‍යතා මෙන්ම සුළු හා මධ්‍යම ව්‍යාපාර මූල්‍ය වාර්තාකරණය මත සුළු හා මධ්‍ය පරිමාණ මූල්‍ය ප්‍රකාශන පිළියෙළ කරන්නන් හා පරිශීලකයන්ගෙන් රැස්කර ගත් ප්‍රත්‍යක්ෂයන් සහ විශේෂයෙන් ම සුළු හා මධ්‍යම ව්‍යාපාර සඳහා ගිණුම්කරණ සම්මත අන්තර්ජාතික මූලය වාර්තාකරණ ප්‍රමිතින්ගේ යෝග්‍යතාව පිළිබඳ සොයා බලයි.

ප්‍රශ්නාවලිය සඳහා වන කාල වකවානුව දළ වශයෙන් විනාඩි 20-30 වේ. ඔබ මෙම ප්‍රශ්නාවලියට පරිගණකය හරහා දායක වන්නේ නම් , කරුණාකර එහි ඊ- මේල් සම්බන්ධතාව වෙත ගොස් ප්‍රශ්නාවලිය අවසානයේ දී ඇති "submit" බොත්තම ක්ලික් කිරිමෙන් ඔබගේ සම්පූර්ණ කරන ලද ප්‍රශ්නාවලිය ඉදිරිපත් කරන ලෙස ඉල්ලා සිටිමි.ඔබ දෘඪ පිටපතක් ලෙස මෙම ප්‍රශ්නාවලිය ඉදිරිපත් කරන්නේ නම් , සම්පූර්ණ කරන ලද ප්‍රශ්නාවලිය මුද්දර අලවන ලද ලියුම් කවරය භාවිත කරමින් නැවත එවන මෙන් ඉල්ලා සිටිමි. සමික්ෂණ ප්‍රශ්නාවලියේ සම්පූර්ණත්වය මෙම පර්යේෂණය සඳහා කැමැත්ත ලබා දිමක් ලෙස සලකනු ලැබේ. පර්යේෂකයා සහභාගී තොරතුරු පත්‍රය තුළ සංක්ෂේපය ලෙස දත්ත භාවිතා කිරිමට අවසර ලබා දි ඇති බව උපකල්පනය කරනු ලැබේ.

ඔබ සපයන ලද දත්ත තොරතුරු පර්යේෂණ අධීක්ෂණයන්ට රහස්‍ය වනු ඇත. මෙම හඳුනාගත් දත්ත කිසිදු ආයතික වාර්තා හෝ ප්‍රකාශන සඳහා භාවිත කරනු නොලැබේ. සහභාගීවූවන්ගේ/ සංවිධානයන්ගේ සැබෑ නම් පර්යේෂණ වාර්තාවේ හෝ ප්‍රකාශනයන් හී භාවිත නොවනු ඇත. සියලුම ප්‍රශ්නාවලී පර්යේෂණය අවසාන වූ පසු විනාශ වනු ඇත. මෙම පර්යේෂණයේ ප්‍රතිඵලය ශාස්ත්‍රීය සාකච්ජාවන් හී ඉදිරිපත් කරනු ලබන අතර ශාස්ත්‍රීය ප්‍රකාශයන්හී   පළ කරනු ලබයි. ඔබ මෙම සමීක්ෂණයට සහභාගී වන්නේ නම් , ඔබට යම් විශේෂිත ප්‍රශ්නයකට පිළිතුරු නොදී සිටිමට අයිතියක් ඇත. තව ද , මෙම පර්යේෂණය අවසන් වූ විට , ඔබට මෙම පර්යේෂණයේ සාරාංශය **ප්‍රවේශ** විමට අයිතියක් ඇත. අවසාන වශයෙන් , ඔබ සපයන ලද දත්ත සති 03 ක් ඇතුලත ඔබට ඉල්ලා අස්කර ගැනිමේ අයිතිය ඇත.

ස්තූතියි

ඔබට මෙම ව්‍යපෘතිය පිළිබඳ යම් ප්‍රශ්නයක් හෝ අවධාරණය කළ යුතු දෙයක් ඇත්නම් වර්තමානයේ දි හෝ අනාගතයේ දි සම්බන්ධ කර ගත හැකිය.

පර්යේෂක:

නිසංසලා විජේකෝන්
ගිණුම්කරණය දෙපාර්තමේන්තුව
Waikato කළමනාකරණ පාසල; Waikato විශ්ව විද්‍යාලය
Private Bag 3105, හැමිල්ටන්, නවසීලන්තය
විද්යුත් තැපැල් ලිපිනය: hnww1@students.waikato.ac.nz; ජංගම: +64 221 955394, කාර්යාලය: +64 7838 4466 (දිගුව: 6419)

නැතහොත්

ප්‍රධාන අධීක්ෂක:
මහාචාර්ය ගාන්ට් සැම්කින්
ගිණුම්කරණය දෙපාර්තමේන්තුව
Waikato කළමනාකරණ පාසල; Waikato විශ්ව විද්‍යාලය; Private Bag 3105, හැමිල්ටන්, නවසීලන්තය
විද්යුත් තැපැල් ලිපිනය: grantsam@waikato.ac.nz ; කාර්යාලය: +64 7838 4466 (දිගුව: 8942)

Appendix N: Non-response test 1 - Number of employees

Case Processing Summary

	Cases					
	Valid		Missing		Total	
	N	%	N	%	N	%
first mailing * Number of employees	231	100.0%	0	0.0%	231	100.0 %

first mailing * Number of employees Crosstabulation

			Number of employees			Total
			5 - 15	16 - 39	40-99	
first mailing	yes	Count	51	36	18	105
		Expected Count	50.5	35.5	19.1	105.0
	No	Count	60	42	24	126
		Expected Count	60.5	42.5	22.9	126.0
Total		Count	111	78	42	231
		Expected Count	111.0	78.0	42.0	231.0

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)
Pearson Chi-Square	.140[a]	2	.932
Likelihood Ratio	.141	2	.932
Linear-by-Linear Association	.081	1	.776
N of Valid Cases	231		

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	.025	.932
	Cramer's V	.025	.932
N of Valid Cases		231	

Non-response test 02 – Number of years been trading

			Q5 . No. of years has the organisation been trading			
			Less than 1 year	1-3 years	4-6 years	7-10 years
first mailing	yes	Count	5	20	25	18
		Expected Count	4.5	19.9	27.6	14.0
	No	Count	5	24	36	13
		Expected Count	5.5	24.1	33.4	17.0
Total		Count	10	44	61	31
		Expected Count	10.0	44.0	61.0	31.0

first mailing * Q5 . No. of years has the organisation been trading Crosstabulation

			Q5 . No. of years has the organisation been trading	
			More than 10 years	Total
first mailing	yes	Count	36	104
		Expected Count	38.0	104.0
	No	Count	48	126
		Expected Count	46.0	126.0
Total		Count	84	230
		Expected Count	84.0	230.0

Chi-Square Tests

	Value	df	Asymptotic Significance (2-sided)
Pearson Chi-Square	2.789[a]	4	.594
Likelihood Ratio	2.781	4	.595
Linear-by-Linear Association	.012	1	.914
N of Valid Cases	230		

Symmetric Measures

		Value	Approximate Significance
Nominal by Nominal	Phi	.110	.594
	Cramer's V	.110	.594
N of Valid Cases		230	

Appendix O: Ethical approval letter

Research Office	Amanda Sircombe
Waikato Management School	Research Manager
The University of Waikato	Phone +64 7 838 4376
Private Bag 3105	Fax +64 7 838 4063

THE UNIVERSITY OF WAIKATO
Te Whare Wānanga o Waikato

MANAGEMENT SCHOOL
Te Raupapa

11th August 2015

Himali Wijekoon Mudiyanselage
1/37 Aurora Terrace
Hillcrest
Hamilton

Dear Himali

Ethical Application WMS 15/93

Towards the development of a financial reporting framework for Sri Lankan SMEs

As per my earlier email the above research project has been granted Ethical Approval for Research by the Waikato Management School Ethics Committee.

Please note: should you make changes to the project outlined in the approved ethics application, you may need to reapply for ethics approval.

Best wishes for your research.

Regards,

Amanda Sircombe

Amanda Sircombe

Research Manager

Appendix P: Financial reporting format for Tier 4 SMEs in the proposed financial reporting framework

Name of the entity
Statement of profit or loss for the year ended 31 March 20XX

	Rs.	Rs.
Gross income from Sales and /or services		**x**
Costs of goods sold		
Opening stock (include work in progress)	x	
Purchases	x	
Closing stock (include work in progress)	(x)	(x)
Gross profit/(Loss)		**x**
Other income		
Interest received	x	
Dividends received	x	
Rental income	x	x
Total income		**x**
Expenses		
Bad debts	x	
Tax depreciation	x	
Insurance	x	
Interest expenses	x	
Professional and consulting fees	x	
Rental expenses	x	
Repairs and maintenance	x	
Remunerations paid to owner and/or director's fee and management fees	x	
Salaries and wages paid to employees	x	
Other expenses	x	x
Net profit /loss before tax		**x**
Tax adjustments		(x)
Current year taxable profit/loss		**x**

Name of the entity
Statement of Assets and Liabilities as at 31 March 20XX

Assets	**Rs.**	**Rs.**
Non-current assets		
Vehicles	x	
Plant and machinery	x	
Furniture and fittings	x	
Land	x	
Buildings	x	x
Other fixed assets		x
Bank deposits - Long term		x
Current assets		
Inventories	x	
Accounts receivable (debtors)	x	
Cash and deposits	x	x
Total assets		**x**
Equity and Liabilities		
Owners' equity		x
Non-current liabilities		
Bank loans - long term		x
Current liabilities		
Bank loans - short term	x	
Accounts payable (creditors)	x	x
Total liabilities		x
Equity and liabilities		**x**